

29. Otter Mountain Theater (OMT) 52

Otter Mountain Theater is a nonprofit social enterprise that was founded in 1965. Originally started as a community theater in which actors and musicians were volunteers, the theater gained a reputation as an organization that put on excellent shows and in which several performers went on to become professional actors. In 2015 the new director of OMT converted the organization to a civic theater, in which the city government pays part of the operating costs, and the theater uses a mix of professional, semi-professional, and volunteer actors and musicians. The increasingly ambitious performances and the need to pay some of its actors dramatically increased OMT's costs, but OMT has been able to put on major plays, and annual audience attendance rose over the years. In 2018, OMT started offering customers memberships, which helped provide additional cash flow in the preparation period before a new play opened.

In the last month, however, local media revealed a shocking report on OMT's debt levels, and the director resigned. The latest play was scheduled to open in two months, but the play's publisher is refusing to send scripts to OMT until it is paid. OMT has done well at increasing its individual donations rather than relying as much on government funding, but $\frac{1}{3}$ of its current assets are donations yet to be received. The new director Amy is seeking a \$150 000 loan from the city, with interest payments delayed for one year, as well as overdrafts on favorable terms with a local bank. A member of the city council has told Amy privately that even if the city approves the loan, they will put several difficult requirements on OMT regarding its performance schedule, cost control, and much more direct oversight of its operations and finances. Amy is also looking into crowdfunding by selling advanced tickets to the upcoming show, and OMT merchandise such as shirts and signs showing support for the theater. OMT leases its theater building from the city, which is in need of significant upgrades; the previous director was working on a fundraising campaign to construct its own theater, and had projected a payback period of ten years, but Amy is pausing that campaign indefinitely.

Below are selected pieces of financial information from the last two annual profit and loss account and balance sheets:

	Prior financial year	Latest financial year
Sales	906 000	809 000
Donations and government funding (revenue)	580 000	455 000
Cost of sales and other direct costs	91 500	98 100
Expenses		
- Wages and salaries	899 000	852 000
- Consulting and professional fees	12 800	104 000
- Advertising	67 000	84 000
- Administrative and other expenses	168 000	294 000
Current ratio	1.24:1	1.31:1

Question	Marks
A. Define the term overdrafts.	2
B. With reference to OMT, distinguish between capital and revenue expenditure.	4
C. Explain two reasons why OMT's additional financing options may be limited due to its non-profit social enterprise status.	4
D. Define the term overheads.	2
E. Calculate the value of OMT's gross profit in each of the two financial years shown.	2
F. Calculate OMT's profit margin in each of the two financial years shown.	2
G. Comment on two aspects of OMT's financial performance that can be seen in the case study given.	4
H. In addition to what is mentioned in the case study, explain two additional revenue streams that may be possible for OMT.	4
I. Explain two challenges in OMT improving its profit margin.	4
J. Explain what an increase in OMT's long term loans will do to its return on capital employed (ROCE), if all else is held equal.	2
K. Explain one way in which OMT could attempt to improve its working capital cycle, and one drawback to that method.	4
L. With reference to OMT, distinguish between cash flow and profit (surplus in this case).	4
M. Discuss the challenges in OMT obtaining sustainable external financing to improve its ability to function.	10