# Nonprofit FINANCE

## Innovating and Adapting to a New Financial Reality

Nonprofits are changing the way they do business because they must. Government funding is not returning to prerecession levels, philanthropic dollars are limited and demand for critical services has climbed dramatically. At the same time, 56 percent of nonprofits plan to increase the number of people they serve.

These are just some of the findings from the *2013 State of the Nonprofit Sector Survey* from the Nonprofit Finance Fund (**www.nonprofitfinancefund.org**) in New York City. The fifth annual survey, supported by the Bank of America Charitable Foundation, includes information on the finances, operations and outlook of 5,983 organizations across the United States.

Among other findings, nonprofits need new funding sources and models:

- Less than half (42 percent) of survey respondents reported that they do not have the right mix of financial resources to thrive and be effective in the next three years.
- One in four nonprofits has 30 days or less cash-on-hand.
- Over the next 12 months, 39 percent of respondents plan to change the main ways they raise and spend money.
- Almost one-fourth (23 percent) will seek funding other than grants or contracts, such as loans or investments.

Nonprofits that receive government funding face particular challenges:

- Only 14 percent of nonprofits receiving state and local funding are paid for the full cost of services; just 17 percent of federal fund recipients receive full reimbursement. Partial reimbursements require additional funding to cover the growing gap as nonprofits serve more people.

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- Government is late to pay: Among those with state or local funding, slightly more than 60 percent reported overdue government payments; more than 50 percent reported late payments from the federal government.

Under these challenging conditions, many nonprofits are unable to meet the growing need in their communities:

- For the first time in the five years of the survey, more than half (52 percent) of respondents were unable to meet demand over the last year; 54 percent said they will not be able to meet demand this year. (This represents a worrying trend. In 2009, 44 percent of nonprofits said they were unable to meet demand.)
- Jobs (59 percent) and housing (51 percent) continue to be top concerns for those in low-income communities.
- Ninety percent of respondents said financial conditions are as hard as or harder than last year for their clients; this is actually a slight improvement from prior years' outlooks.

Nonprofits are changing the way they do business to adapt to the new reality. In the past 12 months:

- Almost half (49 percent) have added or expanded programs or services, while 17 percent reduced or eliminated programs or services.
- Thirty-nine percent have collaborated with another organization to improve or increase services.
- Thirty-nine percent have upgraded technology to improve organizational efficiency.
- Thirty-six percent engaged more closely with their board.

Complete results from the *2013 State of the Sector Survey*, along with an interactive survey analyzer and a look at trends over the past five years, are available at **www.nonprofitfinancefund.org/survey**.

# Leveraging Accountability: Enhancing Your Value to Donors

BY JEFF SOBERS

Information is available as never before, and people have become accustomed to finding what they need when they want it—usually *right now*. When information is not available, or impossible to find, people begin to wonder why—and your donors and supporters are no exception.

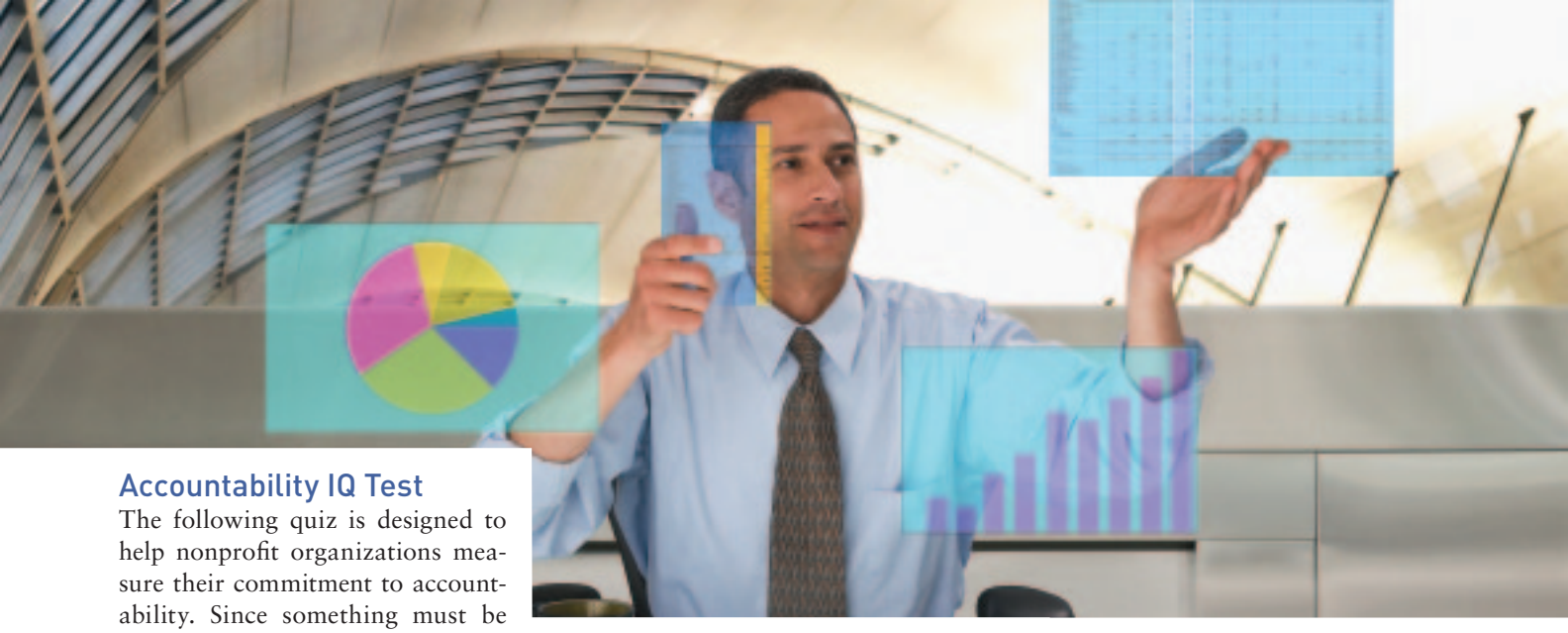
According to the Blackbaud *2012 Donor Perspectives: An Investigation Into What Drives Your Donors to Give*, donors who had stopped regular donations to a charity said that, in addition to a change in their financial situation, the most important reason was that they had a feeling the charity was not making the best use of its financial resources. In the *2010 Blackbaud State of the Nonprofit Industry Report*, 42 percent of donors reported needing updates on how their contributions are spent, up from 33 percent in 2008. In the 2012 report, findings showed that keeping donors informed was the No. 1 reason nonprofits cited for successfully retaining existing donors.

When services are provided only locally, it is easy to understand the need to demonstrate accountability. After all, everyone seems to know everyone else and what is going on. The look of concern or disappointment on donors' faces when a nonprofit does not uphold its end of the bargain is all too apparent.

Then there are the more public cases. For example, country singer Garth Brooks sued an Oklahoma hospital for failing to use his donation as he had intended. The hospital had promised to use his $500,000 donation to name a building after his mother, who had died from cancer in 1999. When the hospital informed him it would be treating his donation as unrestricted, Brooks sued for his money back. Not only did he receive his original donation, but the hospital also was forced to pay an additional $500,000 in punitive damages due to the breach of contract.

Donors are not the only ones who have demanded more of nonprofits in terms of accountability. The Internal Revenue Service (IRS) revised the Form 990 in June of 2007, which took effect in the 2009 tax year for organizations with more than $1 million in revenue or $2.5 million in assets. This new form required increases in the disclosure of executive governance and the board of directors. In addition, the Internal Revenue Code 6104(d) states that an organization must provide copies of its three most recent filings to anyone who requests them.

Ultimately, the answer lies in being accountable. However, what does it mean to be accountable? And once it is understood, how can it be measured and therefore improved?



## Accountability IQ Test

The following quiz is designed to help nonprofit organizations measure their commitment to accountability. Since something must be measured in order to be improved, this quiz may serve as a baseline for your nonprofit to use in measuring its future efforts. Each question should be answered "yes" or "no," with each "yes" getting one point.

## Does your organization:

1. Hold staff and board meetings on ethics or take measures to foster a culture of accountability and transparency?
2. Have a code of ethics and/or statement of values and post it on the website?
3. Follow a conflict of interest policy and post it on the website?
4. Have board members with financial expertise?
5. Have its financial statements independently audited?
6. Take steps to remain current with the law?
7. Have board members review financial statements, including the Form 990?
8. Have the CEO or CFO sign the Form 990?
9. File the Form 990 electronically?
10. Post the Form 990 on its website?
11. Post its policies, financial information and information on program results on the website?
12. Have a supported policy on reporting suspected misconduct (i.e., a whistleblower policy)?

## Scoring the Test:

| Score | Comments |
|---|---|
| 12 | Keep up the great work, and pass along the success stories and model policies to educate others. |
| 9–11 | Good, but there is room for improvement. |
| 6–8 | There is an indication of a commitment to accountability, but you need to move beyond the basics. |
| 0–5 | Time to get serious about accountability. Engage the board, staff and volunteers quickly to help make needed changes. |

Once an objective baseline has been established, nonprofits can begin to formulate strategies to further demonstrate their commitment to the public trust.

## Nine Ways to Improve Accountability

Nonprofits need to think about how they operate and put in place savvy strategies to earn and maintain the public trust. After all, without the trust of the public, there would be no charitable sector. There are several ways in which an organization can ensure it is doing everything it should to be accountable to its stakeholders.

**1. Create a culture of transparency.** Train new employees, volunteers and board members about your organization's principles. Teach them to be open and honest. Provide regular refreshers and updates, and utilize the Web, the intranet and other internal communications vehicles. Set the right tone at the top, and it will cascade throughout the organization.

**2. Abide by the *AFP Code of Ethical Principles and Standards* and *A Donor Bill of Rights*.** Emphasize a culture of transparency by abiding by the AFP code of ethics and adopting *A Donor Bill of Rights*. Focus on those aspects of donor relations that will enhance accountability.

**3. Adopt a conflict of interest policy.** Define conflict of interest for employees and board members, and specify who will be covered under the policy. Require regular disclosure of information related to conflicts of interest, and specify procedures for handling the conflicts when they arise. Non-standard examples may include a lack of term limits for board members or spouses who are at a competing nonprofit.

**4. Ensure members of the board of directors can fulfill their fiscal responsibility.** Your organization has a legal and ethical responsibility to ensure the appropriate use of its assets. The board should have financial literacy or at least be provided some mechanism for drawing on independent financial expertise.

**5. Conduct independent financial reviews and audits.** Not only is this good sense, but, in most cases, it also is required by the IRS. Avoid conflicts of interest in the exchange of information between the audit firm and your organization, and be sure to disclose audited financial statements in a timely and accessible way. Consider rotating audit firms or partners every five years.

**6. Ensure the accuracy of the Form 990, and make it public.** Have the board and/or appropriate committee review and approve the Form 990. Ensure it is signed by the executive director, CEO or CFO. File it electronically, and make it available on the organization's website.

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**7. Be transparent with external stakeholders.** Utilize the Internet to share information on the organization's finances, operations, governance and impact, including but not limited to

- a vision and/or mission statement,
- a statement of values and ethics and conflict of interest policy,
- a Form 990 and audited financials,
- a list of organizational programs as well as their impact and performance measurements,
- the annual report and
- a list of board members, major contributors and staff.

**8. Establish and support a policy of reporting suspected misconduct.** Known as a whistleblower policy, it helps an organization's credibility by ensuring that anyone can feel comfortable reporting misconduct of any form. It protects whistleblowers and levies criminal penalties for actions taken in retaliation against whistleblowers. And it is required by all entities, including nonprofits, under the Sarbanes-Oxley Act.

**9. Remain current with the law.** Designate a board member, staff person, consultant or volunteer to keep up-to-date with the law. Make sure your organization fully complies with all existing laws governing charitable organizations.

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# Moving From Fundraising to Financing

BY NELL EDGINGTON

No doubt about it, donors are changing. According to *NextGen Donors: Respecting Legacy, Revolutionizing Philanthropy*, a study from the Dorothy A. Johnson Center for Philanthropy and 21/64 (**www.nextgendonors.org**), the next generation of donors is very different from preceding generations. Looking at Millennial and Gen X donors (wealthy individuals or individuals who will inherit wealth, born 1964–2000), the study found that these donors are focusing their money on nonprofits that demonstrate change to a social problem—or impact.

In order to stay relevant to donors, be sustainable and achieve their missions, nonprofits need to shift from fundraising to financing. What does this entail exactly?

**1. Move to impact.** It is no longer enough for nonprofits to just do good work. There is a growing demand for nonprofits to 1) articulate what results they hope their work will achieve and 2) track whether those results are actually happening. Nonprofits have long discussed the outputs of their work—number of people served, number of services provided, etc. However, charities are increasingly being asked to articulate and track the outcomes they are achieving. How are people's lives changing because of the work a nonprofit does? Increasing competition for shrinking dollars means nonprofits must develop their own theory of change (how they use community resources to create change to a social problem) and then measure whether that theory is becoming a reality. The more a nonprofit can talk about outcomes and impact, the more donors it will attract.

**2. Connect mission and money.** A nonprofit leader who creates a financial engine for his or her organization that is fully connected to and supportive of the mission will enjoy financial sustainability. Nonprofits must make money one of the goals of their strategic plans and no longer separate fundraising from the mission. All elements of a nonprofit's operations, including the moneymaking ones, must be fully integrated and moving forward together.

**3. Create a financing plan.** Once money and mission are connected, a nonprofit leader must create a comprehensive strategy for bringing enough, and the right kind of, money in the door to achieve strategic goals. This includes revenue and capital, programs and infrastructure dollars and all funding sources. A financing plan integrates all activities that bring money in the door—individual donors, foundation grants, earned income, government contracts, etc.—and funds both short- and long-term goals, as well as the programs and infrastructure of the organization.

**4. Diversify funding.** Relying on only one or two funding sources, particularly foundation grants, which make up less than 2 percent of all the money flowing to the nonprofit sector according to the 2012 *Giving USA* report, can be risky. Look at creating a robust and diverse money mix that fits well with and builds on the nonprofit's mission and competencies.

**5. Find money to build.** In a stark economic environment, the nonprofits that do not have adequate infrastructure sim-

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ply will not survive, let alone be able to adequately address the social problems they were organized to solve. Nonprofit leaders must become savvy about capacity capital and start raising the money they need to build the organization their mission requires. There are two kinds of money in the sector: revenue and capital. Revenue is the day-to-day money necessary to run programs (e.g., staff, beds in a homeless shelter, books in a reading program, etc.). Capital is a one-time infusion of significant money to strengthen or grow the organization so that it can create greater impact. The BAND-AID® reality of inadequate technology, underpaid staffs and underfunded systems that riddle the nonprofit sector is not sustainable. Your nonprofit will only get better at delivering impact if it has an effective organization behind its work.

## The Financing Plan

Creating a financing plan is essential for your nonprofit if it is to move from just fundraising to effective financing.

**1. Develop a budget for your strategic plan.** The most important step in creating a financing plan is connecting money to the work of your strategic plan. If you truly want to bring your strategic plan to fruition, you must connect that plan to the money it will take to execute on it. Go through your strategic plan and ask yourself how much it will cost to make the strategic plan a reality. Project those expenses out over the timeframe of the strategic plan. If you have a three-year strategic plan, determine what your organization's expenses must be each year over the next three years in order to achieve the goals of your strategic plan.

**2. Create revenue goals.** To meet the expenses of your strategic plan, your final financing plan will have approximately five broad goals. These goals come in three types: revenue goals, a capital goal and a financing infrastructure goal. Revenue is the day-to-day money you need to meet the expenses of your strategic plan. You will have one revenue goal for each revenue source that is appropriate to your organization, such as private dollars from foundations, corporations and/or individuals; government dollars; and earned income—the sale of goods or services. Your revenue goals will make up three of the five goals of your final financing plan.

**3. Establish a capital goal.** As mentioned above, capital is the one-time, organization-building money you need to fund special or infrastructure-related purchases within your strategic plan. It may be the money you need for a program evaluation, a new data-gathering system or a new database. If you require capital investments to make your strategic plan a reality, one of the goals of your financing plan will be a capital goal.

**4. Create a financing infrastructure goal.** The last goal of your financing plan should focus on what improvements you will make to the internal systems, staffing and technology you use to bring money in the door. This goal is not a money goal but rather an activity goal. If you want to significantly grow the revenue that flows to your nonprofit, you will have to make some improvements to the financing infrastructure of your organization. This means you may want to add additional development staff, buy a new donor database, upgrade your website or create marketing materials.

**5. Establish your objectives.** Each of the goals in your financing plan will be broken down into objectives to make them achievable. For example, you may have a revenue goal that describes how much private money you will raise. You would then break that total private revenue goal into the individual donor, corporate donor and foundation grant objectives necessary to achieve that goal.

**6. Develop and implement an operational plan.** Once you establish your goals and objectives, you will break each objective into the activities, deliverables, people responsible and due dates necessary. This becomes your tactical operational plan, with which you will execute on and monitor the financing plan. It ensures that the goals and objectives actually come to fruition.

In the end, the goals and objectives of a nonprofit's financing plan may look like this:

## Fiscal Years 2014–2016 Financing Plan

Goal 1: Raise $548,625 annually from private sources by 2016.

- Objective 1: Raise $288,750 from individuals by 2016.
- Objective 2: Raise $86,625 annually from corporations by 2016.
- Objective 3: Raise $173,250 annually from foundations by 2016.

Goal 2: Raise $346,500 annually from government sources by 2016.

- Objective 1: Raise $120,500 from county grant by 2016.
- Objective 2: Raise $226,000 from federal grant by 2016.

Goal 3: Raise $17,325 annually from earned-income sources by 2016.

- Objective 1: Raise $5,000 from T-shirt sales.
- Objective 2: Raise $12,325 from classes.

Goal 4: Raise $220,000 in capital.

Goal 5: Improve our financing infrastructure in order to meet our revenue and capital goals.

- Objective 1: Increase the staff and board's ability to bring money in the door by adding positions and training.
- Objective 2: Add key technology.
- Objective 3: Improve the quality and effectiveness of our marketing efforts.

You then would be ready to create the tactical operational plan to bring each of these goals and objectives to life.

This is not merely semantics. There really is a better way. Nonprofits do not have to exhaust their fundraisers, their donors, their staffs and their messages. By creating a financing strategy, as opposed to just a fundraising plan, your nonprofit can get much closer to sustainable social change.

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