T.C.

TURKISH-GERMAN UNIVERSITY

INSTITUTE OF SOCIAL SCIENCES

BUSINESS MANAGEMENT DEPARTMENT

FINANCIAL HEALTH OF NPOS: A STUDY ON NONPROFIT FINANCIAL WELLBEING AND ACCOUNTING PROCESSES

MASTER'S THESIS

Ardıl Yılmaz KAYA

ADVISOR

Prof. Dr. Ahmet Göksel YÜCEL

ISTANBUL, July 2022

T.C.

TURKISH-GERMAN UNIVERSITY

INSTITUTE OF SOCIAL SCIENCES

BUSINESS MANAGEMENT DEPARTMENT

FINANCIAL HEALTH OF NPOS: A STUDY ON NONPROFIT FINANCIAL WELLBEING AND ACCOUNTING PROCESSES

MASTER'S THESIS

Ardıl Yılmaz KAYA

(198107004)

ADVISOR

Prof. Dr. Ahmet Göksel YÜCEL

ISTANBUL, July 2022

T.C.

TURKISH-GERMAN UNIVERSITY

INSTITUTE OF SOCIAL SCIENCES

BUSINESS MANAGEMENT DEPARTMENT

FINANCIAL HEALTH OF NPOS: A STUDY ON NONPROFIT FINANCIAL WELLBEING AND ACCOUNTING PROCESSES

MASTER'S THESIS

Ardıl Yılmaz KAYA

(198107004)

Thesis Submission Date to Institute: 1.08.2022

Thesis Defense Date : 29.07.2022

Thesis Advisor : Prof. Dr. Ahmet Göksel YÜCEL

Other Jury Members : Prof. Dr. Burcu ADİLOĞLU

Asst. Prof. Dr. Çiydem ÇATAK

ISTANBUL, July 2022

TABLE OF CONTENTS

ÖZET

KAR AMACI GÜTMEYEN KURUMLARIN FİNANSAL SAĞLIĞI: KAR AMAÇSIZ FİNANSAL REFAH VE MUHASEBE SÜREÇLERİ ÜZERİNE BİR ARAŞTIRMA

Bu tez, kar amacı gütmeyen kurumların finansal sağlığını kantitatif ve kalitatif olmak üzere iki boyutta ele almaktadır. Bu bütüncül yaklaşımı desteklemek için kar amaçsız finansal sağlık ile insan sağlığı arasında analojiler oluşturulmaktadır. Tezin ana içeriğinden önce kavramlar açıklığa kavuşturulmakta, yasal çerçeve ve muhasebe standartları tartışılmakta, daha sonra literatüre dayalı olarak kar amaçlı ve kar amacı gütmeyen muhasebe uygulamaları arasındaki farklar ortaya konmaktadır. Bu farklılıklar, kar amacı gütmeyen kuruluşlara rehberlik etmek açısından uluslararası kabul görmüş finansal raporlama standartlarına ihtiyaç duyulduğu yönündeki argümanları desteklemektedir.

Finansal sağlığın ölçülmesi büyük ölçüde muhasebe süreçlerinden elde edilen verilere bağlı olduğundan, kuruluşların finansal raporlamada karşılaştıkları zorlukları belirlemek bu tezin amaçları arasındadır. Bu bağlamda incelenen tüm konular ya sektöre özgüdür ya da kar amacı gütmeyen sektörde önemli ölçüde daha yaygındır.

Kantitatif araştırma kapsamında ise Türkiye merkezli üyesi olunan kuruluşların finansal sağlıkları oran analizi temelinde değerlendirilmektedir. Üyesi olunan kurumlarının genel finansal performansını ölçmek için tipik bir endüstri oranı analizi yapılmıştır. Oran analizine ek olarak, literatür taramasında diğer ölçüm yöntemleri de gösterilmiştir. Kâr amacı gütmeyen kuruluşların finansal sağlığını ölçmenin en iyi yönteminin hangisi olduğu konusunda genel bir uzlaşı yoktur.

Anahtar Kelimeler: Finansal Sağlık, Kar Amacı Gütmeyen Kurum, Muhasebe, Raporlama, Malî Analiz

ABSTRACT

FINANCIAL HEALTH OF NPOS: A STUDY ON NONPROFIT FINANCIAL WELLBEING AND ACCOUNTING PROCESSES

This thesis addresses the financial health of non-profit institutions in two dimensions: quantitative and qualitative. Analogies between nonprofit financial health and human health are drawn in order to justify this holistic approach. Before the main content of the thesis, the concepts are clarified, the legal framework and accounting standards are discussed, and then, based on the literature, the differences between nonprofit and for-profit accounting practices are revealed. These differences support the arguments that there is a need for internationally accepted financial reporting standards to guide nonprofits.

Since measuring financial health is highly dependent on the data obtained from accounting processes, identifying the challenges organizations face in financial reporting are among the objectives of this thesis. All issues examined in this regard are either sector-specific or significantly more common in the non-profit sector.

And within the scope of the quantitative research, financial health of Turkey-based membership organizations is evaluated on the basis of ratio analysis. A typical industry ratio analysis is conducted to measure the aggregate financial performance of membership institutions. In addition to ratio analysis, other measurement methods are also shown in the review of literature. There is no general agreement over the best method of measuring financial health of nonprofits.

Keywords: Financial Health, Nonprofit Organization, Accounting, Reporting, Financial Analysis

LIST OF ABBREVIATIONS

ACFE **:** Association of Certified Fraud Examiners

AICPA : American Institute of Certified Public Accountants

CIPFA **:** Chartered Institute of Public Finance and Accountancy

CSO **:** Civil Society Organization

EPSAS **:** European Public Sector Accounting Standards

FASB **:** Financial Accounting Standards Board

FP **:** For-Profit

GAAP **:** Generally Accepted Accounting Principles

GIK **:** Gift-in-Kind

IAS **:** International Accounting Standards

IASB **:** International Accounting Standards Board

ICNPO : International Classification of Non-Profit Organizations

IFR4NPO : International Financial Reporting for Nonprofit Organizations

IFRS **:** International Financial Reporting Standards

IPSAS **:** International Public Sector Accounting Standards

IRS **:** Internal Revenue Service

ISIC : International Standard Industrial Classification of all Economic Activities

JHCNSP : Johns Hopkins Comparative Nonprofit Sector Project

NEA : National Endowment for the Arts

NFP : Not-For-Profit

NGO **:** Non-Governmental Organization

NPO **:** Nonprofit Organization

NPQ **:** Nonprofit Quarterly

NVSQ **:** Nonprofit and Voluntary Sector Quarterly

SORP : (Charity) Statement of Recommended Practice

TCMB **:** The Central Bank of the Republic of Turkey

TFRS **:** Turkish Financial Reporting Standards

TL **:** Turkish Lira

TMS **:** Türkiye Muhasebe Standartları

TÜİK **:** Turkish Statistical Institute

UN **:** United Nations

USCC : United States Chamber of Commerce

VUK : Vergi Usul Kanunu (Tax Procedure Law)

WHO **:** World Health Organization

LIST OF FIGURES

LIST OF TABLES

CHAPTER 1: INTRODUCTION

In today's political and economic environment, there is a constantly increasing necessity for effective financial management in all types of organizations. The primary objectives of corporate financial management are achieved through the maximization of profit or wealth (Pandey, 2017, p. 5). Wealth relies mostly on profit, and profitability usually means growth (Enke, 1970). And according to the renowned economist Milton, generating a healthy profit is the only purpose and responsibility of a business (Friedman, 1970). Profit is the lifeblood of a firm (Smart, 1992).

Not every organization's primary goal is creating an economic surplus. Some prioritize social outcomes, not material gains. Public sector, also known as the state sector, and the so-called nonprofit sector serve public interest unlike the for-profit sector which focuses solely on material interests.

Different types of organizations have different objectives, and there is a variety of measures of success. In for-profit corporations, financial metrics alone are traditionally sufficient to provide ready-made measures of success. This approach was upheld by Katz and Kahn (Yuchtman & Seashore, 1967). In most of the organizations in the nonprofit sector, however, assessing success can be more complex and several different factors are taken into account: Impact, strategy, financial health and stability, reputation, internal DEI (Diversity, equity and inclusion) etc.

Even though nonprofits are value-driven organizations, they still need effective and efficient financial management for their existence, functionality and accountability. It is a key function for an institute to build trust and increase operational capacity. Since the last decades, finance has been getting more significance as an integral part of strategic management (Pedro M. Kono & Barry Barnes, 2010).

Nonprofit is an umbrella term that represents a wide range. The organizations and their structures vary according to their status, field of activity, size and location. Therefore, how they raise money and the way they use it differ from institution to institution. For instance, membership organizations' main source of funding is the so-called membership fee while aid agencies mostly depend on donations. Some other examples generate income through commercial activities or investments. Besides these, other methods of raising funds include government-support, sponsorship, awards, cooperation and so on.

Regardless of status, category or anything else, every entity desires to stay financially healthy. It's crucial for nonprofits since they face a growing pressure by stakeholders to measure success and inform the public for accountability. Apart from public accountability, NPOs are also pressured by the funders and their own members. In order to enable and keep the flow of donations or recruit new members, the institutions must have a good reputation which is possible with effective financial management.

This study reviews the term "financial health" as a two-dimensional concept, utilizes a holistic approach to analyze the financial health of nonprofits. Accordingly, quality as well as the quantity indicators are taken into account to examine the institutions' monetary affairs and stability. Both qualitative and quantitative research methods are conducted in the hope of drawing the best possible conclusions.

The thesis consists of six chapters. Each chapter -except the introduction and conclusion parts- was intended to form an article answering different research questions and showing distinct aspects of financial wellbeing of nonprofit organizations. All articles which are directed cover the topic in different scopes are based on the same fundamental literature.

Research objectives are as follows:

- Identifying the major issues and challenges in nonprofit financial management.
- Testing whether nonprofit financial practices are different from the corporate financial practices.
- Measuring the financial performance of the nonprofit organizations.

Goals and research questions are parallel to the objectives of this thesis.

The second chapter is divided into three sections. In the first section, the concepts are defined in detail. Financial health is explained and the comparison between pro-profit and nonprofit drawn further. Different types of NPOs are listed in respect of the international classification. Their legal status and obligations are documented in the second section. This part documentates the principles, rules and regulations regarding the nonprofit financial management processes; in short, the standards entities need to comply with. The third part of Chapter 2 contains the review of existing literature and theoretical framework. Research questions are developed on the basis of primary literature. Next chapters address the research questions which are parallel to the objectives posed above.

Chapter 3 identifies the shortcomings in nonprofit financial management. Based on the literature, the issues nonprofits face in accounting and reporting are highlighted. These issues are either sector-specific or more common in the third sector compared to the pro-profit sector. Mini cases as well as the comments from experts demonstrate practical evidence regarding the challenges.

In chapter 4, a financial analysis was conducted to test the monetary strength of Turkey's third sector. Ratio analysis was used to assess the liquidity, solvency and profitability of Turkey-based membership associations.

The thesis comes to a close in Chapter 5, Final Conclusion. This part briefly summarizes the key findings interpreted in the previous sections, and draws analogy between nonprofit financial health and human health.

CHAPTER 2: DEFINITIONS, LITERATURE AND LEGISLATIVE FRAMEWORK

2.1.DEFINITIONS

Before doing the literature review and documenting the legislative framework, there is a need to clarify the keywords of this dissertation, elements of pro-profit and nonprofit measurement and terminology used in the articles.

Defining the Sector and Organizations

Nonprofit Organizations: Non-corporate entities which are intended to create social impact.

Various definitions of NPOs can be found in literature. The Handbook on Non-Profit Institutions in the System of National Accounts (United Nations, 2003, p. 17) published by the UN in collaboration with the Johns Hopkins Center for Civil Society Studies define the non-profit sector with these five keywords: Sector that includes (1) Organizations that are (2) NFP and not-profit-distributing, (3) institutionally separate from government, (4) self-governing and (5) non-compulsory.

Nonprofits are classified by different standards like ICNPO, ISIC, NAICS etc. The Handbook specially endorses the International Classification of Non-Profit Organizations (ICNPO) which was developed (Salamon & Anheier, 1992) and later revised (Salamon & Anheir, 1996) by a group of academics from Johns Hopkins Institute for Policy Studies for their Johns Hopkins Comparative Nonprofit Sector Project (JHCNSP).

ICNPO classified the NPIs under 12 categories, and each category -except the last one, Group 12- branches into subcategories. Table 1.1 accessed through the book *Global Civil Society: Dimensions of the Nonprofit Sector* (Toepler et al., 1999, p. 7) which was collaboratively written by several academics, lists the main fields of nonprofit activities. It was originally adopted from the JHCNSP. Table 1.2 shows the list of major nonprofit activity groups which are divided into 30 subgroups according to the Handbook (UN, 2003, p.30).

Table 2.1

Nonprofit activity fields covered by the second phase of the JHCNSP

1. Culture	7. Civic and advocacy
2. Creation	8. Philanthropy
3. Health	9. International
4. Social Services	10. Religious congregations
5. Environment	11. Business and professional, unions
6. Development	12. Other

Table 2.2

ICNPO: Main Groups

1. Culture and recreation	7. Law, advocacy and politics
2. Education and research	8. Philanthropic intermediaries and voluntarism promotion
3. Health	9. International
4. Social Services	10. Religious congregations
5. Environment	11. Business and professional associations and, unions
6. Development and housing	12. Not elsewhere classified

Each group listed in Table 1.2 -except the last one- has subgroups with codes. For instance, 1. Culture and recreation contains 1 100 Culture and arts, 1 200 Sports and 1 300 Other recreation and social clubs.

According to both tables, the umbrella term “nonprofit” covers such a large spectrum of organizations that includes charities, hometown societies, labor unions, fan-owned football clubs, even leading business associations like TÜSİAD or the United

States Chamber of Commerce (USCC).

Not-for-Profit Organization: a synonym of NPO, according to the book "A Dictionary of Nonprofit Terms and Concepts" (Smith et al., 2006, p. 161). These terms are used generally interchangeably whereas NPO is used more frequently. On the other hand, these two terms are not always perceived as the same. In an article written in 1987, the distinction is explained as such:

Nonprofit organization, from the accounting perspective, refers to an organization whose revenue equals expenses. Not-for-profit organizations are entities with missions other than generating income (Perry, 1987, p. 37).

Although NFPO and NPO do substitute each other in most of the academic literature, they can be conceptualized differently from a legal perspective. This inference is based on the IRS (Internal Revenue Service) codes and their definition of the organizational status in terms of requirements for tax exemption. The distinction is discussed with the justification in the Legislative Framework.

Membership Organization: Legal organization that consists of members with common interest. These institutions typically depend on their own members and are usually member-serving. However, they can be public-serving at the same time.

In Chapter 5, a comprehensive financial analysis conducted on the consolidated sectoral balance sheet of Turkey-based membership organizations. The data was acquired from Türkiye Cumhuriyet Merkez Bankası, TCMB (en: The Turkish Republic Central Bank).

Charity: Nonprofit organization that provides aid, raises bulk of the fund through donations and grants.

Charities, or charitable organizations, have special status in most of the countries. A nonprofit needs to fulfil some specific criterias in order to get recognized as a charity and gain tax-exempt status. This topic is further discussed in the Legislative Framework.

Foundation: Legal entity that carries out charitable activities.

This definition is relatively short since there is no worldwide accepted definition of the term “foundation”. Likewise, their legal status differs from country to country. Unlike the charities, foundations are generally founded by wealthy families, companies, or institutions like universities. They tend to receive most, if not all, endowment from single sources which are either founders or sponsors.

Non-Governmental Organizations: Voluntary organizations which are generally non-profit and not associated with any government (*Nongovernmental Organization | Britannica*, n.d.). They vary in size and can operate on local, regional, national, international or global level.

Non-governmental organizations are significant actors in today’s political and economic environment. International Federation of Red Cross and Red Crescent Societies, Greenpeace, Oxfam International, Amnesty International and Human Rights Watch are among the world’s most influential NGOs.

Civil Society Organization (CSO) is a widely-used synonym of Non-Governmental Organization (NGO).

For-Profit Organization: Organization designed to generate income for the shareholders and maximize the wealth of owners. Synonyms of FPO are profit making organization and for-profit corporation.

Non-Financial Measurement and Indicators

In respect of the fact that nonprofit institutions are mission-oriented and value-driven organizations, financial management is just a tool that facilitates the goal attainment. It doesn’t come first as long as an NP doesn’t consider the transition to FP. Success is more than being financially healthy. Scholars working on this subject documented the necessity of success measurement in non-business entities in detail. Now, the question must be what to measure. What are the indicators?

The indicators of success are inputs, outputs, impact, throughputs and outcomes. All these markers were adopted from the private business world but proven to be applicable by charities, and eventually became standards in the nonprofit and voluntary sector.

Impact: "a powerful effect that something, especially something new, has on someone or something; 2) a resource such as materials or labour that is involved in producing something and has a cost that affects profits"

Input: "help, ideas, or knowledge that someone gives to a project, organization, etc."

Outcome: "a result or effect of an action, situation, etc."

Output: "the amount of goods and services, or waste products, that are produced by a particular economy, industry, company, or worker"

Throughputs: the amount of work done; or people, materials, etc. that are dealt with in a particular amount of time.

The definitions above are from the online dictionary of Cambridge (Accessed in March 2022). Apart from their vocabulary meanings, their contextual meanings in this thesis are as follows:

Inputs: Everything the organization needs in order to achieve a mission or conduct a specific work. For instance: Organizational staff, donations, materials.

Outputs: The amount an organization's work staged. For example: The quantity of aid a charity delivered.

The ratio between inputs and outputs refers to efficiency.

Throughputs: Measure of all activities of the organization, the charity's capacity. For instance: How accurately the charity works in case of a disaster (short-term, tactical).

Outcomes: The degree of an organization's mission-achievements, can be both short-term and long-term. For instance: Voluntary satisfaction.

Impact: All affects as a result of the organization's activities, regardless of purpose. Impacts can be negative or positive. For instance: The charity's harm on the political atmosphere, or an association's indirect and unintended assistance to the poor.

To what degree a charity achieves its missions, refers to its effectiveness.

Financial Measurement and Indicators

Financial Performance: "The act of performing financial activity. In a broader sense, financial performance refers to the degree to which financial objectives are being or has been accomplished." (Ravinder & Anitha, 2013)

Financial Health: Financial wellbeing; being financially stable, operational, and free of distress

This definition of financial health is derived from the definition of Health by the World Health Organization (WHO).

Financial Distress: Organization's suffering from an unwelcome economic situation or inadequate financial practices.

The term *Financial Distress* stands at the center of the thesis. Because, just like human health is defined as the absence of illness, disease or sickness; financial health is the absence of malfunction in financial management and enjoying favorable economic conditions.

Integrity, Transparency and Accountability

The UN underlined the integrity, transparency and accountability as key concepts of public administration.[1] These three terms improve the performance and build the public trust. Elia Armstrong (2005) from the UN Ethics Office argues that integrity, transparency and accountability are the fundamental principles for the service to the public. Similarly, non-governmental governance depends on these three values.

[1] UNITED NATIONS CONVENTION AGAINST CORRUPTION, UNITED NATIONS OFFICE ON DRUGS AND CRIME Vienna, 2004, Page 7, Article 1

Organizational Integrity: Described by Ken Jowitt as "an organization's practical (not simply rhetorical) ability to sustain a specific competence by identifying socio-political tasks and enforcing strategies that subordinate particular member to general organizational interests" (Jowitt, 1983).

Transparency: Accessibility of information regarding the structure of an entity and the operations conducted inside or outside the organization.

Financial Transparency: "The ease with which donors, beneficiaries, and the general public can evaluate how efficient an organization is operating" (Lee & Joseph, 2013). Practically, how much financial information disclosed by the entity refers to the degree of financial transparency

Transparency and accountability are highly interconnected. According to Ebrahim (2010), transparency is one of the core components of nonprofit accountability.

Accountability: An entity's ability to take responsibility for their situation and actions. It can also be defined as a charity's/association's capacity to answer when they are questioned or judged.

The term accountability has no globally accepted definition (Schatteman, 2013). Different kinds of accountability exist; such as performance accountability, financial accountability etc. And accountability can occur in disparate directions: Horizontal, vertical, upward and downward.

Apart from the members, administrative and voluntary staff and employees, nonprofits have a wide range of stakeholders; from an ordinary citizen to the state. Schatteman (2013) points out that this sector delivers most of the social services on behalf of the state in both Germany and the United States, two major developed countries. The organizations' accountability towards the state/government are based on the audit and tax requirement. This topic is documented broadly in the section of Legislative Framework. As for the accountability towards the donors, members and sponsors; they are the sustainers of an NPO.

Considering that donors increasingly demand transparency, accountability and concrete evidence for the achievements (Beamon, 2004; Schatteman, 2013; Eftekhar et al., 2017); disclosure of the financial information and being financially healthy are significant aspects of nonprofit accountability.

2.2.LEGISLATIVE FRAMEWORK

Before starting the major content, it's essential to describe the legislative framework relevant to nonprofit financial management. In the context of NP financial management, the legislative framework includes the organizational identity (NPO or NFPO), tax-exempt status, local and international standards, requirements, and to whom the organizations are accountable.

The legislative framework here begins with the existing financial reporting standards which alone don't have legislation on any type of organization unless mandated by governments. Financial Reporting Standards, the first part of this subsection is aimed to justify the role of regulations and to underline the need of globally accepted accounting standards specific to the third sector.

2.2.1. Financial Reporting Standards

To begin with the accounting standards, there is no globally accepted common set of accounting rules and principles to meet the needs of the nonprofit sector. International Financial Reporting Standards (IFRS) which was issued by the International Accounting Standards Board (IASB) prioritizes providing guidance for the for-profit business. International Public Sector Accounting Standards (IPSAS) issued by the IPSAS Board for the use of governmental bodies. Although IPSAS is public oriented thus not-for-profit by nature, it's still inadequate for the use of non-business private entities. For instance, nonprofit organizations largely rely on non-exchange transactions such as grants, donations, in-kind gifts and services etc. Accounting of these receiving and giving acts must be done precisely and in an order. In 2017, IPSAS released a Consultation Paper (CP), *Accounting for Revenue and Non-exchange Expenses* to fill a gap in the literature and profession. However, it was developed to address the issues in public accounting practices such as taxes and transfers. Comments from Ian Carruthers, IPSAS Board Chair are explaining:

"This Consultation Paper is an important first step in addressing some key IPSAS implementation issues while seeking to maintain IFRS convergence,"

"It also provides an opportunity to address gaps in literature that have been identified in accounting for non-exchange expenses and the measurement of non-contractual receivables and non-contractual payables—such as taxes, fines and licenses."[2]

As a result, both IFRS and IPSAS are not adequate for the guidance of non-profit financial reporting. This conclusion is shared by the study of Cordery et. al. (2019) who highlight the views of NPO employees. Furthermore, international cooperation and the need for comparability result in the necessity of the internationally applicable accounting standards specific to the nonprofit sector.

Currently, some initiatives like IFR4NPO (International Financial Reporting for Nonprofit Organizations) seek to develop guidance on financial reporting for the nonprofit sector. This initiative is led by Humentum and CIPFA, the Chartered Institute of Public Finance and Accountancy based in the UK. In 2015, 162 organizations across the world including those who operate globally, such as Save the Children International and Compassion International, declared their support for the campaign (Boyes-Watson, 2019). Other than the increasing endorsements, this project is sponsored by Open Society Foundations, Ford Foundation and Oak Foundation. IFR4NPO was launched in July 2019, their Consultation Paper published in January 2021, and the initiative set 2025 as the due date to complete the IFR4NPO Guidance (Musoke, 2020).

All these disharmony and the gaps in the standardization in context of guidance indicate the role of local accounting frameworks which are defined mainly by the legal systems and other local authorities of the accounting profession. Regulations and jurisdiction comes out to be more relevant since they determine the status of entities, set the rules, and have decisive roles.

[2] https://www.ipsasb.org/news-events/2017-08/ipsasb-seeks-views-updating-accounting-approaches-revenue-and-new-approaches-non-exchange-expenses

2.2.2. The Role of Legislation

Apart from their inadequacy for nonprofit financial reporting, existing standards such as IFRS and IPSAS do not pose legislative authority despite having been mandated by jurisdictions. Plus, the implementation of these two standards didn’t remove the barriers to harmonization of financial reporting practices. In the EU, for example, the countries are coming closer in nearly every aspect. The cooperation is tightening, cross-border activities are increasing in every level and non-business entities -just like the corporations- establish HQs in multiple countries. In contrast with the convergence, there is a disharmony between member states in this specific context and it’s significant. Researchers suggest that the usability of financial statements can be negatively affected by the union’s diversity in terms of local regulations (Lopez-Arceiz et al., 2021, p. 45)**.**

Although local regulations may lead to such problems as mentioned above, they are key elements of the nonprofit accounting framework. The role of the regulatory system in this context comprehends the classification of organizations by legal forms, providing guidance, public supervision, taxation, and national legislation on the nonprofits.

Entities that have different institutional purposes and related aspects, are categorized by law. Two most common forms of NPOs (at least in Turkey and in the EU) are association and foundations. They perform divergent kinds of activities. Their structures as well as the governance aspects differ accordingly.

Hereinbefore, NPOs and NFPOs may carry different legal status in respect of the codes under which they operate. The distinction based on the Internal Revenue Code (Kenton, 2022) is explained on Investopedia as such:

“The sections of the IRS's 501(c) code that governs each of NPOs and NFPOs serve to further delineate their differences. Nonprofits operate under 501(c)(3), for corporations, funds or foundations that operate for religious, charitable, scientific, literary or educational purposes. NFPOs, by contrast, primarily do so under other sections, such as 501(c)(7), for recreational organizations. One classic example of an NFPO, then, is a sports club that's jointly owned by its members and sustained simply for their enjoyment.”

On the website of USCC as well, the distinction between NPO and NFPO is explained on the basis of IRC (Heaslip, 2020):

“Nonprofits are granted 501(c)(3) status by the IRS. NFPOs are also governed by IRS tax code section 501(c), but depending on their purpose they could fall under a different section, like section 501(c)(7).”

It’s noteworthy that these interpretations of Internal Revenue Code are not necessarily applicable to other tax codes and the acronym NPO may stand for “not-for-profit” in some academic papers[3]. Consequently, a disharmony between legal and academic interpretations of these terms is identified.

Tax policy and charitable deduction are one of the most relevant topics regarding the financial management of the nonprofits. Charities or philanthropic organizations are generally tax-exempt while foundations are rarely granted this status. Different ratios are applied in tax deduction and non-monetary philanthropic givings (in-kind contributions or gifts-in-kind) are also usually tax-deductible. Hence, they are not to be omitted in bookkeeping.

As for local standards it’s understood TMS (Turkish Accounting Standards, a direct translation of IFRS) in Turkey, GAAP in the US and IFRS in the EU. This section puts Turkey’s local regulations on focus while international standards are also briefly documented in an attempt to draw a comparison.

2.2.3. Financial Reporting Requirements

Under the term *Financial Reporting Requirements* shall be understood the regulations and accounting standards. In this subsection, it’s aimed to highlight the financial reporting frameworks in the US, UK and the continental Europe.

In the United States, non-profit institutions are organized under state law. At federal level, they must comply with the tax regulations issued by the Internal Revenue Service (IRS), follow the Generally Accepted Accounting Principles (GAAP) and care about Sarbanes-Oxley (SOX). IRS specifies the prerequisites for tax-exemption, issues Form 990 to receive information about the organizations’ eligibility to retain their tax-exempt status. GAAP, the US-based equivalent of IFRS, provides guidance on accounting, creates transparency, and helps the government in monitoring an entity’s

[3] “Financial reporting is an important aspect of not-for-profit organisations’ (NPOs’) accountability”

eligibility to stay tax-exempt. In comparison with the IFRS, GAAP is more rules-based and contains sector-specific guidance (US SEC, 2011, p.9). There are rules specific to the nonprofit sector as well (Paljug, 2020): (1) *Labelling net assets* as unrestricted or restricted; (2) *Describing cash flow* by providing quantitative data and showing limitations; and (3) Reporting the *Investing* income net of related external and internal expenses. As for SOX, it is largely recommended to be taken into account since it has redefined the favorable practices in governance for every kind of entity[4]. Apart from these, organizations that operate in some specific fields need to follow certain guidelines to receive federal support. For instance, the National Endowment for the Arts (NEA), a federal agency, provides financial assistance to applicant organizations that meet the conditions they lay down. In 2008, NEA published the *Financial Management Guide for Non-Profit Organizations* for this purpose. Audit is another important aspect of management. Nonprofit audit requirements differ from state to state[5].

In the United Kingdom, charities legally differ from other types of NPOs. They are obligated to prepare their financial statements in accordance with the UK GAAP, while other NPOs can choose either IFRS or UK GAAP to follow. UK GAAP, unlike the US GAAP which imposes the accrual basis, allows the charities with a gross annual income of £250,000 or less to apply cash basis. Charities that have more than £250,000 gross income are required to use accrual accounting. The accrual accounts must be filed in compliance with the Charity Statement of Recommended Practice (SORP). Independent examination or audit requirements also vary based on the gross income. With some exceptions, charities which have less than £25,000 annual gross income are not required to have their account audited or independently examined[6]. Charities are registered and regulated by The Charity Commission in England and Wales, Office of the Scottish Charity Regulator in Scotland, and Charity Commission for Northern Ireland

[4] SARBANES-OXLEY: WHAT IT MEANS TO NONPROFITS by Marcus S. Owens
URL: https://mn.gov/mnddc/council/rfp-grants/SARBANES-OXLEY.pdf

[5] Source: National Council of Nonprofits, Accessed on 23.04.2022
URL: https://www.councilofnonprofits.org/nonprofit-audit-guide/state-law-audit-requirements

[6] Charity reporting and accounting: the essentials November 2016 (CC15d)
URL: https://www.gov.uk/government/publications/charity-reporting-and-accounting-the-essentials-november-2016-cc15d/charity-reporting-and-accounting-the-essentials-november-2016-cc15d--2

in Northern Ireland. These non-ministerial government departments run the register of charities and provide information about them, including their fiscal data.

In the continental Europe, where the legal system is also continental based on Roman civil law, nonprofits are most frequently defined by civil codes (Lopez-Arceiz et al., 2021, p. 52). They are therefore regulated mostly under civil law, followed by commercial laws and fiscal legislation. European countries have adopted the IFRS for financial reporting and European Public Sector Accounting Standards (EPSAS) in intention to unify the public sector. EPSAS the European equivalent of IPSAS is accrue-based while both cash- and accrue-bases are allowed within the IFRS. As previously stated, their applicability in nonprofit financial management is questioned. Implementation of both standards results in complexity and dual institutionality. Local legislations which carry different characteristics across the countries are addressed to fill the gaps in these standards. Since the basic elements of accounting frameworks -such as the regulation, profession of accounting, conceptual framework and financial reporting and accounting criteria (recognition and assessment)- differ significantly, disharmony occurs in many aspects of financial management.

2.2.4. Local Accounting Requirements for the NPOs in Turkey

In Turkey, the most common legal forms of NPO are foundations and associations. Both of them are primarily defined by Turkish Civil Code and the law distinguishes between these two types of institutions. Associations are member-based and require at least 7 persons to be founded. On the other hand, foundations are asset-based, requiring a certain amount of capital to be started. Foundations which were established before the adoption of Swiss Civil Code in October 1926 are categorized as *eski vakıf* (en: old foundation) and the rest are under the category of *yeni vakıf* (en: new foundation). A Large majority of the foundations are privately run while some of those old foundations are governed by the General Directorate of Foundations, a governmental institution.

Tax-advantages are rarely granted to nonprofits in Turkey. Of the 5479 (as of 11.08.2021) new foundations, only 301 enjoy tax-exemption. And only 361 among 122,119 associations have this status. The principle of "public benefit" is decisive for an association to be exempt from tax. The status of a public benefit association requires the fulfillment of certain procedures and approval from the presidency[7]. Foundations that desire to gain this status must follow a similar process: They need approval from the Presidency or Ministry of Treasury and Finance after being organizationally and financially eligible. Donations from individuals or corporations are tax-deductible if the organization is tax-exempt or formed by the state.

Institutions that are involved in business activities (directly or through subsidiaries) are considered as merchants, and stand within a wider scope of tax regulations. According to Turkish Commercial Law, associations working for the public interest and foundations that spend more than half of their income on public works are not considered to be merchants themselves, no matter if they run a commercial enterprise directly or through a legal entity that is managed and operated in accordance with the provisions of public law[8].

Ordinary associations keep books on the basis of single entry bookkeeping. Every revenue and expense of the association are clearly and regularly recorded in this book. However, associations with the status of public benefit, including their branches, and associations whose annual gross income exceeds ₺500,000[9], keep their books on the basis of double-entry accounting starting from the following accounting period. In addition to the ledger of accounts, they are obliged to use a general journal daybook and general ledger. Associations that keep books on the double-entry accounting basis should prepare the balance sheet and income statement at the end of the year, based on the General Communiqué on Accounting System Implementation published by the Ministry of Finance. Associations that keep their records on the basis of cash accounting issue a "Business Account Table" at the end of the year as shown in the Regulation on Associations[10].

Accounting requirements for the foundations are similar to those for associations. Most of the foundations keep their accounting records in accordance with the *Vakıflar Tek Düzen Hesap Planı* which is published on the official website of the General Directorate of Foundations, and prepare their balance sheet and income statements

[7] https://www.siviltoplum.gov.tr/kamu-yararina-calisan-dernek-statusu
[8] Turkish Commercial Code No. 6102 Article 18
[9] https://www.siviltoplum.gov.tr/ankara/tutulacak-defterler-ve-uyulacak-esaslar (Accessed on 1/5/2022)
[10] https://www.siviltoplum.gov.tr/ankara/tutulacak-defterler-ve-uyulacak-esaslar

according to the sample tables. For the foundations with annual gross income above the amount determined by the Ministry of Finance and foundations with tax exemption, it's obligatory to keep records on the basis of double-entry bookkeeping. Here, the inventory ledger constitutes an exception. It's mandatory for the foundations -unlike for the associations- that keep their books on the double-entry basis. The regulation on foundations also mandates a ledger to record the invoices of donations[11].

Nonprofits in Turkey are obliged to comply with the Turkish Accounting Standards (TMS) and Turkish Financial Reporting Standards (TFRS) which are the direct translations of IAS and IFRS respectively.

2.2.5. Legal Accountability of NPOs in Turkey

This subsection briefs about to whom and for what Turkey-based institutions are legally accountable.

The governmental office to which associations are accountable is The Ministry of Interior the Directorate General for Relations with Civil Society. At the end of each year, associations submit a declaration to the ministry through the local authorities until April. This declaration, which consists of 12 sections, contains organizational (structure, affairs, members/employees) and financial (revenue/expenses, grants/donations, balance sheet) information about the association. Internal audit is mandatory for associations[12], must be conducted at least once a year.

Foundations are legally accountable to the Directorate General of Foundations which operates under the Ministry of Culture and Tourism. As stated in the Article 32 of the Law on Foundations[13], a statement that contains organizational and financial information of the preceding year shall be submitted to the Directorate General by the management of the foundation within the first 6 months of a year. Foundations must also document that they disclose financial information via appropriate media and means. Internal Audit is a must for the foundations.

---

[11] Regulation On Foundations:
https://www.mevzuat.gov.tr/mevzuat?MevzuatNo=12466&MevzuatTur=7&MevzuatTertip=5
[12] https://www.siviltoplum.gov.tr/sivas/derneklerde-ic-denetim-zorunlulugu-
[13] Law on Foundations, Article 32: https://www.mevzuat.gov.tr/MevzuatMetin/1.5.5737.pdf

The article 33 is regarding the audit procedures of the foundations:

"Internal auditing is a must in annexed (mülhak), Community, artisans' and new foundations. The foundation may be audited by its own bodies or by independent audit firms.

Foundation managers shall submit the reports of in-house audits which are to be conducted at least once a year and the results to the Directorate General within two months following the date of the report, at the latest.

The Directorate General shall carry out an audit for checking compliance of the foundation to its objectives and the applicable laws as well as for compliance of its economic enterprises with the legislation and its activities."

2.3. PRIOR LITERATURE

2.3.1. Non-Profit Accounting Compared to the Commercial Accounting

Although the literature reveals that the differences between for-profit and non-profit accounting are significant, there are also claims that these two practices are actually one in principle (Konca, 2006, p.7):

"The accounting system is one. While establishing the system, no distinction was made between for-profit organizations and non-profit organizations. In principle, the same system is applied in for-profit commercial companies and non-profit NGOs, especially associations and foundations. Since the interests and fields of activity of commercial organizations and NGOs are different, some special adaptations are made especially in the chart of accounts, provided that the essence of the system remains the same."

Through the definition in the book named *A Dictionary of Nonprofit Terms and Concepts* (Smith et al., 2006), it can be inferred that the difference between the two terms is on the basis of the organization in which it is carried out. Apart from this, no distinction was mentioned in the dictionary.

The literature, on the other hand, highlights that not-for-profit accounting has its own characteristics which distinguish it from governmental and commercial accounting:

- To begin with, commercials -unlike the governmental bodies and nonprofits that meet some specific criteria- can not be tax-exempt (Hopkins, 2011, p. 3). This point is followed by the fact that nonprofits are usually unincorporated (Cordery et al., 2016).
- Nonprofit organizations do not have stockholders unlike for-profit corporations (Bhandari, 2010). Total assets less total liabilities equals to net assets of an NPO while it gives the equity of stockholders in a corporate balance sheet (Calabrese, 2011).

Assets – Liabilities = Net Assets

- Non-profit capital structure extends the distinctions further (Bowman, 2002): Some assets are subjected to legal and donor restrictions. Donors can place restrictions on their donations as well as government-grants can be specific to fund certain programs (Yermack, 2017). These contributions are not to be used for any other purpose. Yermack (2017) revealed that this has been a growing trend over the last decades.

Unrestricted Net Assets = Net Assets - Restricted Assets

- The restriction on assets affects the management of equity, and the necessity of fund accounting arises (Kilcullen et al., 2007). Fund accounting enables the organization to keep and track the records accurately, comply with the standards, and provide the donors with the information that their contributions are used in the direction they want (Reck & Lowensohn, 2014, p. 589)**.**
- Another feature that distinguishes npo accounting from for-profit accounting is the presence of gifts-in-kind. They are non-monetary charitable givings to the tax-exempt entities. Nonprofit institutions are highly reliant on the gifts-in-kind (Reck & Lowensohn, 2014, p. 536). Depending on the national accounting standards, recognition and assessment of these kinds of contributions can vary (Lopez-Arceiz et al., 2021).
- In nonprofit accounting, there are costs associated with fundraising and publicity. Disclosure of fundraising and programme expenses matters for the sake of a charity's accountability. In the UK, for instance, Charity SORP (Statement of Recommended Practices) requires the charities to report these 3 classification of activity costs (fundraising, charitable activity and governance) separately (Connolly et al., 2013).
- Some items have cultural value even if their economic value is insignificant (Ellwood & Greenwood, 2016). In non-profit financial reporting, cultural assets which actually have no market-value are not to be omitted. The cultural properties with low to zero

economic value (for instance, heritage assets) must be recognized, measured and reported for accountability purposes (Craig et al., 2012; Aversano et al., 2019).

- The requirements for narrative reporting constitute the final significant distinction (Connolly & Dhanani, 2009; Morgan & Fletcher, 2013). Within an annual report, a narrative report plays a complementary role by providing non-financial information. It's intended to provide a broader picture of an organizations' work. Considering that nonprofits' missions are non-monetary, financial reporting without narrative reporting is usually incomplete.

2.3.2. The Concept of Financial Health

The concept of financial health is multiplex and has multiple dimensions (Chen, 2021). Neither in the literature nor in law there's a clear and agreed upon definition of financial health. This term is conceptualized differently by different scholars. The health in this context can be therefore generalized as financial condition or situation.

Researchers have attributed a variety of qualities to the concept of financial health. For instance, Anne Abraham (2003) defines the negative health with *vulnerability* which occurs through mission. And the entity's ability to keep operating is *sustainability* which is possible with *accountability* through adequate control systems. Sustainability is measured and promoted with adequate control systems.

From both for-profit and nonprofit perspectives, the diagnostic role of auditing and accountability has been recognized by the literature (Puplampu, 2005). Corporate failures and scandals in the last decades have provided concrete evidence in this regard.

According to Bowman (2008), the concept of financial health is two-dimensional: (1) capacity and (2) sustainability. From an organizational perspective, financial capacity is the amount of resources that makes it able "to adapt to internal pressures for adjustment or to external pressures for change in policy, as well as to initiate changes in strategy with respect to the external environment." (L. J. Bourgeois, 1981). Bowman defines financial sustainability as the quantity "measured by the rate of change in capacity in each period" (Bowman, 2011).

Positive financial health is often represented by the terms of resilience, stability, wellbeing, sustainability, strength etc. Likewise, negative financial health is expressed in the words like distress, vulnerability, ill-health, failure etc.

In most of the earlier academic works, “financial vulnerability” used to refer to “financial health” (Prentice, 2016b). However, financial health has a broader meaning that can describe an organization’s economic conditions.

Researchers reveal that even nonprofit financial vulnerability is a relatively new field of academic work (Tevel et al., 2015). Tevel et al. (2015) define the financial vulnerability as “an organization’s susceptibility to financial problems”. Earlier, Tuckman and Chang (1991) defined nonprofit financial vulnerability as the likelihood of an institution to cease their services instantly after a fiscal shock.

Financial distress, like financial vulnerability, has various definitions. Unlike vulnerability, it mostly refers to a specific period or a certain event; identified with shortage, decline, failure, disaster, or more specifically downturning liquidity, bankruptcy etc. In literature, financial distress is mainly defined from the for-profit perspective as:

- Inability of an enterprise to reimburse its fiscal obligations after the time of expiration (Fitzpatrick, 1932).
- Downsizing, illiquidity, insolvency and high amount of operating expenditure (Beaver, 1966).
- A costly event that has potential to force the administration to conduct more harmful actions (Opler & Titman, 1994).
- An outcome of long-standing economic losses that results in the inflation of debt and loss of assets (Van Gestel et al., 2006).
- The risk of bankruptcy, depending on the amount of liquid assets, access to credit and ability to get a loan (Hendel, 1996).
- A company’s in-between state of going from solvent to insolvent (Purnanandam, 2007).

Not all scholars define corporate financial distress as a turning point on the road to bankruptcy. Jensen (1989) argued that distress is actually beneficial to organization.

It's like a symptom that leads to the initiation of treatment. Jensen's hypothesis was supported by some empirical tests (Whitaker, 1999).

Whitaker's paper (1999) also doesn't treat financial distress as a one-off incident. Because a corporation under distress already suffers from failures even before the situations like insolvency or bankruptcy. Turetsky and Mcewen (2001) depict financial distress as "a series of financial events that reflect varied stages of corporate adversity". Several studies have revealed that it's a dynamic process and has a heterogenous nature (Turetsky & McEwen, 2001).

In literature, scholars paid little attention to financial distress in nonprofits. Even definitions of "nonprofit financial distress" are extremely scarce. Hence, this subsection ends with an exceptional definition.

Nonprofit financial distress usually refers to the failure of organizations to practice the necessary processes that must be performed in a professional manner (Williams, 2010).

2.3.3. Analyzing Non-Profit Financial Health

Before highlighting the existing literature on this topic, it is worth mentioning that there's no general agreement over the best method of measuring financial health of nonprofits (Prentice, 2016a).

Various definitions of financial distress from a business perspective listed in the previous subsection indicate that an organization's financial statements are sufficient to provide the necessary data to assess the organization's financial health. Based on the fact that these markers rely on historical data, they are often criticized to be retrospective. However, accounting-based indicators are still utilized by professionals and academic researchers. Because they have proven to be useful to analyze trends and predict potential failures (Michalkova et al., 2018).

In the literature, the analysis of financial distress and vulnerability of non-profit organizations is clustered around the method developed by Tuckman and Chang (Myser, 2016). They elaborated four operational criterias:

1. Equity Balance (Formulated as Net Assets/Total Revenue): Institutions with more net assets are healthier;
2. Revenue Concentration (Formulated as 1/Number of Funders): Getting funded from multiple sources is better than a single source;
3. Administrative Cost (Formulated as Administrative Costs/Total Costs): More administrative costs is a good sign;
4. Operating Margin (Formulated as Net Income/Total Revenues): Lower net income is a symptom of vulnerability (Tuckman & Chang, 1991).

Altman's renowned method to forecast bankruptcy has been adopted from for-profit prediction to be utilized in measurement of nonprofit financial health. For instance; Lord, Landry, Savage and Weech-Maldonado (2020) used a modified Altman Z-Score to assess the nursing homes' risk of financial distress:

"$F = \beta_0 + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \varepsilon$

$F = \beta_0 + (0.18 \times \text{Liquidity}) + (0.30 \times \text{Profitability}) + (0.81 \times \text{Efficiency}) + (0.14 \times \text{Net Worth}) + \varepsilon$"

The equation above is applicable to both for-profit and not-for-profit nursing homes (Lord et al., 2020).

Another well-known bankruptcy prediction method adopted from the business sector is Ohlson's model (1980). He built his probabilistic model on 9 independent variables:

1. "SIZE = log(total assets/GNP price-level index)"
2. "TLTA = Total liabilities divided by total assets"
3. "WCTA = Working capital divided by total assets"
4. "CLCA = Current liabilities divided by current assets"
5. "OENEG = One if total liabilities exceeds total assets, zero otherwise"
6. "NITA = Net income divided by total assets"
7. "FUTL = Funds provided by operations divided by total liabilities"
8. "INTWO = One if net income was negative for the last two years, zero otherwise"

9. "CHIN $=(NI_t - NI_{t-i})/(|NI_t| + |NI_{t-1}|)$, where NI_t is net income for the most recent period. The denominator acts as a level indicator. The variable is thus intended to measure change in net income. (The measure appears to be due to McKibben [1972])" (Ohlson, 1980).

By reviewing the literature, it can be seen that these methods are sometimes applied in modified forms. Trussel's article (2002) provides a good example of this: He added debt ratio (Total Liabilities/Total Assets) to the model of Tuckman and Chang (1991). His research concluded that the relationship between debt ratio and financial vulnerability is positive and statistically significant (Trussel, 2002).

The comprehensive research conducted by Keating, Fischer, Gordon and Greenlee (2005) to compare these models suggests that Ohlson (1980) model is statistically more significant than the models of Altman (1968) as well as Tuckman and Chang (1991). To be more specific, the Ohlson model was found to be superior in predicting financial vulnerability. On the other hand, none of the models -alone or in combination- found effective to predict financial distress (Keating et al., 2005).

According to a more recent study to examine the validity of prediction models, the Tuckman and Chang model outperforms the Ohlson model. The study concludes that Ohlson's business model may not be appropriate for measuring or predicting nonprofit financial vulnerability (Tevel et al., 2015).

Ratio analysis has been a useful tool for measuring nonprofit financial performance and accountability (Hairston, 1985). The ratios have been in use since the last decades of the 1800s (O'Connor, 1973) to evaluate an organization's fiscal stability along with three basic concepts that describe financial performance: solvency, liquidity and profitability.

Aside from the commonly used financial ratios which are categorized under profitability, liquidity and solvency; NPOs tend to use different sets of financial ratios depending on their missions and field of activity (Abraham, 2006). Calculating the relevant ratios of some consecutive years and examining the trend is considered to be the most useful method in terms of providing a bigger picture and more accurate results (Chabotar, 1989).

Although existing literature prioritizes quantitative measurement, there are also quality factors and indicators to be considered. Because focusing solely on the numbers and amount can result in missing the context. In addition, some non-monetary concepts are highly relevant to nonprofit financial health: Leadership, reputation (Peng et al., 2019), reliability of funds, motivation etc.

Based on their review (2018), Michalkova et al. point that there is no sufficient examination of qualitative indicators. According to their paper, even some lesser known quality indicators have potential to be predictors of financial distress.

Research by McHugh and Brotherton (2000) reveals that wealth doesn't necessarily mean health. Organizations that enjoy favorable economic conditions may be actually suffering from unfavorable management practices at the same time. Sustaining malpractices are the sources of long term economic ill health.

In public financial health which is similar to NP financial health in terms of being not-for-profit, qualitative measures such as analysis of information collected from discussions and local workshops are utilized to predict the financial distress of local governments (Padovani et al., 2010).

Even in the for-profit literature, there are studies examining the role of non-financial in predicting bankruptcy. Sun and Li (2007) concluded in their paper based on the hybrid methodology, that *group decision making* is a useful tool to predict and diagnose financial distress.

To summarize this section, measurement of nonprofit financial vulnerability and distress is almost completely accounting-centric. This raises the question regarding the accuracy of financial reporting in these institutions. It is discussed in the next chapter.

CHAPTER 3: THE ISSUES ORGANIZATIONS FACE IN ACCOUNTING AND REPORTING

3.1. INTRODUCTION

In the previous section, the differences between commercial and non-profit accounting practices were revealed by reviewing the literature. At this stage, the problems encountered specifically in non-profit financial reporting are addressed. There is no doubt that financial reporting can be problematic in any type of organization. Some challenges apply to everyone. All issues examined in this section are either sector-specific or more significant in the non-profit sector.

The aim of this chapter is to explore and discuss the challenges nonprofit organizations face in financial reporting. As the measurement of nonprofit financial health is almost totally accounting-centric, the accuracy of financial reporting and reliability of metrics are justifiably questioned. Furthermore, the problems investigated in this thesis directly affect the health of organizations. For instance, congestion in operations causes stress; and stress triggers loss of employees/volunteers as well as materials.

3.2. METHODOLOGY

Major challenges nonprofits face in financial reporting are identified by briefly reviewing the literature. In other words, the prior literature highlighted in Chapter 2 is further extended in the next subsection. Mini cases and comments from experts were gathered in intention to reinforce the theoretical background with practical evidence.

The sampling here is purposive. Some criteria were taken into consideration while sampling. For example, all cases are real world stories from the nonprofit and voluntary sector. And the experts are people who have been in managerial positions in the institutions. The conclusion was drawn by critical thinking.

3.3. THE ISSUES ORGANIZATIONS FACE

Based on the existing literature, some major issues regarding the financial reporting listed with no ranking as:

- Accounting Basis Conflict
- Accounting Errors
- Gifts-in-Kind
- Compliance with the Standards
- Vulnerability to Fraud

Accounting Basis Conflict

Cash and accrual are the two main bases of accounting. Apart from these two, there are also modified or mixed approaches.

Cash basis recognizes a transaction when cash flows in or out. Accrual accounting, on the other hand, requires the recording of income when earned and expenses when incurred.

Grants are recorded after confirmation, regardless of whether the transfer of cash actually happens (Bourgeois, 2003, p. 13). This creates confusion and makes the accounting basis conflict even fiercer. Unpaid bills and uncollected revenues are shown in the statements.

The main reason that makes this problem a serious dilemma is that some legislations mandate accrual accounting.

As stated earlier in the Legislative Framework, US GAAP mandates. Even if some institutions may choose the cash basis for internal usage, they are required to prepare and disclose all financial statements on the accrual basis in order to comply with GAAP (Reck & Lowensohn, 2014, p. 527).

Accounting Errors

Accounting errors are unintentional malpractices in financial reporting. In NPOs, these non-fraudulent wrongdoings happen mainly because of low attention, poor level of financial literacy and lack of professionalism (Aranda, 2019).

An insightful research by Burks (2015) is explaining:

"A sample of 5,511 audited financial statements, predominantly from the years 2006 to 2010, was obtained from GuideStar, a data provider for nonprofits. Public charities report errors at a rate that is 60 percent higher than that of publicly traded corporations, and almost twice as high as that of similar-sized corporations. The errors are commonly errors of omission (i.e., failing to recognize items)." (Burks, 2015)

Gifts-in-Kind

Gifts in kind (GIK) or in-kind donations are charitable contributions which are not monetary. They can be tangible such as clothing, food, drugs as well as intangible like medical or legal service.

A study on developments of not-for-profit sheltering revealed that around 19.1% of grants and donations were made in non-monetary ways (Herbert & Wallace, 1998) such as donation of land, fee waiver, credit with no interest etc.

Non-cash status of gifts-in-kind does not change the fact that they have economic value. Since in kind donations are usually tax-deductible, they are not to be omitted in financial reporting. And the problem arises when it comes to the valuation of these items.

The way GIKs are valued is dependent on local regulations. While in Turkey GIKs are recognized mostly at cost value (Income Tax Law, Article 40/10), in the US the recognition of these contributions is standardized at fair value (AICPA, accessed on 3.6.2022).

Valuation of in-kind contributions is a complex and exhausting procedure, especially in case of the lack of professional expertise. Furthermore, it is a two-sided problem since the donor's valuation can be inappropriate as well. As a result of inconsistent valuation of in-kind donations, this practice became controversial in the nonprofit and voluntary sector (Brenner, 2013). For these reasons, organizations that accept donations should manage this procedure strategically.

Compliance with The Standards

Another significant issue is the absence of globally accepted accounting standards specific to the third sector. In addition to the guidance, international standards have a noteworthy role in keeping the harmony. As stated earlier, both IPSAS and IFRS are inadequate to provide guidance to the nonprofits and remove the disharmony.

Surveys conducted within the scope of a study on international financial reporting in non-profit organizations reveal the need for the standardization (Crawford et al., 2014). And to meet this need, projects such as IFR4NPO have emerged in recent years (See page 12).

However, bearing in mind that non-profits are considered to be tardy in regulatory filing and poorly compliant with the existing accounting frameworks, there is no guarantee that they will follow the nonprofit accounting standards (Morgan & Fletcher, 2013; Reheul et al., 2014; Breen et al., 2018).

Vulnerability to Fraud and Corruption

The risk of fraud exists in all types of organizations, but nonprofits particularly are more vulnerable to this risk due to poor monitoring and inadequate internal controls. And given the importance of reputation to these institutions, the harm caused by fraud can be more devastating.

"Report to the Nations: 2020 Global Study on Occupational Fraud and Abuse" published by the Association of Certified Fraud Examiners (ACFE) contains comparative information on fraud. The report reveals the weaknesses of nonprofits in this regard:

- Likelihood of surprise audits: 21% in NPOs, 40% in other organizations,
- Frequency fraud risk assessments: 24% in NPOs, 43% in other organizations,
- Management review: 44% in NPOs, 68% in other organizations,
- Having internal audit departments: 57% in NPOs 76% in organizations (ACFE, 2020, p.29).

Nonprofits’ susceptibility to adverse publicity makes them more reluctant to report internal fraud cases (Seyam et al., 2018). Studies show that the likelihood of whistleblowing in NPOs is lower than in corporations (Scheetz et al., 2020).

3.4. PRACTICAL EVIDENCE

This subsection intends to reinforce the theoretical background with practical evidence which is grouped under mini cases and comments from experts.

3.4.1. Case Studies

Case 1: Red Crescent’s Inability to Account

After the devastating Haiti earthquake of 2010 which killed 220,000 people, the American Red Cross ran a massive campaign endorsed by Michelle Obama.

In 2015, it turned out that the Red Cross raised $500 million following the Haiti earthquake in 2010, but nothing concrete was done with the money raised. The Red Cross, which claimed to have built houses for 130,000 people, had built only 6 permanent houses.

There were allegations that the American Red Cross saw the Haiti earthquake in 2010 as an opportunity to raise money. Because they did nothing tangible with half a billion dollars they raised. The eminent charity was being subjected to investigative journalism.

Finally, it turned out that the charity actually failed to track its spendings. The funds were severely mismanaged. There was "no correct process for monitoring project spending”. And "Poor, inadequate, slow support from NHQ [national headquarters] was also regularly cited as a reason for poor morale." (Elliott & Sullivan, 2015; Elliott, 2015)

Sources: NPR (National Public Radio) & Propublica

Case 2: Overvaluation by $250 Million

Overvaluation, be it intentional or unintentional, is a serious issue that a charity may cause or face.

Overvaluation of non-cash donations can give potential donors the impression that the charity is larger and more efficient than it actually is. It can also lead to a misleading increase in efficiency rates, which are important indicators of financial health.

William P. Barret, a contributor to Forbes, has reported multiple overvaluation scandals. One of the cases he covered on Forbes was probably the highest overvaluation up to that time: A charity had exaggerated the donated goods by $250 million.

Operation Compassion, which declared $931 million in revenue between 2008 and 2011, was supposed to correct this figure by reducing it by $250 million due to overvaluation. Of the revenue declared by the Cleveland-based charity, approximately $919 million was in-kind donations. Only $12 million was cash and cash equivalent.

David Lorency, the president of the institution at the time, admitted the mistake and attributed this huge amount of overvaluation to rapid growth and the incompetence of the staff. He promised that they would do whatever necessary to fix all retrospective errors.

Source: Forbes (Barrett, 2013) accessed on 7.6.2022

Case 3: Accounting Error in the Theater

The Carolina Theatre of Durham Inc. a not-for-profit entity operates a theatre facility in Durham, Carolina on a non-profit basis in agreement with the city government. It has a good reputation: known to be transparent and supported by a wide philanthropic network.

In 2013, the non-profit theater decided to implement some kind of growth strategy. Since then, more audiences have been reached and diversity of shows has increased. The number of shows increased from 25 per week in 2009 to over 100 in 2015.

In addition, there was an impression that the Carolina Theatre of Durham was also performing financially effectively. Revenues seemed to have increased from 2.5 million to 5 million. In February 2015, they declared that they were generating surplus for the last two years.

In May 2015, the then-CEO received an email from the bank informing him that the state had imposed a levy on the account of Carolina Theatre and that there was more than $155,000 in taxes due. The finance director who was responsible for this trouble was fired in a couple of days. When executives hired an accounting firm, they got a closer look at what kind of disaster they were in.

“Dozens of invoices had not been entered into the financial reports. Large chunks of revenue had not been accounted for. Larger chunks of expenses had not been accounted for. The accounting firm had to reconcile dozens of vendor accounts from scratch.” (Hudnall, 2016)

The theater, which was thought to be generating surplus for the last two years, actually had a deficit of $830000. They had a total debt of more than $1 million, with $225,000 in debt from previous years.

Executives agreed that this enormous deficit was due to lousy accounting, and there was no fraud. The city manager's comment was more descriptive and also inclusive: "Certainly there was horrible accounting, but there was also poor oversight across the board."

Source: indyweek.com, accessed on 07.06.2022

Case 4: Trouble Caused by Unpaid Membership Dues

Saint Josephliler Derneği, which consists of people educated in one of Istanbul’s leading private high schools, was facing a hard dilemma. Out of a total of 2500 members, around 1100 used to pay their dues on a regular basis. Apart from these, 400 members were contacted and their accrued fees were successfully collected. The remaining 1000 members had debts of approximately ₺ 1,000,000.

Article 70 of the Turkish Civil Code states that:

“Members' obligation to pay dues is regulated by bylaws. If there is no regulation in the bylaws, the members participate equally in the compulsory payments for the realization of the purpose of the association and the payment of their debts. The member who voluntarily leaves or is removed from the Association must pay for the period of membership. Honorary members are not obliged to pay dues.”

In addition, the administration reminded that:

“Based on the relevant provisions of the Turkish Civil Code and the Law on Associations, enforcement proceedings without verdict can be executed against the members for the unpaid dues.”

The association which has overwhelmingly wealthy members was actually struggling with financial difficulties. Even though it had a high liquidity when evaluated on an accrual basis, SJD was actually in a financial bottleneck. And this is the case for many other associations.

Source: SJD Facebook Page: facebook.com/sjdernek/posts/903947916284344/

3.4.2. Comments from Experts

Scandals of overvaluation of GIKs were covered by Ruth McCambridge on Nonprofit Quarterly (NPQ). Some entities were fined with thousands of dollars, and some others fell under scrutiny. In the comments section, nonprofit managers shared their own experiences regarding this issue.

Keith Oberg says that such malpractices undermine the trust towards nonprofits that accept in-kind contributions. Paul Fischette emphasizes the importance of fair value when evaluating such donations. He adds, however, that subjectivity is inevitable. Both experts explained their own fair value practices.

Keith Oberg: “Such practices as Food for the Hungry and the Breast Cancer Society are reported to have done endanger the credibility and tax advantages of other non-profits handling in-kind donations. Bikes for the World carefully documents its donations of used bikes sampling receipts issued at donation points by volunteers and staff, which engage individual donors in valuing their widely-varying donations using written guidance on determining market value. Donors depart with a receipt containing a written estimate (for which they are responsible should they use for tax purposes), and Bikes for the World keeps copies for its records. The result is that Bikes for the World can calculate a statistically-valid average value for donations applicable to our entire "production" for a given year.”

Paul Fischette: “This scandal is a reminder that in-kind donations must ALWAYS be accounted for at Estimated Fair Market Value.

There will always be some subjectivity in trying to determine Fair Market Value. Nonprofits SHOULD ALWAYS find a neutral third party. When I was Finance Manager for a Rochester, NY nonprofit, we received an in-kind donation of a mixed use residential and commercial building from a local business man. We obtained all necessary closing documents, prior property tax bills and documentation from the City of Rochester. The City noted on its tax bills that the property had an Assessed Value of $55,000. The attorneys whom we worked with consulted a local property appraisal firm. The appraisal firm estimated that the Fair Market Value of the property was $73,000. We booked the value of the property based on the $73,000 estimated Fair Market Value from the appraiser. Figures don't lie, but liars figure!”

In the case covered by Rick Cohen on NPQ, there were allegations of fraud against the senior executive, and apparently the board members either turned a blind eye or were completely unaware. A commentator named Judi Patrick points out the invisibility of red flags.

Judi Patrick: “I would like to propose a novel idea ... that some amount of tension between executive director and board is a healthy dynamic. While no director wants a board of directors that micro-manages daily operations, a skilled executive director should embrace a board that keeps a close perspective on the organization's programs, services and finances. Additionally, no skilled executive director should want a board of directors that is uninformed or detached from the organization's operations. Such a board provides little input into the organization and little opportunity for healthy output from the organization... In fact, such a board is merely a "rubber stamp".

It is natural for the director to want to lead his/her organization in the direction they feel is best. However, none of us is as smart as all of us (as the saying goes), and the perspective of the board is often less subjective and more objective.

Again, micro-management is not the board's purpose. However, direction and oversight certainly are within the purpose of the board. It should be a red flag to any board if and when a director (or any executive staff) is providing only selective information or fails to provide complete programmatic or financial reports.

No... I'm not on a non profit board of directors. (Admittedly, I have been on a nonprofit board in the past.) I am the associate director for a nonprofit that has a board of directors that is both challenging and engaged."

3.4. SUMMARY AND CONCLUDING REMARKS

As nonprofit financial reporting is different from corporate financial reporting, the challenges organizations face are also different. It's a phenomenon that the vast majority if not all of the organizations in the nonprofit and voluntary sector face enormous challenges in financial reporting. They may become a huge burden even for the globally renowned NGOs with decades of experience and capacity to raise millions of dollars.

To measure financial health, organizations (both for-profit and nonprofit) mostly rely on the data obtained through financial reporting since these metrics are objective and quantifiable. However, the reliability of accounting-centric approaches in NPOs may not be as much as in corporations.

First of all, financial statements are usually retrospective. Before conducting an analysis, it should be noted that most of the non-business entities publish their statements months or even years after a fiscal year-end.

Secondly, the reliability of accounting-centric measurement of financial health is lower in nonprofits than in corporations due to higher risks of error and manipulation largely as a result of complexity and lack of professionalism.

Last but not least, numbers can provide a picture but can't tell the whole story. Focusing solely on the numbers may result in missing the context.

CHAPTER 4: FINANCIAL PERFORMANCE OF TURKEY'S THIRD SECTOR

4.1. INTRODUCTION

This section constitutes the quantitative part of the thesis. Financial health of Turkey-based membership organizations is evaluated on the basis of ratio analysis. A typical industry ratio analysis is conducted to measure the aggregate financial performance of membership institutions.

In collaboration with TÜİK (Turkish Statistical Institute), TCMB (The Central Bank of the Republic of Turkey) produces and publishes the sector balance sheets. The Central Bank follows the Statistical Classification of Economic Activities in the European Community (NACE Rev. 2), and publishes the balance sheets in line with those sections, divisions and codes.

Membership organizations are classified in Section S (Other Service Activities), identified by the code 94. The division with code 94 is divided into groups which are represented with three digits such as 94.2 (Activities of trade unions). And groups are subdivided into classes which are coded with four digits. For instance, "Activities of other membership organisations" contain:

- 94.91 Activities of religious organisations
- 94.92 Activities of political organisations
- 94.99 Activities of other membership organisations n.e.c. (EUROSTAT, 2008, p. 88)

As already highlighted in the literature review, different quantitative approaches can be taken to evaluate the financial health of membership organizations. Every analytical method has strengths and limitations.

This study examines organizations' financial performance on the basis of traditional ratio analysis. Not every traditional performance indicator is appropriate for analyzing nonprofits' financial conditions. For instance, equity ratio cannot be undertaken to evaluate stability due to the absence of "Shareholders Equity".

Studies conducted to test the usefulness of key financial ratios in the financial analysis of nonprofits suggested that the following ratios are applicable:

- Rate of Return on Total Assets,
- Current Ratio,
- Quick Ratio,
- Debt Ratio (Kent, 1993).

4.2. DATA AND METHODOLOGY

The data used in this analysis was acquired from the TCMB's page of "Company Accounts" which shares sector statistics annually. A file downloaded from the website of the Central Bank in late 2020 contains sectoral balance sheets and income statements between 2009-2019 (TCMB, 2020). It has been the last dataset that includes sectoral financial statements of the membership organizations. And this cross-sectional analysis addresses the balance sheet of 2019.

Sectors which are not covered in the scope of the collaborative work of TÜİK and TCMB are "K Financial and insurance activities", "O Public administration and defence; compulsory social security", "T Activities of households as employers; undifferentiated goods- and services-producing activities of households for own use" and "U Activities of extraterritorial organisations and bodies".

Since there are no geographical restrictions in the statistics published by the central bank and the scope is country-wide, this study is comprehensive in nature.

This method has both strengths and limitations. On the one hand, it is applicable to a wide spectrum of organizations, provides an understandable basis to stakeholders for evaluating an organization's financial performance and condition (Abraham, 2006). On the other hand, mission-oriented approaches are more specific and precise than the basic financial ratios.

As for the limitations of the study in terms of data, the data from small-sized membership organizations is not included in the balance sheets. Plus, the number of samples had fluctuated between 2009 and 2019 (194 organizations were sampled in

2019). In addition, the difficulties faced by these institutions in financial reporting raise questions about the reliability of the figures.

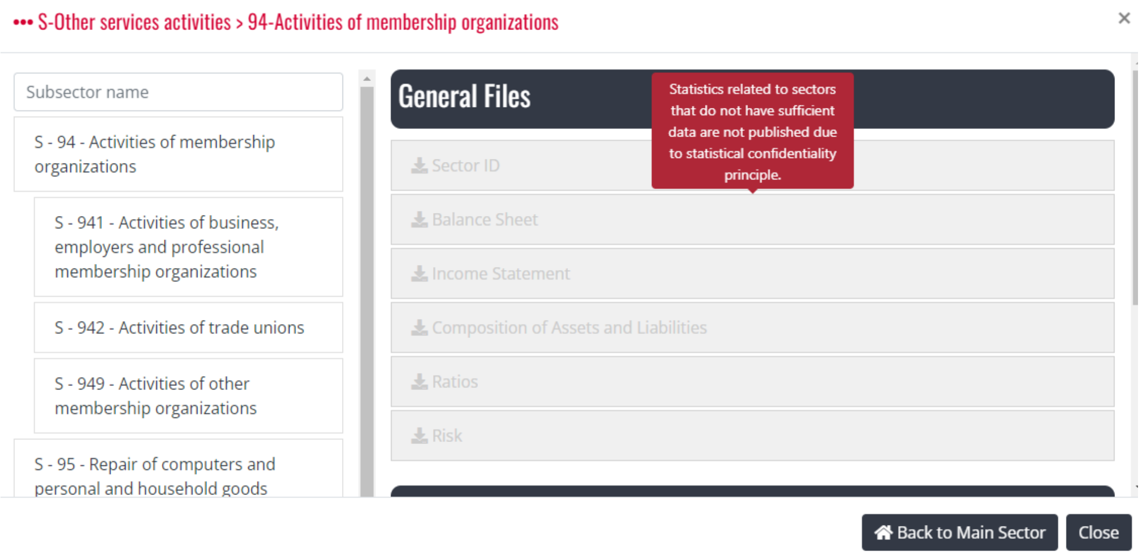

Figure 4.1 2020 Sectoral Statistics of the Turkey-based Membership Organizations. (TCMB, 2022) https://www3.tcmb.gov.tr/sektor/#/en/S/other-services-activities

Figure 4.1 shows that Statistics on the performance of the member organizations in 2020 were not sufficient, so they were not published.

4.3. FINANCIAL ANALYSIS OF MEMBERSHIP ORGANIZATIONS IN TURKEY

Ratio analysis has been a useful tool for measuring nonprofit financial performance and accountability (Hairston, 1985). The ratios have been in use since the last decades of the 1800s (O'Connor, 1973) to evaluate an organization's fiscal conditions based on three fundamental concepts that describe financial performance: solvency, liquidity and profitability.

4.3.1. Liquidity Ratios

They measure an organization's capacity to cover its near-term payment obligations. Balance sheets contain sufficient data to calculate liquidity ratios by displaying the structures of assets and liabilities.

Table 4.1. Liquidity ratios of Membership Organizations in Turkey

	2021	2020	2019
Current ratio	N/A	N/A	104.7%
Quick ratio	N/A	N/A	100.6%
Cash ratio	N/A	N/A	5.4%

(Source: Own Tabulation)

Current ratio answers the question whether the current resources are sufficient to cover current liabilities. It’s formulated as:

$$\text{Current Ratio} = \text{Current Assets} / \text{Current Liabilities}$$

The traditional rule of thumb for this ratio is 2:1 or 200%. Special attention needed if the current ratio drops below 1.

Quick ratio, also known as the acid-test ratio, answers the question whether non-inventory current assets can cover the current liabilities. It’s formulated as:

$$\frac{\text{Current Assets} - (\text{Inventories} + \text{Prepayments and Accrued Income for the Next Months} + \text{Other Current Assets})}{Short - Term\ Liabilities}$$

Traditionally, the rule of thumb for acid-test ratio is considered to be above 1:1. If this ratio is less than 0.25, it indicates that the organization is in distress.

Cash ratio which is the least popular liquidity ratio answers the question whether the most liquid assets are enough to cover current liabilities. It’s formulated as:

$$\text{Cash Ratio} = \frac{Liquid\ Assets + Marketable\ Securities}{Short{-}Term\ Liabilities}$$

Cash ratio is generally preferred to be between 0.5 and 1.

4.3.2. Solvency Ratios

They measure an organization’s ability to generate sufficient resources to meet its short-term and long-term obligations. Since the so-called shareholders’ equity doesn’t exist, the applicability of solvency (leverage) ratios is more limited in comparison to the liquidity ratios. Some studies utilize only debt to assets ratio (or shortly debt ratio) to measure the NPOs’ solvency (Kent, 1993).

Table 4.2. Debt Ratio of Membership Organizations in Turkey

	2021	2020	2019
Debt ratio	N/A	N/A	98%

(Source: Own Tabulation)

Debt ratio answers the question to what degree assets are financed with borrowings. In other words, how dependent is the organization on debt. It is formulated as:

$$\text{Debt Ratio} = \frac{\text{Total Debt}}{\text{Total Assets}}$$

As a rule of thumb, debt to assets ratio is usually preferred to be under 1. Especially for the nonprofits, it’s better to have a lower score of debt ratio. Ken (1993) suggests that an alternative rule of thumb with the upper limit of 20% can be more appropriate in determining nonprofit financial stability.

4.3.3. Profitability Ratios

Profitability ratios test whether the revenues of an institution are enough to cover its operating expenses. They also measure the organization’s ability to generate surplus. In calculating profitability ratios, figures from the income statement are used, as well as those on the balance sheet.

Table 4.3. Profitability Ratios of Membership Organizations in Turkey

	2021	2020	2019
Rate of Return on Total Assets	N/A	N/A	0.49%
Net Profit to Total Assets	N/A	N/A	0.39%

(Source: Own Tabulation)

According to Tuckman and Chang (1991), lower net income is a symptom of financial vulnerability. Organizations that generate higher amounts of surplus have greater chances of surviving a possible financial crisis.

Rate of return on total assets is widely used to measure the relationship between the operating profit before tax and average total assets. Since net income is not distributed to non-existent shareholders, total assets of the previous year are found by subtracting net income from the total assets. Ken (1993) demonstrates the formula as:

$$\text{Rate of Return on Total Assets} = \frac{\text{Operating Profit Before Tax}}{\text{Average Total Assets}}$$

Net Profit to Total Assets relates the organization's after-tax profit to its total assets. The fact that membership organizations in Turkey are exceptionally granted tax-exempt status means that this ratio is more relevant. According to the list by TCMB, it's formulated as such:

$$\text{Net Profit to Total Assets} = \frac{\text{Net Profit (Income after Tax)}}{\text{Total Assets}}$$

Organizations need to pay special attention if they have negative net income or their profitability ratios are in decrease.

4.4. FINDINGS AND CONCLUSION

In this subsection, the results of ratio analysis are interpreted, some major issues are figured out and finally a conclusion is drawn.

To begin with the profitability of the sector, it's not surprising that these organizations have such low profitability ratios: Rate of return on total assets and net profit to total assets are 0.49% and 0.39% respectively. The income statement published by Turkey's Central Bank indicates that the sector's net income is slightly above the break-even point. Also as revealed by the data from previous years, the sector had repeatedly created deficits.

As for the ratio of debt to assets, the sector has a score of 0.98, slightly below the generally accepted upper limit of the rule of thumb (1.0). However, recent studies on nonprofit budgeting and financial management suggest that this ratio should not exceed 0.4 (Weikart & Chen, 2021, p. 143). Back in 1993, Ken suggested that 0.2 is more appropriate.

The most significant findings of analysis are related to the liquidity ratios. The results in Table 4.1 indicate that Turkey-based membership organizations may face difficulties in covering their short-term liabilities. Traditionally, it's acceptable to have a current ratio of (1:1) but over (2:1) is more desired. Likewise, the acid-test ratio should be at least 1 (Wells, 2006, p. 51), yet over 2 is considered to be best (Weikart & Chen, 2021, p. 142).

According to the rule of thumb proposed by Kent (1993), nonprofit organizations should have both current and acid-test ratios close to 5:1. Based on this ratio, it can reasonably be inferred from the results shown in Table 4.1 that Turkey-based membership organizations have great difficulties in short-term payments.

Another key finding is that the sector has a serious issue with collecting the membership dues. This is the interpretation of the 5.4% low cash ratio displayed in Table 4.1. It constitutes a major symptom of financial ill-health.

To summarize this section, based on the data from the TCMB and TÜİK, it can be concluded that the financial situation of membership organizations in Turkey is not favorable.

CHAPTER 5: FINAL DISCUSSION

In this thesis, the financial health of non-profit institutions was examined both qualitatively and quantitatively. Based on the fact that there is no agreed-upon definition of financial health nor a best method to analyze it; instead of discussing which method is superior, the main focus has been on the issues organizations face in financial management.

This thesis also aimed to create analogies, specifically between human health and the organizations' financial health. For instance, relying solely on the balance sheet figures to evaluate an NPO's financial health is like relying solely on the blood values to evaluate a human's overall health. A complete physical examination entails not only laboratory tests but also review of the patient's medical history, eye examination, tests of physical capability, mental status examination and other clinical examinations. Likewise, the financial health of nonprofits has different aspects in addition to the monetary status: Quality of reporting, compliance with the standards, quality of internal control etc. Chapter 3 of this thesis supports the relevance of qualitative factors through real-life cases and comments from nonprofit professionals. Therefore, quality indicators have the potential of becoming diagnostic tools for early detection of distress. In addition, having knowledge of sector-specific challenges and setting policies accordingly can serve as preventive care.

A brief conclusion of this thesis may begin by restating the need for internationally accepted accounting standards specific to the nonprofit sector. Because as highlighted in the prior literature and the legislative framework, nonprofit accounting practices are mostly different from the for-profit accounting practices. Plus, traditional financial ratios and mathematical prediction models are dependent on the data obtained through financial reporting since these metrics are objective and quantifiable. However, the reliability of accounting-centric approaches in NPOs may not be as much as in corporations.

In Chapter 3, financial reporting issues that are specific to the third sector or significantly more common in the sector are explored. Major issues faced by nonprofits in financial reporting are identified to be (1) Accounting Basis Conflict, (2) Accounting

Errors, (3) Gifts-in-Kind, (4) Compliance with the Standards, and (5) Vulnerability to Fraud.

Finally, utilizing the ratio analysis, the financial situation of the membership organizations in Turkey was evaluated in the light of the data obtained from the central bank and the results were below the generally accepted rule of thumb.

Both qualitative and quantitative analyzes carried out within the scope of the thesis indicate that one of the biggest problems of the member organizations is the non-payment of membership fees.

BIBLIOGRAPHY

Abraham, A. (2006). *Financial Management in the Nonprofit Sector: A Mission-Based Approach to Ratio Analysis in Membership Organizations*. 10.

Aranda, J. (2019). *Nonprofit Financial Troubles: A Case for Financial Literacy in the Nonprofit Sector*. 43.

Aversano, N., Christiaens, J., & Van Thielen, T. (2019). Does IPSAS Meet Heritage Assets' User Needs? *International Journal of Public Administration*, *42*(4), 279–288. https://doi.org/10.1080/01900692.2018.1433205

Barrett, W. P. (2013, January 14). *Charity Eyes Quarter-Billion-Dollar Write-Down In Value Of Goods Handled*. Forbes. https://www.forbes.com/sites/williampbarrett/2013/01/14/charity-eyes-quarter-billion-dollar-write-down-in-value-of-goods-handled/

Beamon, B. (2004). *Humanitarian relief chains: Issues and challenges*.

Beaver, W. H. (1966). Financial Ratios As Predictors of Failure. *Journal of Accounting Research*, *4*, 71–111. https://doi.org/10.2307/2490171

Bhandari, S. B. (2010). Ethical dilemma of nonprofits in the agency theory framework. *Journal of Leadership, Accountability and Ethics*, 33–40.

Bourgeois, K. (2003). *NONPROFIT FINANCIAL STATEMENTS*. 50.

Bourgeois, L. J. (1981). On the Measurement of Organizational Slack. *The Academy of Management Review*, *6*(1), 29–39. https://doi.org/10.2307/257138

Bowman, W. (2002). The Uniqueness of Nonprofit Finance and the Decision to Borrow. *Nonprofit Management and Leadership*, *12*(3), 293–311. https://doi.org/10.1002/nml.12306

Bowman, W. (2011). Financial capacity and sustainability of ordinary nonprofits. *Nonprofit Management and Leadership*, *22*(1), 37–51. https://doi.org/10.1002/nml.20039

Boyes-Watson, T. (2019, July 16). Finally, the nonprofit sector will get the international financial standards we need. *Humentum*. https://humentum.org/blog-media/finally-the-nonprofit-sector-will-get-the-international-financial-standards-we-need/

Breen, O. B., Cordery, C. J., Crawford, L., & Morgan, G. G. (2018). Should NPOs Follow International Standards for Financial Reporting? A Multinational Study of Views. *VOLUNTAS: International Journal of Voluntary and Nonprofit Organizations*, *29*(6), 1330–1346. https://doi.org/10.1007/s11266-018-0040-9

Brenner, J. (2013, August 1). *Gifts-in-kind: What are they worth?* Journal of Accountancy. https://www.journalofaccountancy.com/issues/2013/aug/20137726.html

Burks, J. J. (2015). Accounting Errors in Nonprofit Organizations. *Accounting Horizons*, *29*(2), 341–361. https://doi.org/10.2308/acch-51017

Calabrese, T. D. (2011). Testing Competing Capital Structure Theories of Nonprofit Organizations. *Public Budgeting & Finance*, *31*(3), 119–143. https://doi.org/10.1111/j.1540-5850.2011.00989.x

Chabotar, K. J. (1989). Financial Ratio Analysis Comes to Nonprofits. *The Journal of Higher Education*, *60*(2), 188–208. https://doi.org/10.2307/1982176

Chen, X. (2021). Are Disasters Disastrous to Nonprofit Organizations? Investigating the Financial Implications of Hurricane Sandy for Nonprofits. *Nonprofit and Voluntary Sector Quarterly*, *51*(1), 53–75. https://doi.org/10.1177/0899764021998454

Connolly, C., & Dhanani, A. (2009). *Narrative reporting by UK charities* [Report]. Association of Chartered Certified Accountants. https://research-repository.st-andrews.ac.uk/handle/10023/3798

Connolly, C., Hyndman, N., & McConville, D. (2013). Conversion Ratios, Efficiency and Obfuscation: A Study of the Impact of Changed UK Charity Accounting Requirements on External Stakeholders. *VOLUNTAS: International Journal of Voluntary and Nonprofit Organizations*, *24*(3), 785–804. https://doi.org/10.1007/s11266-013-9371-8

Cordery, C. J., Fowler, C. J., & Morgan, G. G. (2016). The development of incorporated structures for charities: A 100-year comparison of England and New Zealand. *Accounting History*, *21*(2–3), 281–303. https://doi.org/10.1177/1032373216638104

Craig, R., Taonui, R., & Wild, S. (2012). The concept of taonga in Māori culture: Insights for accounting. *Accounting, Auditing & Accountability Journal*, *25*(6), 1025–1047. https://doi.org/10.1108/09513571211250233

Crawford, L., Morgan, Gareth G., Cordery, C., Breen, O., & Consultative Committee of Accountancy Bodies. (2014). *International financial reporting for the not-for-profit sector: A study commissioned by CCAB : final report*.

Ebrahim, A. (2010). The Many Faces of Nonprofit Accountability. In D. O. Renz & R. D. Herman (Eds.), *The Jossey&;#x02010;Bass Handbook of Nonprofit Leadership and Management* (pp. 102–123). John Wiley &;#38; Sons, Inc. https://doi.org/10.1002/9781119176558.ch4

Eftekhar, M., Li, H., Van Wassenhove, L. N., & Webster, S. (2017). The Role of Media Exposure on Coordination in the Humanitarian Setting. *Production and Operations Management*, *26*(5), 802–816. https://doi.org/10.1111/poms.12669

Elliott, J. (2015, July 21). *Confidential Documents: Red Cross Itself May Not Know How Millions Donated for Haiti Were Spent*. ProPublica. https://www.propublica.org/article/confidential-documents-red-cross-millions-donated-haiti?token=mELlroDoLRCGUryA5jeM152UwNqQZjyd

Elliott, J., & Sullivan, L. (2015, June 3). *How the Red Cross Raised Half a Billion Dollars for Haiti -and Built Six Homes*. ProPublica. https://www.propublica.org/article/how-the-red-cross-raised-half-a-billion-dollars-for-haiti-and-built-6-homes?token=3-o2TVyAqASwdG65PPRjM0V-pxKrSOzK

Ellwood, S., & Greenwood, M. (2016). Accounting for heritage assets: Does measuring economic value 'kill the cat'? *Critical Perspectives on Accounting*, *38,* 1–13. https://doi.org/10.1016/j.cpa.2015.05.009

Enke, S. (1970). Does Growth Mean Profits Too? *Business Economics, 5*(1), 92–95.

EUROSTAT. (2008). *NACE rev. 2*. Office for Official Publications of the European Communities.

Fitzpatrick, P. J. (1932). *A comparison of the ratios of successful industrial entreprises with those of failed companies: Vol. v.; 4°*. Washington : The Accountants Publ. Co, 1932.

Friedman, M. (1970, September 13). A Friedman doctrine-- The Social Responsibility Of Business Is to Increase Its Profits. *The New York Times*. https://www.nytimes.com/1970/09/13/archives/a-friedman-doctrine-the-social-responsibility-of-business-is-to.html

Hairston, C. F. (1985). Using Ratio Analysis for Financial Accountability. *Social Casework*, *66*(2), 76–82. https://doi.org/10.1177/104438948506600202

Heaslip, E. (2020, March 30). *Nonprofit, Not-for Profit & For-Profit Organizations Explained*. Https://Www.Uschamber.Com/Co. https://www.uschamber.com/co/co/start/strategy/nonprofit-vs-not-for-profit-vs-for-profit

Hendel, I. (1996). Competition Under Financial Distress. *The Journal of Industrial Economics*, *44*(3), 309–324. https://doi.org/10.2307/2950499

Herbert, S., & Wallace, J. (1998). Nonprofit housing: A study of costs and funding. *Shelter and Society: Theory, Research, and Policy for Nonprofit Housing*, 201–218.

Hopkins, B. R. (2011). *The Law of Tax-Exempt Organizations*. John Wiley & Sons.

Hudnall, D. (2016, May 11). *Accounting Errors Put the Carolina Theatre in a Hole. Can Dan Berman Dig It Out?* INDY Week. https://indyweek.com/api/content/3db587a2-60c8-57f1-b02d-15309f33d36f/

Jowitt, K. (1983). Soviet Neotraditionalism: The political corruption of a Leninist regime. *Soviet Studies*, *35*(3), 275–297. https://doi.org/10.1080/09668138308411481

Keating, E., Fischer, M., Gordon, T., & Greenlee, J. (2005). Assessing Financial Vulnerability in the Nonprofit Sector. *SSRN Electronic Journal*. https://doi.org/10.2139/ssrn.647662

Kent, R. (1993). *THE APPLICATION OF FINANCIAL RATIOS IN ANALYSING NONPROFIT ORGANISATIONS*. 21.

Kenton, W. (2022, March 15). *Nonprofit Organization (NPO)*. Investopedia. https://www.investopedia.com/terms/n/non-profitorganization.asp

Kilcullen, L., Hancock, P., & Izan, H. Y. (2007). User Requirements for Not-For-Profit Entity Financial Reporting: An International Comparison. *Australian Accounting Review*, *17*(41), 26–37. https://doi.org/10.1111/j.1835-2561.2007.tb00451.x

Konca, M. (2006). *Sivil toplum kuruluşları için muhasebe, finansman ve vergi uygulamalarına giriş*. İstanbul Bilgi Üniversitesi.

Lee, R. L., & Joseph, R. C. (2013). An examination of web disclosure and organizational transparency. *Computers in Human Behavior*, *29*(6), 2218–2224. https://doi.org/10.1016/j.chb.2013.05.017

Lopez-Arceiz, F. J., Bellostas, A. J., & Moneva, J. M. (2021). Accounting Standards for European Non-profits. Reasons and Barriers for a Harmonisation Process. *Accounting in Europe*, *18*(1), 43–74. https://doi.org/10.1080/17449480.2020.1795215

Lord, J., Landry, A., Savage, G. T., & Weech-Maldonado, R. (2020). Predicting Nursing Home Financial Distress Using the Altman Z-Score. *INQUIRY: The Journal of Health Care Organization, Provision, and Financing*, *57*, 0046958020934946. https://doi.org/10.1177/0046958020934946

Michalkova, L., Valašková, K., Frajtová Michalíková, K., & Drugau, A. C. (2018). The Holistic View of the Symptoms of Financial Health of Businesses. *Proceedings of the 3rd International Conference on Economic and Business Management (FEBM 2018), Honhot, China*, 20–22.

Morgan, G. G., & Fletcher, N. J. (2013). Mandatory Public Benefit Reporting as a Basis for Charity Accountability: Findings from England and Wales. *VOLUNTAS: International Journal of Voluntary and Nonprofit Organizations*, *24*(3), 805–830. https://doi.org/10.1007/s11266-013-9372-7

Musoke, S. (2020, December 7). Opinion: The need for harmonized financial reporting requirements for nonprofits. *Devex*. https://www.devex.com/news/sponsored/opinion-the-need-for-harmonized-financial-reporting-requirements-for-nonprofits-98709

Myser, S. (2016). *FINANCIAL HEALTH OF NONPROFIT ORGANIZATIONS*. 104.
Nongovernmental organization | Britannica. (n.d.). Retrieved 12 March 2022, from https://www.britannica.com/topic/nongovernmental-organization

O'Connor, M. C. (1973). On the Usefulness of Financial Ratios to Investors in Common Stock. *The Accounting Review, 48*(2), 339–352.

Ohlson, J. A. (1980). Financial Ratios and the Probabilistic Prediction of Bankruptcy. *Journal of Accounting Research*, *18*(1), 109–131. https://doi.org/10.2307/2490395

Opler, T. C., & Titman, S. (1994). Financial Distress and Corporate Performance. *The Journal of Finance*, *49*(3), 1015–1040. https://doi.org/10.1111/j.1540-6261.1994.tb00086.x

Padovani, E., Manes Rossi, F., & Orelli, R. L. (2010). The Use of Financial Indicators to Determine Financial Health of Italian Municipalities. *SSRN Electronic Journal*. https://doi.org/10.2139/ssrn.1679128

Paljug, K. (2020, February 13). *A Guide to Accounting for a Nonprofit Organization*. Business.Com. https://www.business.com/articles/nonprofits-guide-accounting/

Pandey, K. (2017, February 26). *Financial Management*. Lulu Publication.

Pedro M. Kono, D. B. A., & Barry Barnes, P. (2010). The Role of Finance in the Strategic-Planning and Decision-Making Process. *2010 Volume 13 Issue 1*, *1*. https://gbr.pepperdine.edu/2010/08/the-role-of-finance-in-the-strategic-planning-and-decision-making-process/

Peng, S., Kim, M., & Deat, F. (2019). The Effects of Nonprofit Reputation on Charitable Giving: A Survey Experiment. *VOLUNTAS: International Journal of Voluntary and Nonprofit Organizations*, *30*. https://doi.org/10.1007/s11266-019-00130-7

Perry, R. (1987). Survival is not enough—The case for profit. *The Journal of Mental Health Administration*, *14*(1), 37–39. https://doi.org/10.1007/BF02828430

Prentice, C. R. (2016a). Why So Many Measures of Nonprofit Financial Performance? Analyzing and Improving the Use of Financial Measures in Nonprofit Research. *Nonprofit and Voluntary Sector Quarterly*, *45*(4), 715–740. https://doi.org/10.1177/0899764015595722

Prentice, C. R. (2016b). Understanding Nonprofit Financial Health: Exploring the Effects of Organizational and Environmental Variables. *Nonprofit and Voluntary Sector Quarterly*, *45*(5), 888–909. https://doi.org/10.1177/0899764015601243

Puplampu, B. B. (2005). Toward a framework for understanding the distressed organization: Insights from practitioner-based organizational interventions in an emerging economy. *Consulting Psychology Journal: Practice and Research*, *57*(4), 246–258. https://doi.org/10.1037/1065-9293.57.4.246

Purnanandam, A. K. (2007). Financial Distress and Corporate Risk Management: Theory & Evidence. *SSRN Electronic Journal*. https://doi.org/10.2139/ssrn.782425

Ravinder, Dr. D., & Anitha, M. (2013). Financial Analysis – A Study. *IOSR Journal of Economics and Finance*, *2*(3), 10–22. https://doi.org/10.9790/5933-0231022

Reck, J. L., & Lowensohn, S. L. (2014). *Accounting for governmental & nonprofit entities* (Seventeenth Edition). McGraw-Hill Education.

Reheul, A.-M., Van Caneghem, T., & Verbruggen, S. (2014). Financial Reporting Lags in the Non-profit Sector: An Empirical Analysis. *VOLUNTAS: International Journal of Voluntary and Nonprofit Organizations*, *25*(2), 352–377. https://doi.org/10.1007/s11266-012-9344-3

Salamon, L. M., & Anheier, H. K. (1992). In search of the non-profit sector II: The problem of classification. *Voluntas*, *3*(3), 267–309. https://doi.org/10.1007/BF01397460

Salamon, L. M., & Anheir, H. K., coaut. (1996). *The international classification of nonprofit organizations ICNPO-Revision 1, 1996*. The Johns Hopkins University Institute for Policy Studies.

Schatteman, A. (2013). Nonprofit Accountability: To Whom and for What? An Introduction to the Special Issue. *International Review of Public Administration*, *18*(3), 1–6. https://doi.org/10.1080/12294659.2013.10805260

Scheetz, A., Smalls, T. D. W., Wall, J., & Wilson, A. B. (2020). Do Employee Fraud Reporting Intentions Differ between For-Profit and Nonprofit Organizations? *Journal of Governmental & Nonprofit Accounting*, *9*(1), 94–117. https://doi.org/10.2308/JOGNA-18-008

Seyam, Y., Seyam, O., Salama, N., & Seyam, A. (2018). An Overview of Fraud in Nonprofit Organizations and the Appropriate Approach to Prevent It. *International Journal of Accounting and Finance Studies*, *1*, 183. https://doi.org/10.22158/ijafs.v1n2p183

Smart, B. (1992). Industry as a metabolic activity. *Proceedings of the National Academy of Sciences*, *89*(3), 804–806. https://doi.org/10.1073/pnas.89.3.804

Smith, D. H., Stebbins, R. A., & Dover, M. A. (2006). *A dictionary of nonprofit terms and concepts*. Indiana University Press.

TCMB (CBRT: Central Bank of the Republic of Turkey), (2020). Company Accounts Between 2009-2019, URL: https://www3.tcmb.gov.tr/sektor/#/en/S/94/activities-of-membership-organizations, - Accessed on 27.12.2020

TCMB (CBRT: Central Bank of the Republic of Turkey), (2022). Company Accounts Between 2009-2020, URL: https://www3.tcmb.gov.tr/sektor/#/en/S/94/activities-of-membership-organizations, - Accessed on 05.03.2022

Tevel, E., Katz, H., & Brock, D. M. (2015). Nonprofit Financial Vulnerability: Testing Competing Models, Recommended Improvements, and Implications. *VOLUNTAS: International Journal of Voluntary and Nonprofit Organizations*, *26*(6), 2500–2516. https://doi.org/10.1007/s11266-014-9523-5

Toepler, S., Salamon, L., Anheier, H., Sokolowski, S., & List, R. (1999). *Global Civil Society: Dimensions of the Nonprofit Sector*.

Trussel, J. M. (2002). Revisiting the Prediction of Financial Vulnerability. *Nonprofit Management and Leadership*, *13*(1), 17–31. https://doi.org/10.1002/nml.13103

Tuckman, H. P., & Chang, C. F. (1991). A Methodology for Measuring the Financial Vulnerability of Charitable Nonprofit Organizations. *Nonprofit and Voluntary Sector Quarterly*, *20*(4), 445–460. https://doi.org/10.1177/089976409102000407

Turetsky, H., & McEwen, R. (2001). An Empirical Investigation of Firm Longevity: A Model of the Ex Ante Predictors of Financial Distress. *Review of Quantitative Finance and Accounting*, *16*, 323–343. https://doi.org/10.1023/A:1011291425075

Van Gestel, T., Baesens, B., Suykens, J., Van den Poel, D., Baestaens, D.-E., & Willekens, M. (2006). Bayesian kernel based classification for financial distress detection. *European Journal of Operational Research*, *172*, 979–1003. https://doi.org/10.1016/j.ejor.2004.11.009

Weikart, L. A., & Chen, G. G. (2021). *Budgeting and Financial Management for Nonprofit Organizations: Using Money to Drive Mission Success*. Waveland Press.

Wells, M. K. (2006). *Understanding Nonprofit Finances*. Continuing Education Press.

Whitaker, R. B. (1999). The early stages of financial distress. *Journal of Economics and Finance*, *23*(2), 123–132. https://doi.org/10.1007/BF02745946

Williams, A. (2010). New and Improved?: A Case Study of Nonprofit Policy Governance. *Human Organization*, *69*(3), 295–305. https://doi.org/10.17730/humo.69.3.t418t570x1v21782

Yermack, D. (2017). Donor governance and financial management in prominent US art museums. *Journal of Cultural Economics*, *41*(3), 215–235. https://doi.org/10.1007/s10824-017-9290-4

Yuchtman, E., & Seashore, S. E. (1967). A System Resource Approach to Organizational Effectiveness. *American Sociological Review*, *32*(6), 891–903. https://doi.org/10.2307/2092843

APPENDICES

Appendix A: BALANCE SHEETS

94-Activities of Membership Organizations
BALANCE SHEET (TRY THOUSANDS)

ASSETS	2017	2018	2019
I-CURRENT ASSETS	**448.308,2**	**504.418,3**	**618.696,2**
A-Liquid Assets	**40.394,9**	**29.392,2**	**31.944,9**
1- Cash	1.318,7	936,6	876,8
2- Checks Received	543,0	736,6	500,7
3- Banks	37.393,3	28.018,5	29.963,3
4- Checks Given and Payment Orders (-)	833,4	1.550,3	856,2
5- Other Liquid Assets	1.973,4	1.250,9	1.460,3
B-Marketable Securities	**960,8**	**14,2**	**14,2**
1-Securities	0,0	6,2	6,2
2-Private Sector Bonds, Notes & Bills	939,4	7,8	7,8
3-Public Sector Bonds, Notes & Bills	0,0	0,0	0,0
4-Other Marketable Securities	21,4	0,2	0,2
5-Provisions for Marketable Securities (-)	0,0	0,0	0,0
C-Short-Term Trade Receivables	**43.780,6**	**34.032,5**	**42.466,3**
1-Customers	35.858,0	29.373,7	36.236,0
2-Notes Receivable	4.019,9	3.547,0	2.807,7
3-Discount on Notes Receivable (-)	0,0	0,0	0,0
4-Unearned Financial Leasing Interest (-)	0,0	0,0	0,0
5-Deposits and Guarantees Given	313,7	333,7	404,8
6-Other Short-Term Trade Receivables	3.064,6	495,5	2.734,5
7-Doubtful Trade Receivables	1.957,9	1.749,9	1.874,1
8-Provis. for Doubtful Trade Receivables (-)	1.433,4	1.467,3	1.590,8
D-Other Short-Term Receivables	**317.114,3**	**417.471,9**	**520.177,9**
1- Receivables from Shareholders	7.424,2	4.776,9	4.940,1
2- Receivables from Participations	406,7	360,6	238,3
3- Receivables from Affiliated Enterprises	301.895,2	407.956,4	509.783,6
4- Receivables from Employees	58,4	61,6	72,2
5- Other	7.252,7	4.239,2	5.066,5
6- Discount on Other Notes Receivable (-)	0,0	0,0	0,0
7- Other Doubtful Receivables	77,2	77,2	77,2
8- Provis. for Other Doubtful Receivables (-)	0,0	0,0	0,0
E- Inventories	**34.107,9**	**15.305,0**	**14.438,3**
1- Raw Materials & Consumables	2.177,1	443,6	764,9
2- Work in Progress	11.626,7	0,0	0,0
3- Finished Goods	13,0	610,6	684,9
4- Merchandise	14.152,9	12.342,3	11.981,5
5- Other Inventories	886,0	617,5	54,3
6- Provisions for Inventories (-)	0,0	0,0	0,0
7- Advances on Purchase Orders	5.252,2	1.291,1	952,6
F- Constr.& Restor.Costs Spread Over Yrs.	**333,2**	**0,0**	**0,0**
1-Constr.&Restor.Costs Spr. Over Yrs.	328,2	0,0	0,0

2-Constr.Costs Reval.Adjust.to Inflation Spr.Over Yrs.	0,0	0,0	0,0
3-Advances to Subcontractors	5,0	0,0	0,0
G- Prepaym.& Accr. Inc.for the Next Months	**572,0**	**638,8**	**627,6**
1- Prepayments for the Next Months	463,0	577,3	364,1
2- Accrued Income	109,1	61,6	263,5
H- Other Current Assets	**11.044,3**	**7.563,7**	**9.027,1**
1- V.A.T.Carried to the Next Period	9.453,6	6.240,1	7.227,9
2- V.A.T. Paid	8,0	15,4	147,6
3- Other V.A.T	4,9	39,4	41,4
4- Prepaid Taxes and Funds	691,6	216,1	429,3
5- Business Related Advances	356,2	471,1	743,5
6- Advances to employees	270,3	251,6	158,2
7- Stock Taking and Receiving Shortages	255,3	196,3	198,9
8- Other	4,4	133,7	80,3
9- Provisions for Other Current Assets (-)	0,0	0,0	0,0
II- FIXED ASSETS	**82.037,6**	**66.681,4**	**70.087,8**
A- Long-Term Trade Receivables	**1.704,0**	**140,1**	**354,5**
1- Customers	1.532,7	0,7	0,0
2- Notes Receivable	7,4	7,4	7,4
3- Discount on Notes Receivable (-)	0,0	0,0	0,0
4- Unearned Financial Leasing Interest (-)	0,0	0,0	0,0
5- Deposits and Guarantees Given	163,9	132,0	347,1
6- Provisions for Doubtful Trade Receivables (-)	0,0	0,0	0,0
B- Other Long-Term Receivables	**1.560,7**	**2.093,8**	**920,2**
1- Receivables from Shareholders	776,0	30,0	138,3
2- Receivables from Participations	426,7	1.593,3	495,7
3- Receivables from Affiliated Enterprises	0,0	103,8	3,8
4- Receivables from Employees	0,0	2,3	2,0
5- Other	358,0	364,3	280,3
6- Disc.on Oth.Short-Term Notes Receivable (-)	0,0	0,0	0,0
7- Provis. for Other Doubtful Receivables (-)	0,0	0,0	0,0
C- Financial Fixed Assets	**2.720,3**	**2.802,9**	**3.353,2**
1- Non-Marketable Securities	10,6	11,6	13,8
2- Provis.for non-Marketable Securities (-)	0,0	0,0	0,0
3- Participations	190,4	260,8	714,3
4- Subscribed Capital to Participations (-)	12,5	0,0	31,6
5- Provis.for Capital Share in Participations (-)	0,0	0,0	0,0
6- Affiliated Enterprises	2.513,6	2.634,4	2.754,4
7- Subscribed Capital to Affili. Enterprises (-)	37,5	104,0	100,0
8- Provi.for Capital Share in Affili.Enterp. (-)	0,0	0,0	0,0
9- Other Financial Fixed Assets	119,4	0,1	2,3
10- Provi. for Other Financial Fixed Assets (-)	63,8	0,0	0,0
D- Tangible Fixed Assets	**68.506,0**	**54.964,3**	**58.986,5**
1- Land	5.043,0	1.906,5	2.030,1
2- Land Improvements	439,8	67,5	207,5
3- Buildings	33.402,7	25.666,0	27.353,7
4- Machinery, Plant & Equipment	14.071,1	12.284,8	14.308,1
5- Motor Vehicles	13.763,6	9.115,5	10.191,0
6- Furniture & Fixtures	14.550,8	12.333,0	13.504,2
7- Other Tangible Fixed Assets	670,5	329,1	455,7
8- Accumulated Depreciation (-)	15.292,0	9.126,7	11.347,8
9- Assets in Construction	1.360,7	2.109,7	1.098,9
10- Advances Paid	495,7	278,9	1.185,0
E- Intangible Fixed Assets	**1.983,3**	**1.864,2**	**2.276,3**
1- Know-How	1.577,8	1.814,3	2.400,0
2- Goodwill	0,0	0,0	0,0

3- Formation and Organisation Expenses	94,4	108,5	122,5
4- Research and Development Expenses	0,0	0,0	0,0
5- Special Expenses	1.714,1	1.573,4	1.829,0
6- Other Intangible Fixed Assets	296,1	225,8	240,5
7- Accumulated Depreciation (-)	1.718,0	1.876,6	2.520,8
8- Advances Paid	18,9	18,8	205,1
F- Assets Subject to Depletion	**0,1**	**0,3**	**11,6**
1- Exploration Expenses	0,0	0,0	0,0
2- Preparation and Development Expenses	0,0	0,0	0,0
3- Other Assets subject to Depletion	0,0	0,0	0,0
4- Accumulated Depletion (-)	0,0	0,0	0,0
5- Advances Paid	0,1	0,3	11,6
G-Prepaym.& Accrued Inc. for the Next Yrs.	**5.089,2**	**4.245,5**	**3.741,9**
1- Prepayments for the Next Years	5.060,3	4.245,4	3.741,9
2- Accrued Income	28,9	0,1	0,0
H- Other Long-Term Assets	**474,0**	**570,2**	**443,7**
1- V.A.T. Deductable in the Following Years	0,4	111,4	0,4
2- Other V.A.T.	16,3	16,3	0,4
3- Inventory Held for the Next Years	0,0	0,0	0,0
4- Inventories and Tang.Fixed Assets to be Sold	451,0	440,7	446,4
5- Prepaid taxes and funds	6,3	1,9	2,2
6- Other	0,0	0,0	0,0
7- Provisions for inventories (-)	0,0	0,0	0,0
8- Accumulated depreciation (-)	0,0	0,0	5,7
9- Suspence Account	0,0	0,0	0,0
TOTAL ASSETS	**530.345,7**	**571.099,7**	**688.784,0**

LIABILITIES	**2017**	**2018**	**2019**
I- SHORT-TERM LIABILITIES	**387.975,5**	**481.452,4**	**591.065,6**
A- Financial Liabilities	**3.408,7**	**2.434,1**	**2.608,5**
1- Bank Loans	3.097,7	2.178,3	2.013,6
2- Financial Leasing Payables	0,0	0,0	0,0
3- Deferred Financial Leasing Payable Costs (-)	0,0	0,0	0,0
4- Princip.Installm.& Int.Paym.of Long-Term Loans	257,2	208,3	208,3
5- Principal Installm.& Int.Paym.of Bonds	0,0	0,0	0,0
6- Commercial Papers Issued	0,0	0,0	0,0
7- Other Securities Issued	0,0	0,0	0,0
8- Adjust.for Secur.Issued under Par Value (-)	0,0	0,0	0,0
9- Other Financial Liabilities	53,8	47,5	386,6
B- Trade Debts	**24.553,1**	**17.752,8**	**18.822,0**
1- Creditors	17.485,8	14.542,0	16.223,1
2- Notes Payable	2.199,6	2.057,6	1.039,3
3- Discount on Notes Payable (-)	0,0	0,0	0,0
4- Deposits and Guaranties Received	60,6	50,5	57,0
5- Other Trade Debts	4.807,1	1.102,7	1.502,6
C- Other Short-Term Debts	**340.341,4**	**442.158,3**	**549.414,9**
1- Amounts Owed to Shareholders	18.484,5	14.453,7	16.497,8
2- Amounts Owed to Participations	710,5	746,9	1.200,0
3- Amounts Owed to Affiliated Enterprises	310.128,6	414.663,8	518.813,2
4- Amounts Owed to Employees	3.594,9	4.904,6	4.530,4
5- Other	7.423,1	7.389,3	8.373,6

6- Disc.on Oth.Short-Term Notes Payable (-)	0,1	0,0	0,0
D- Advances Received	**8.379,3**	**8.113,4**	**8.669,4**
1- Advances Received on Purchase Orders	7.236,7	7.174,5	8.101,4
2- Other Advances Received	1.142,6	938,8	568,0
E- Remunerations Spread Over Years	**0,0**	**0,0**	**0,0**
1- Advances to Constr.&Restor.Costs Spr. Over Yrs.	0,0	0,0	0,0
2- Constr.Costs Reval.Adjust.to Inflation Spr.Over Yrs.	0,0	0,0	0,0
F- Taxes and Other Liabilities Payable	**9.773,4**	**9.222,0**	**9.391,3**
1- Taxes and Funds Payable	3.291,7	4.975,3	5.279,8
2- Social Security Costs Payable	5.115,0	3.072,7	3.302,2
3- Taxes & Oth.Liab.that are Overd.or Deferred	723,6	902,7	486,8
4- Other Liabilities Payable	643,2	271,4	322,5
G- Provisions for Liabilities and Charges	**195,4**	**582,3**	**490,4**
1- Provisions for Inc.Tax & Oth.Liab.to Gov.	363,6	738,0	690,7
2- Prepaid Inc.Tax & Other Liab.to Gov.(-)	213,1	225,5	274,0
3- Provisions for Severance Payments	0,0	0,0	0,0
4- Provisions for Costs	0,0	0,0	0,0
5- Other Provisions for Liabilities and Charges	45,0	69,8	73,7
H- Defer.Inc.& Accr.Exp.for the Next Months	**1.049,4**	**825,4**	**1.313,3**
1- Deferred Income for the Next Months	901,1	640,6	1.196,1
2- Accrued Expenses	148,3	184,7	117,2
I- Other Short-Term Liabilities	**274,8**	**364,1**	**355,8**
1- V.A.T. Calculated	3,1	7,5	0,4
2- Other V.A.T.	0,0	0,0	0,0
3- Main and Branch Offices' Current Account	257,1	344,1	343,0
4- Stock Taking and Receiving Surpluses	14,5	12,5	12,3
5- Other	0,0	0,0	0,0
II- LONG-TERM LIABILITIES	**24.263,8**	**15.429,7**	**15.529,3**
A- Financial Liabilities	**12.853,0**	**5.454,3**	**2.758,7**
1- Bank Loans	12.853,0	5.454,3	2.758,7
2- Financial Leasing Payables	0,0	0,0	0,0
3- Deferred Financial Leasing Payable Costs (-)	0,0	0,0	0,0
4- Bonds Issued	0,0	0,0	0,0
5- Other Securities Issued	0,0	0,0	0,0
6- Adjust.for the Secur.Issued Under Par Value (-)	0,0	0,0	0,0
7- Other Financial Liabilities	0,0	0,0	0,0
B- Trade Debts	**648,8**	**495,5**	**506,1**
1- Creditors	477,0	260,1	260,1
2- Notes Payable	50,0	232,6	246,0
3- Discount on Notes Payable (-)	0,0	0,0	0,0
4- Deposits and Guaranties Received	0,0	2,8	0,0
5- Other Trade Debts	121,8	0,0	0,0
C- Other Long-Term Debts	**8.240,5**	**7.032,0**	**9.751,9**
1- Amounts Owed to Shareholders	6.945,8	5.541,6	7.691,4
2- Amounts Owed to Participations	506,8	139,1	139,1
3- Amounts Owed to Affiliated Enterprises	400,6	351,6	351,7
4- Other	204,1	914,2	391,7
5- Disc. on Oth.Short-term Notes Payable (-)	0,0	0,0	0,0
6- Deferred & Scheduled Paym.to Gov.	183,2	85,5	1.178,1
D-Advances Received	**53,0**	**0,0**	**80,3**
1- Advances Received on Purchase Orders	53,0	0,0	0,0
2- Other Advances Received	0,0	0,0	80,3
E- Provisions for Liabilities and Charges	**143,4**	**121,9**	**177,7**
1- Provisions for Severance Payments	0,0	0,0	0,0
2- Other Provisions	143,4	121,9	177,7
F- Defer.Inc.& Accr.Exp.for the Next Yrs.	**1.197,9**	**1.210,6**	**1.124,8**

1- Deferred Income	1.197,9	1.210,6	1.124,8
2- Accrued Expenses	0,0	0,0	0,0
G- Other Long-Term Liabilities	**1.127,2**	**1.115,4**	**1.129,7**
1- V.A.T. Deferred to the Next Years	0,0	0,0	0,0
2- Shares in the Plant and Equipment	0,0	0,0	0,0
3- Other	1.127,2	1.115,4	1.129,7
V-EQUITY	**118.106,5**	**74.217,6**	**82.189,2**
A- Paid-in Capital	**58.054,6**	**49.648,7**	**48.492,6**
1- Subscribed Capital	56.967,9	49.659,6	48.558,4
2- Subscribed Capital Uncalled (-)	564,5	71,5	114,3
3- Revaluation Adjustment to Capital (+)	1.651,2	60,6	48,5
4- Revaluation Adjustment to Capital (-)	0,0	0,0	0,0
B- Capital Reserves	**16.044,4**	**14.912,1**	**16.105,0**
1- Share Premium Account	0,0	0,0	0,0
2- Gains From Reedemption of Shares	0,0	0,0	0,0
3- Revaluation of Tangible Fixed Assets	241,9	0,0	1.329,8
4- Revaluation of Participations	0,0	0,0	0,0
5- Provisions for Commodities Recorded	109,0	0,0	0,0
6- Provisions for Machinery and Equipment	0,0	0,0	0,0
7- Other Capital Reserves	15.693,6	14.912,1	14.775,2
C- Reserves from Retained Earnings	**11.675,1**	**6.671,5**	**11.906,8**
1- Legal Reserves	1.584,9	1.692,1	2.026,2
2- Reser.Provided for by the Artic.of the Assoc.	1.880,7	1.867,1	2.151,8
3- Extraordinary Reserves	128,2	133,8	190,5
4- Other Reserves	507,4	36,0	4.048,1
5- Special Funds	7.573,9	2.942,5	3.490,1
D- Profit Brought Forward	**95.199,6**	**77.592,6**	**93.241,3**
E- Loss Brought Forward (-)	**(51.198,2)**	**(75.959,8)**	**(90.209,4)**
F- Net Profit or Loss for the Financial Year	**(11.669,0)**	**1.352,4**	**2.652,9**
1- Profit for the Financial Year	6.353,1	8.860,7	9.902,3
2- Loss for the Financial Year (-)	18.022,1	7.508,3	7.249,4
TOTAL LIABILITIES	**530.345,7**	**571.099,7**	**688.784,0**
Number of Organizations	**304**	**205**	**194**

Source: TCMB, accessed on 27.12.2020

Appendix B: INCOME STATEMENTS

94-Activities of membership organizations

INCOME STATEMENT (TRY THOUSANDS)

	2017	2018	2019
A-GROSS SALES	**239.108,9**	**207.338,3**	**252.925,6**
1-Domestic Sales	215.316,5	185.685,5	230.184,0
2-Exports	635,8	1.813,2	456,5
3-Other	23.156,6	19.839,6	22.285,1
B-DEDUCTIONS FROM SALES (-)	**1.939,8**	**1.485,3**	**4.344,1**
1-Sales Returns (-)	1.843,9	1.469,7	4.186,0
2-Sales Discounts (-)	81,4	15,6	158,1
3-Other Deductions (-)	14,6	0,0	0,0
C-NET SALES	**237.169,1**	**205.853,0**	**248.581,5**
D-COST OF GOODS SOLD (-)	**216.470,0**	**173.883,3**	**213.700,6**
1-Cost of Finished Goods Sold (-)	9.237,5	6.430,5	3.061,6
2-Cost of Merchandise Sold (-)	91.464,0	67.363,9	89.765,9
3-Cost of Services Sold (-)	115.674,0	100.044,8	120.559,8
4-Other Cost of Sales (-)	94,5	44,1	313,2
GROSS PROFIT OR LOSS	**20.699,1**	**31.969,8**	**34.880,9**
E-OPERATING EXPENSES (-)	**46.936,7**	**37.533,7**	**39.289,3**
1-Research and Development Expenses (-)	0,0	6,0	0,0
2-Marketing, Selling and Distribution Expenses (-)	1.428,3	1.444,2	1.643,9
3-General Administration Expenses (-)	45.508,4	36.083,5	37.645,4
OPERATING PROFIT OR LOSS	**(26.237,6)**	**(5.563,9)**	**(4.408,4)**
F-INCOME FROM OTHER OPERATIONS	**15.009,3**	**9.614,9**	**10.981,7**
1-Dividends from Participations	339,8	330,6	242,3
2-Dividends from Affiliated Enterprises	0,0	0,0	0,0
3-Interest Income	2.982,4	1.325,4	1.624,0
4-Commissions	64,2	0,8	0,0
5-Provisions that are Cancelled	545,7	411,3	1.868,0
6-Income from Sale of Securities	0,0	2,1	0,1
7-Exchange Profits	344,3	233,3	114,9
8-Discount Income	9,9	0,0	0,0
9-Inflation Adjustment Profits	0,0	0,0	0,0
10-Other Income	10.723,1	7.311,3	7.132,4
G-EXPENSES FROM OTHER OPERATIONS (-)	**1.658,7**	**1.706,0**	**2.622,0**
1-Commissions (-)	18,8	6,2	5,6
2-Provision Expenses (-)	883,6	838,7	1.729,7
3-Loss from Sale of Securities (-)	0,0	0,0	0,0
4-Exchange Losses (-)	22,7	114,0	41,0
5-Discount Costs (-)	0,0	0,0	0,0
6-Inflation Adjustment Losses (-)	0,0	0,0	0,0
7-Other Expenditures (-)	733,6	747,0	845,7
H-FINANCING EXPENSES (-)	**1.238,7**	**973,8**	**1.037,0**
1-Short-term Financing Expenses (-)	960,9	834,7	928,5
2-Long-term Financing Expenses (-)	277,8	139,2	108,5
PROFIT BEFORE EXTRAORDINARY ITEMS	**(14.125,7)**	**1.371,2**	**2.914,3**
I-EXTRAORDINARY INCOME AND PROFITS	**3.866,3**	**2.535,6**	**2.025,7**
1-Profits and Income from Previous Period	271,2	500,5	0,0
2-Other Extraordinary Profits and Income	3.595,1	2.035,1	2.025,7

J-EXTRA ORDINARY EXPENSES AND LOSSES (-)	**1.046,0**	**1.816,4**	**1.596,5**
1-Losses from non-Operating Parts (-)	71,3	120,0	128,4
2-Losses from Previous Periods (-)	97,2	400,8	120,8
3-Other Extraordinary Expenses (-)	877,6	1.295,6	1.347,2
PROFIT OR LOSS BEFORE TAXES	**(11.305,4)**	**2.090,4**	**3.343,5**
K-PROVISIONS FOR INC.TAX & OTH.LIAB.TO GOV.	**363,6**	**738,0**	**690,7**
NET PROFIT OR LOSS FOR THE FINANCIAL YEAR	**(11.669,0)**	**1.352,4**	**2.652,9**
Number of Organizations	**304**	**205**	**194**

Source: TCMB, accessed on 27.12.2020

CURRICULUM VITAE

Ardıl Yılmaz Kaya graduated from the Business Administration Bachelor’s Program of the İstanbul University in 2019. He has been working as a Research Assistant at the Business Administration Department of the Turkish-German University since November 2020.