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NONPROFIT

Financial Quicksand for Nonprofits

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From time to time, we report on the findings of surveys in the nonprofit sector including those related to financial issues. It's important to stray, occasionally, from the (often confining) prism of commentary by experts, academics, and advisors to hear what the people in the trenches have to say. For instance, we've posted about the results of **BoardSource's 2017 "Leading With Intent"** Survey as well as the invitation to participate in the upcoming 2020 Survey.

Last year, the Nonprofit Finance Fund published its eighth ***Nonprofit Sector Survey*** of philanthropy leaders around the nation. Respondents included **some 3,369 mid- and large-size nonprofits** in all 50 states. The data, including financial information, was timely when it was published in May 2018 – based on responses on the internet in January and February of that same year – and holds up well even now.

That's the opinion of Ger Tonnessen of Colorado-based **XLedger**, a cloud Enterprise Resource Planning (ERP) firm that specializes in organizations with complex financial management needs. In ***THESE 4 FINANCIAL THREATS COULD SINK YOUR NONPROFIT. HOW TO OVERCOME THEM*** (June 4, 2019), he has some thoughts on the responses to a particular question; that is, which are the respondents' **four main financial concerns.**

We have a few thoughts of our own to add:

Top Four Financial Concerns

Mr. Tonnessen explains that "nonprofit executives **share four top-of-mind financial concerns**: financial sustainability, effective funding, unrestricted revenue, and competitive pay." He believes that the first worry is "inseparable" from the second.

Financial Sustainability

In **The Hidden Threat To Successful Nonprofits** (October 3, 2017), Michael Etzel of Bridgespan and Hilary Pennington of the Ford Foundation report on a Bridgespan review of almost 300 "name-brand nonprofits with big budgets and successful programs – which together account for a third of the top 15 US foundations' spending." The bottom-line finding is that "shaky [financial] foundations are, in fact, the rule" rather the exception.

Over half of the organizations – 53% – had " **recurring or chronic budget deficits** in at least two of the past five years." Some "40 percent had fewer than than three months of reserves to cushion all-too-frequent shortfalls." Thirty of the 275 responding organizations were "technically insolvent" since they had no reserves at all.

Mr. Etzel and Ms. Pennington observed that "these numbers **are alarming, but ultimately understandable"** because "nonprofits and donors" alike "instinctively" allocate money to programs, often shortchanging infrastructure and overall financial health and stability. (Eradicating the destructive "overhead myth" means not just funding so-called current overhead along with direct program items, but also investing in the building and stabilizing the foundation of the organization for the long haul.)

Mr. Tonnessen explains as well that "long-term **financial planning** requires **long-term funding**. That requires "predictable multi-year revenue"; so the first "concern" – "financial stability" – is " **inseparable" from the second one:** "effective funding."

Effective Funding

The revenue landscape for nonprofits in 2019 is – to say the least – volatile.

According to the most recent Giving USA report, there are troubling trends particularly in connection with individual donations. While there was a slight rise in overall giving, the total number of individual givers has declined. As predicted, the dramatic change in the tax code in late 2017 – expanding the standard deduction to many more taxpayers who previously were itemizers – has had a worrisome, negative, effective on charitable giving.

"Along with these shifts," explains Mr. Tonnessen, "**so-called 'impulse giving'** has **boomed** in the wake of mobile and social technologies. Although 85% of givers say they rely on performance data when donating, only 3% actually do; and even deliberate giving is bias-prone." Nonprofits can **use "behavioral 'nudges'" to help this along**, but "… impulse donations **can't provide** long-term certainty."

We've discussed the phenomenon of "surge" or "rage" giving in a number of past posts since the 2016 presidential election. More than a few nonprofits around the nation have benefited from these unexpected buckets of money falling out of the sky. But not only is it an unreliable funding stream over the long course, it also can sometimes create unexpected problems for the recipient-organizations. Many organizations don't have the capability of properly dealing with a sudden influx of cash.

Another source of recent instability in the nonprofit sector arises from the dramatically different funding priorities of the current Administration from past years. Many organizations were jolted by news of severe funding cuts – sometimes announced and implemented abruptly.

Unrestricted Revenue

"In the past year," writes Ger Tonnassen, "changes to GAAP reporting standards have **highlighted a thorny issue: restricted funding**." Conceptually, this financial worry of nonprofit leaders is related to the first two – that is, financial sustainability and effective funding – although not as "inseparable" from them as they are to each other.

Only about **one-fifth of all nonprofit funding** in the U.S. is unrestricted. Some 80% of all donations "come with **(often absurdly) specific requirements** for how organizations can spend them. Multi-year grants often impose the most restrictive conditions." Sometimes, the restrictions require funding for direct programming only. As a result, explicitly or not, overhead spending is limited, and the "**starvation cycle**" continues to devour nonprofits' long-term sustainability. This is the unfortunate result even when the organization's leaders understand this problem but are helpless in the face of unfortunate donor restrictions.

"Needless to say, **most nonprofit leaders prefer no-strings-attached giving**. Restricted donations **complicate** planning, hobble cash flow, and limit capital investment. Although there is some movement in the nonprofit sector to "**change that botched financing structure,**" in the meantime, organizations must figure out ways to survive.

Competitive Pay

Competitive pay is a complex, often contradictory, problem for nonprofits. On the one hand, recruiting good talent is recognized as a key factor in steering a nonprofit to success, but "nonprofit leaders still **face an uphill battle** to hire the right talent. Donor and board scrutiny impose often-unrealistic expectations for payroll and overhead."

There's some interesting – and unexpected – news on that front, though. While there is a prevalent belief that (generally) nonprofit pay levels always come in below for-profit compensation, that is not always the case. In ***Nonprofit Workforce Study Finds Strengths in Growth, Pay, and Resilience*** (February 7, 2019) Steve Dubb of *The Nonprofit Quarterly* discusses the findings of ***The 2019 Nonprofit Employment Report*** from the Johns Hopkins Center for Civil Society Studies (January 2019). While the most recent data is from 2016 (and the report includes coverage of years back to 2006), the authors remain confident that the findings remain relevant. "One interesting report finding is that, within their industries, nonprofit workers typically out-earn their for-profit brethren, as shown in **Figure 8**."

"For instance, an average nonprofit worker in ambulatory health" has a "**24 percent … wage advantage**" over a "person employed in the same industry by a for-profit firm." And in the "social assistance sector, the nonprofit wage advantage is a stunning 55 percent…."

Conclusion

The Nonprofit Finance Fund invites interested parties to visit **nff.org/surveydata** to delve more deeply into these results (including analyses of historical data) and to customize and download the many graphs.

Take a look, also, at ***What Nonprofit Leaders Wish More People Knew*** (April 5, 2019) by Antony Bugg-Levine, CEO of NFF, the survey sponsor, and Kerry Sullivan, president of the Bank of America Charitable Foundation, for a discussion of "four takeaways" from this NFF Survey and "how the broader social sector should respond."