



Small Nonprofits

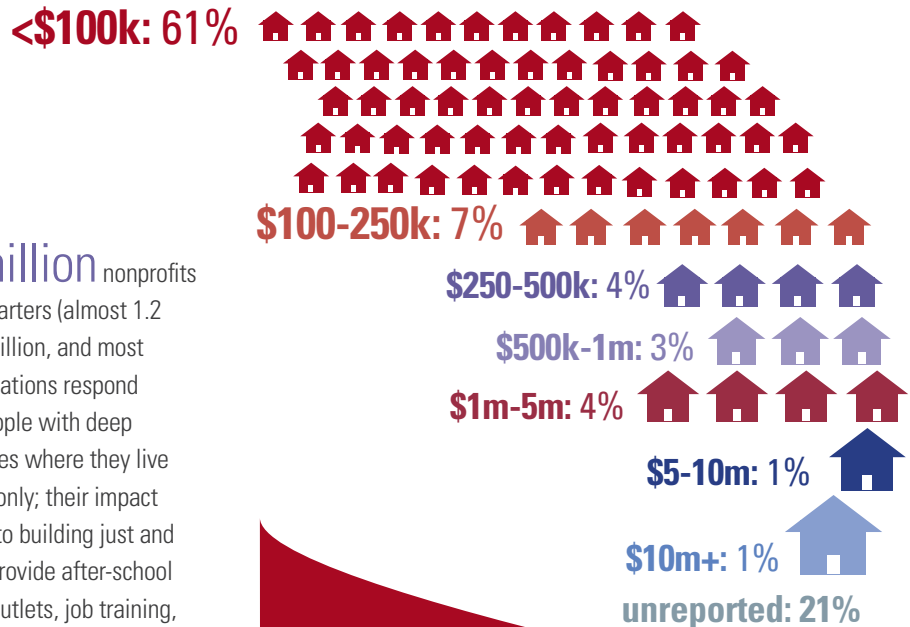
Solving Big Problems

By Angela Francis and Jennifer Talansky
of Nonprofit Finance Fund



The Plight of the Smallest

registered nonprofits, by revenue¹



There are over 1.5 million nonprofits in the United States.² Of those, three-quarters (almost 1.2 million) have annual budgets under \$1 million, and most are even smaller.³ These “small” organizations respond to localized needs and are staffed by people with deep knowledge and caring for the communities where they live and work. They are small in budget size only; their impact and community engagement are crucial to building just and vibrant neighborhoods and cities. They provide after-school programs, community centers, creative outlets, job training, food pantries, and much more.

As a result of the 2008 recession and the ensuing economic fallout, increasing numbers of Americans have suffered serious financial woes. As unemployment rose, so did the number of people living in poverty and the need for social services. At the same time, credit became harder to obtain, and funding began to decline, especially from government sources. These conditions have persisted and are now particularly challenging for small “safety net” social service organizations that rely on government funding. These organizations, which always run lean, are now stretched even further and in danger of reducing services or even closing their doors.

The following report draws on Nonprofit Finance Fund’s experience working with 22 nonprofits through the Capital and Capacity for Economic Recovery (CCER) program in Greater Philadelphia, as well as our 30 years of work with small social service organizations nationwide. It highlights these nonprofits’ common financial challenges and offers suggestions for how they and their supporters can enact financially stabilizing practices in response. We draw on real-life lessons from nonprofits that used small capacity grants and financial training opportunities to create positive programmatic and infrastructure shifts for the benefit of their clients.

NFF pushes for improvement

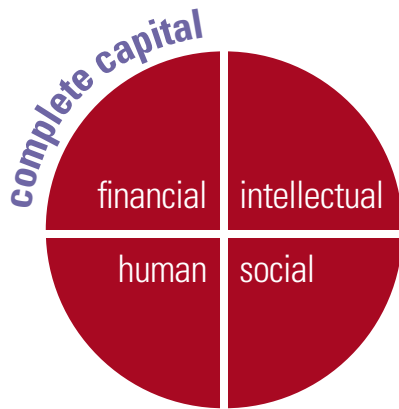
in how money is given and used in the sector. Since 1980, we’ve worked to connect money to mission effectively so that nonprofits can keep doing what they do so well.



We provide financing, consulting, and advocacy services to nonprofits and funders nationwide. Our services help great organizations

stay in balance, so that they can successfully adapt to changing financial circumstances and grow and innovate when they’re ready. In addition to providing loans and lines of credit, we organize financial training workshops, perform business analyses, and offer customized consulting services.

Capital & Capacity for Economic Recovery (CCER)



To stabilize these critical providers that are helping communities with economic recovery, the Federal government provided funding in 2009 through the American Recovery and Reinvestment Act (ARRA). With \$1 million in ARRA funding and additional support from local foundations and corporations, Nonprofit Finance Fund (NFF) developed a unique program in the five-county Greater Philadelphia area. The Capital and Capacity for Economic Recovery (CCER) program offered grants paired with technical assistance to address the key financial challenges of 22 nonprofits—with the end goal of improving job training services and aiding economic development activities in the region.⁴ The program took a **Complete Capital** approach, combining elements of financial

capital (the right money), intellectual capital (the right thinking), social capital (the right networks) and human capital (the right expertise) to improve each organization's health in the context of the economic issues facing its community.

CCER acknowledged that the demand for services has long outpaced financial resources, and this dynamic—which is likely to continue—has pushed many nonprofits to the financial breaking point. Amid diminishing resources, nonprofit leaders face a dizzying array of decisions: how to meet the rise in demand, assess the impact of expanding or eliminating certain programs, and whether to forge new partnerships or expand into new service areas. CCER offered financial guidance and training, combined with up to \$30,000 in capacity building grants to help nonprofits balance their capacity, capital, and mission considerations.

The 22 CCER participants

BuildaBridge International, The Business Center for Entrepreneurship and Social Enterprise, The Center Foundation, Community Action Agency of Delaware County, Inc., Fairmount Community Development Corporation, Francisville Neighborhood Development Corporation, Girard Coalition, Inc. (GCI), Handi-Crafters, Inc., Interfaith Housing Assistance Corporation of Chester County, Jobs for Pennsylvania's Graduates, Inc., Life Transforming Ministries (LTM), LIFT-Philadelphia, Montgomery County Community Action Development Commission, National Comprehensive Center for Fathers, Nationalities Service Center, Nonprofit Technology Resources, Philadelphia Area Project on Occupational Safety & Health (PhilaPOSH), Philadelphia Chinatown Community Development Corporation, Welcoming Center for New Pennsylvanians, Whosoever Gospel Mission, Women's Opportunities Resource Center, Women's Resource Center

Developing healthy options for an urban food desert...

Capital & Capacity for Economic Recovery (CCER)



CCER targeted grassroots and community nonprofits that work towards neighborhood revitalization and provide job training, employment resources, homeless services, and access to state and Federal benefits. The median annual budget size of CCER participants was \$400,000. Whether they sought to expand their impact, change their mix of services, or simply survive, each organization faced unique financial circumstances. NFF enabled these providers on the front lines of economic recovery to better understand their financial dynamics, make informed decisions and mitigate risk, ultimately stabilizing the human resources, facilities and systems that power them.

While these 22 organizations had various mission objectives—ranging from providing job opportunities for people with disabilities, to resources for homeless individuals, and economic revitalization of local neighborhoods—and unique financial considerations, a number of defining characteristics applied to all. Throughout this report, we will highlight a similar pattern of challenges often experienced by smaller urban and suburban organizations nationwide.

Improving job prospects for a brighter future...



Photo Courtesy Francisville Neighborhood Development Corporation, by Chasi Annexy

Common Goals, Shared Challenges



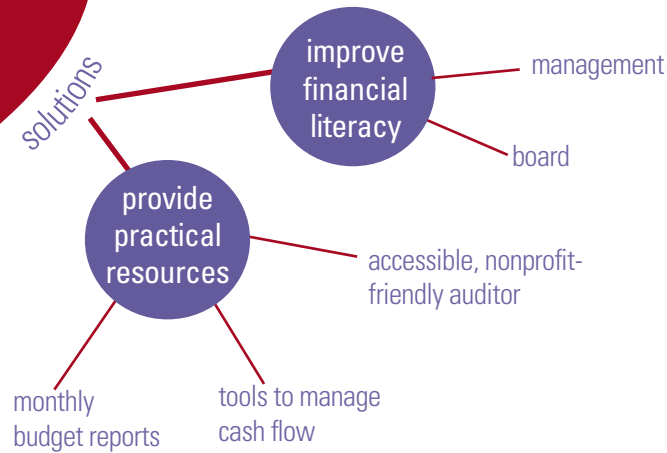
Nonprofits must change to survive through volatile economic conditions. For small community-based organizations—particularly those that rely on government funding—adaptation is critical for long-term viability. Some will reconfigure just to maintain their current services; others will expand their impact in response to rising demand.

Change, and in particular growth, can be risky. Yet many of the organizations that NFF served through CCER were compelled by a common goal: they wanted to keep up with the growing need for their services. To do so, they sought to strengthen their systems, increase funding, improve programs and deepen community impact.

Shared challenges hindered or slowed many of the organizations in CCER from readily meeting the demands of the environment. These challenges included lack of financial infrastructure and/or expertise, a lack of money to support operations or existing programs, and a mindset that standardized reporting alone provided enough financial information to make decisions. To achieve their impact goals, organizations must monitor, analyze, and understand the links between money and program effectiveness. Too often, these links are neglected or not well understood, particularly in the face of pressing program demands. Understanding these links leads to informed financial and programmatic decision making, which is essential to advancing an organization's mission.

Challenge #1

Lack of infrastructure and specialized knowledge of nonprofit finance creates a strain on resources and decision-making.




At most small businesses, employees wear many hats; small nonprofits are no different. What is different for nonprofits is the nature of their underlying business challenges (generally, the work is not profitable) and the way the work is funded (which often imposes myriad restrictions and onerous reporting requirements). As a result, the fiscal management of a small nonprofit is incredibly specialized and often requires more than its fair share of available time in an already capacity-constrained environment.

Very few of the small nonprofits that NFF works with have a dedicated financial infrastructure. Instead, the executive director is often responsible for managing the finances with some part-time external help. A part-time bookkeeper is typically all these agencies can afford and is a resource intended to meet only the most fundamental, immediate need for accountability and compliance. In addition, when these organizations receive their audits, a lack of formal finance training—or time—can make it difficult for nonprofit leaders

to ask their auditor or bookkeeper meaningful questions about the audit data or to make the best use of it for communication with external stakeholders. With this limited financial capacity, these organizations have only the most basic of financial reports on which to rely. Without real-time financial tools, data-driven decision making is a significant challenge.

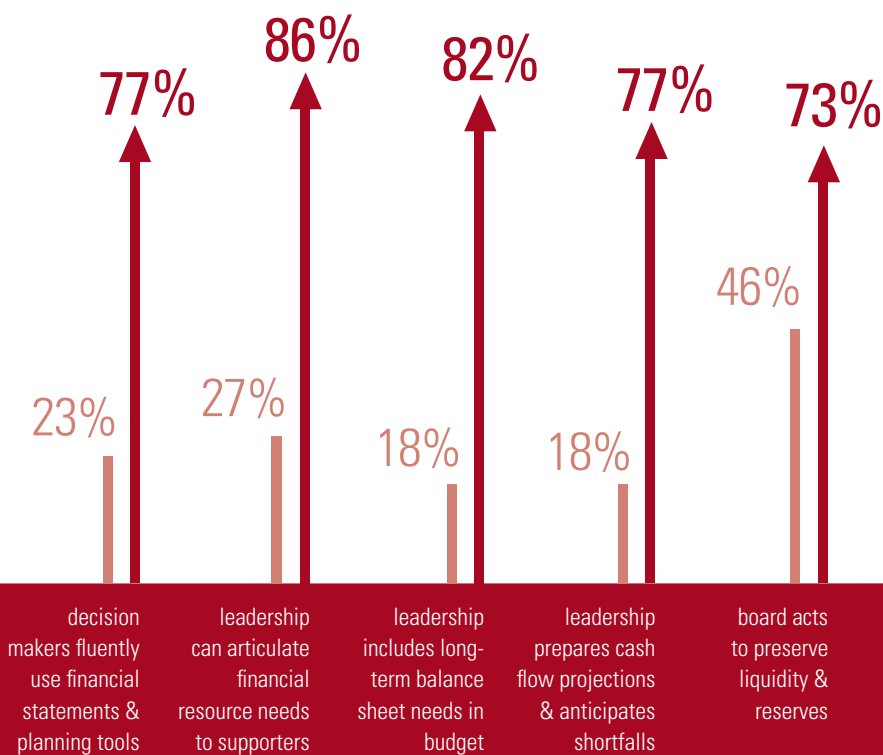
In many cases, the board is not well positioned to help. It may have a range of expertise, but a critical challenge NFF has observed is a lack of board familiarity with nonprofit financial statements. In addition, the executive director may unintentionally share unclear financial reports with the board, preventing its members from providing robust financial oversight.

Through CCER, NFF provided several participants with financial literacy training for leadership staff and board members. This training can be helpful especially for board members lacking a finance background or for small nonprofits that rely on a “working board” for help with finances and fundraising.



Giving second chances...

Branch Associates conducted an outcome study to measure changes in CCER participants' capacity levels before and after receiving NFF's services. Participating organizations completed a pre-assessment at the start of CCER and a post-assessment after the program concluded. Below are core nonprofit financial activities where we saw a substantive change in the number of organizations reporting strong ability and understanding after the CCER program.



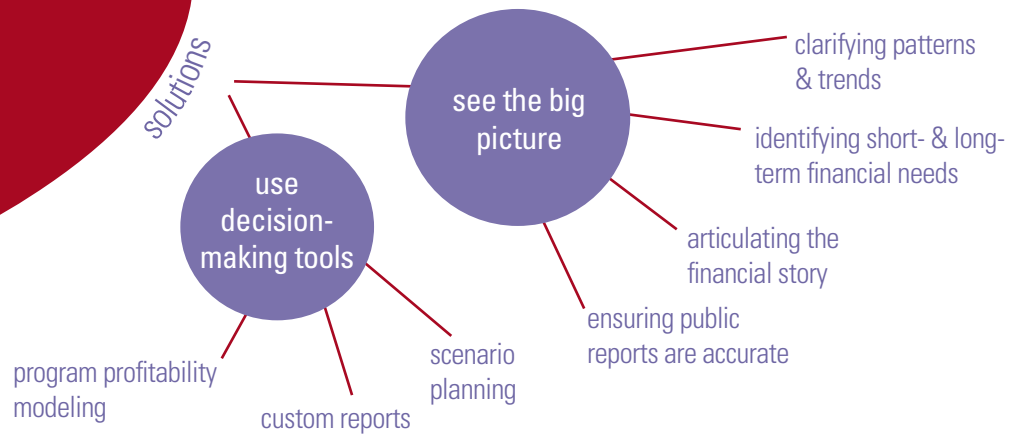
Before & After CCER

"One of our board members had never dealt with finances at all ... [S]he commented that she didn't know how to read a budget before but can do so now. The board members are now on the same page with what a budget looks like. They know where the money comes from and are taking responsibility for funding programs."

CCER Participant Executive Director

Challenge #2

A “compliance only” mindset prevents organizations from using finance effectively to make rapid and strategic decisions, let alone adapt or grow.



Financial compliance alone isn't useful for decision-making. Small nonprofits may have the financial records necessary to comply with government or funder requirements, but on their own, even well-kept books—or annual audits or 990 data—can't help with real-time, day-to-day management decisions. The information is not presented in a way that can answer key questions about program financials, clarify the capacity required to deliver on contracts, identify resource needs, or assess new grant opportunities.

To make matters worse, compliance rules in the current economic landscape are changing, particularly for nonprofits with a significant percentage of government funding. Changes in funding contracts may require service providers to track different activities or fundamentally alter the nature of their work. Social service agencies participating in CCER were increasingly seeing government contracts shift from a cost-reimbursement to a performance-based model.

These changes have a major structural impact on an organization, including definitions of success, infrastructure and staffing needs. For example, workforce development providers might need to increase the number of clients successfully placed in a job or track the length of time that a former client is able to retain employment. Or perhaps now the organization's externally focused relationship-building and “job development” activities are not as critical as the need for intensive job-skills counseling. What may seem like minor contract changes can have major implications for staff structure, program activities and business model.

Unfortunately, new requirements do not come with resources to support the necessary program or administrative changes. More often than not, organizations

are forced to use precious unrestricted or general operating dollars to manage the change.

So how can leadership make strategic program and resource decisions with clear data? NFF's financial training and technical assistance, combined with grant funding, helped organizations look beyond compliance and gave them a financial framework for strategic, long-term decision-making. Following are a few examples of NFF's solutions:

Don't rely on annual standardized financial reports.

For a local community development corporation, NFF customized a financial report that allowed the organization's leadership to understand the practical impact of their day-to-day transactions on their year-end financials. NFF's process enabled management to make the connections between bookkeeping transactions and financial reports in real time so that they could make timely decisions—rather than waiting for their audit to be completed several months into the next fiscal year. The process also informed leadership about the type of financial and bookkeeping skills that were needed in-house, so that they could better track their income statement and balance sheet throughout the year.

am I looking at the right numbers?

will a potential grant cover overhead?

is our revenue reliable, from month to month & year to year?

Analyze the revenue and expense dynamics of major programs.

Program participant BuildaBridge reexamined their annual budget and costs of service delivery through the lens of NFF's Program Profitability Model (PPM), which shows how much profit or loss each major program generates in a way that lets managers understand how those programs fit into the organization's overall financial picture. The process revealed key insights about an after-school arts program for children in shelters: although this program was by far the organization's most profitable, it was entirely dependent on volunteer labor and only one source of funding. Previous reports had obscured how financially important this program was for BuildaBridge and the extent to which it helped support their other programs.

Make data-driven decisions.

Through the analysis, BuildaBridge staff recognized the need to seek additional funders to support the program. But perhaps more importantly, this exercise greatly informed their resource priorities. Their annual budget planning projected a \$35,000 surplus, which led to a major decision: should leadership use the projected surplus to invest in a

key development hire? Using the PPM, BuildaBridge created data-driven parameters to trigger a response, hinging the decision to hire on whether they met that surplus goal at the end of the first quarter. Another CCER participant, PhilaPOSH, used a similar approach to make hiring decisions.

NFF's training and tools gave CCER participants a new framework for making organizational decisions, which was absolutely critical when seeking to grow or change the organization's structure. Prior to working with NFF, Whosoever Gospel Mission was considering closing their off-site thrift store. The store's revenue had declined, and organizational leadership viewed it as a burden. Assessing this program through the lens of the PPM helped the Mission determine that the off-site thrift store was actually a financial boon, with the potential to generate future revenue to support the organization's flagship New Life Program. As a result, leadership determined that the store should remain open and continue providing low-cost clothing and household items to the community.

is program revenue covering cost?

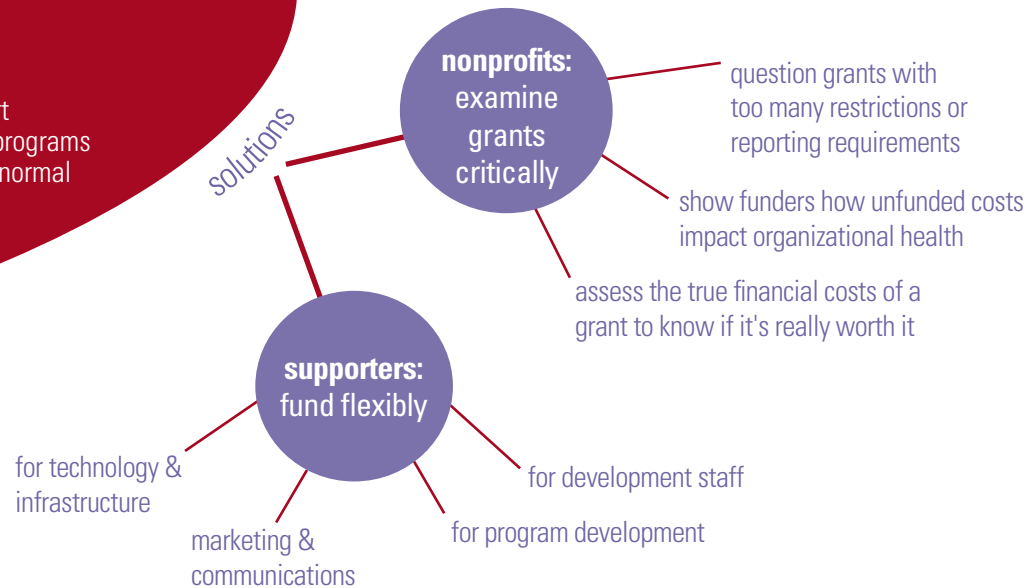
do financial data help me make decisions?

do we need new staff to manage evaluations?

what do we do if our gov't funding is cut?

Challenge #3

Lack of money to support operations and existing programs makes it hard to sustain normal operations.



Funding overhead is unpopular, despite how vital it is to programs. For many community-based nonprofits addressing poverty, one of the biggest problems is finding funders who are interested in paying for existing programs along with enough “overhead” or “administration” to sustain normal operations. Nonprofit leaders know all too well that their programs cannot be run in isolation and require supporting services and infrastructure to be effective. But many are heavily reliant on government funding, which tends to be very strict about administrative spending. As a result, organizations must seek private funds to close the gap.

Yet it can be difficult to raise operations funding from private donors as well. All too often, such funding is only attainable when a nonprofit tweaks its programs or target population, and it rarely covers the full associated costs. Private or public grants routinely spur the development of entirely new programs, without supporting the related increase in infrastructure.

But new programs—even when they develop in deliberate increments or organically over time—aren’t made sustainable just by tacking on new grants and contracts. Although there can be mission arguments for doing more, chasing grant dollars can be a major pitfall for small organizations. In addition to the costs of program development, new contracts bring new administrative burdens. Turning talented program staff into grant-compliance monitors will not help an organization make thoughtful financial decisions or grow its impact.

The reality is that non-program dollars are hard to come by, which means that organizations can barely cover ordinary administration and infrastructure costs, let alone use funding to thoughtfully, strategically plan for growth or change.

CCER provided flexible grants of up to \$30,000, creating a unique opportunity for many of these small organizations to meet a critical capacity need—and applicants were able to define these projects for themselves. For an organization with a \$400,000 annual budget, this had a meaningful impact. This flexible funding freed organizations to address mission-critical issues determined by management. In many cases, organizations chose to implement a deferred capacity project, and the funding supported much-needed infrastructure improvements that allowed them to work more efficiently.

The majority of CCER funding helped to shore up technology infrastructure or implement new accounting or outcomes measurement systems. For instance, BuildaBridge chose to split their grant award between the purchase of new outcomes measurement software and the development of a new online employment program that will provide job training and connect artists with potential employers.

A number of grantees used this resource to thoughtfully develop new programming or buy the equipment necessary to sustain a key program. Francisville Neighborhood Development Corporation used the award to develop the business plan for a key piece of their corridor revitalization strategy: The Francis Village Market Place. Life Transforming Ministries upgraded the outdated technology in their computer lab and are now better outfitted to provide their tax prep assistance and online college courses. Without flexible funding, many of these vital projects would have been postponed or left undone.



Seeing beyond the financial problems of individual organizations is critical if we are to solve social problems. In addition to their day-to-day financial issues and operating concerns, small nonprofits are buffeted by external environmental and economic conditions that are critical factors in determining their success or failure. Increases in need for services; shaky fundraising conditions; uncertain, inappropriate, and/or unreliable funding; and economic conditions dramatically affect their options and outcomes.

The services offered through CCER were designed to help organizations make financially informed decisions and improve their ability to deliver services. But what happens when their challenges are caused or exacerbated by the funding system and environment in which they operate?

Stronger financial management alone will not solve these structural problems. For communities to truly thrive, nonprofits, funders, supporters, and investors must work together by adopting a Complete Capital approach—one that targets social challenges and creatively incorporates all of the financial, intellectual, social and human resources available to solve them.

To address some of the systemic issues related to Financial Capital, the following pages include suggestions for improving best practices in the sector and explore data on small organizations collected through NFF's Annual State of the Nonprofit Sector Survey.

Connecting artists to employment...



Nonprofit
Finance Fund®

What are the core issues small nonprofits face?

And what can funders and nonprofits do to manage or solve these challenges? NFF has worked with nonprofits large and small for over 30 years. Post-recession, our work with smaller organizations has only reinforced some of our long-held observations about the conditions they face. Below is our most concise advice for nonprofits and their supporters alike.

What Nonprofits Can Do...

Spend time seeking and applying for capacity grants, even small ones, if they'll allow you to take care of deferred infrastructure needs.

Money makes programs possible. Devote time and resources to keep finances running well. If you don't have adequate resources, borrow financial management templates from a peer organization or bring on board or staff (or both!) with expertise in nonprofit finance.

Aim for operating surpluses, not just break-even. This money can be set aside to fund infrastructure and equipment, growth, program improvements, and more.

What type of board do you have? Does it primarily approve the budget and assist with fundraising? Or do its members volunteer significant labor and professional skills? Put in writing the function that your board is meant to serve, and revise expectations as your organization evolves.

investing in the enterprise is difficult for small nonprofits, which often run lean

financial understanding and capacity are necessities, not luxuries

surpluses are critical, particularly in difficult times

the roles of a small nonprofit's board members can vary

What Funders Can Do...

A small grant can be meaningful to a small organization. Fund important capacity needs, which include things like financial reporting systems, development staff, and improved technology. Mission returns from these investments can be just as large as those from a program grant.

If you value your grantees' programs, make sure they have the financial tools and know-how to successfully manage their nonprofits. If they are lacking tools or expertise, help fund them—this is especially critical for those that rely on restricted government funding.

Embrace the idea that nonprofits should have surpluses, and don't penalize them or automatically reduce funding if they do.

Don't rush to judgment if a small nonprofit is not at 100% for board giving. Many small nonprofits incorporate professional expertise or other contributions from board members. Financial commitments can be especially challenging for former clients or low-income members.

What Nonprofits Can Do...

Embrace in-kind, but have a plan and budget for replacing volunteer labor or worn-out equipment and systems when necessary.

in-kind donations are often key resources for small nonprofits—even for infrastructure

Don't buy a facility if you can't support the capacity to manage it (e.g., can your Executive Director divert time from fundraising to deal with the boiler?). Depreciation, a non-cash item that accounts for the wear and tear on your building, must also be addressed; saving for future (or emergency) costs is critical.

owning real estate can turn small nonprofits into full-time property managers

Growth is not always good. Be wary of mission creep and imbalances that can come from tacking on new programs in an ad hoc fashion. Don't empower your grantwriter to make program tweaks just to increase the odds of getting a grant.

sometimes, nonprofits will do anything for funding, even develop an entirely new program

A 'net grant' means considering the resources required for submission, future reporting and oversight when deciding whether to apply for a grant. Assess the full costs and benefits of the grant opportunity—don't be afraid to turn down funding if it doesn't cover full costs.

it's time to embrace and apply the principle of 'net grants'

Working capital is your cash on hand plus any line of credit. While it can be hard for small nonprofits to access lines of credit, explore all your options if it's appropriate for your situation. Reach out to banks—starting with the one holding your deposits—CDFIs, and your board/funder networks.

working capital is crucial, especially if a nonprofit is primarily government-funded

What Funders Can Do...

Encourage your grantees to understand the useful life of donated equipment and develop a plan for replacing donated goods (such as computers) at the appropriate time. Indicate your willingness to fund these replacements when they come due.

Don't encourage grantees to purchase a property, even a cheap one, if managing it will overwhelm their staff. If a grantee owns a facility, help them create a building reserve. Solely funding urgent requests validates an "emergency only" approach to facility management.

Fund what already works, rather than only offering funds for new or innovative approaches—especially when funding small, local organizations that have already identified and are filling a real need in their community.

When developing application and reporting requirements, make the administration commensurate with the grant size: a \$5,000 grant should come with different reporting expectations than a \$500,000 one. Consider adding funding to cover the organization's true 'net grant' administration costs.

Consider the impact of payment timing on your grantees' cash flow. For many small nonprofits, when the check arrives is as critical as when the grant is awarded. Consider other ways to help small nonprofits with cash flow, such as making Program Related Investments or bridge loans.

NFF 2012 State of the Sector Survey

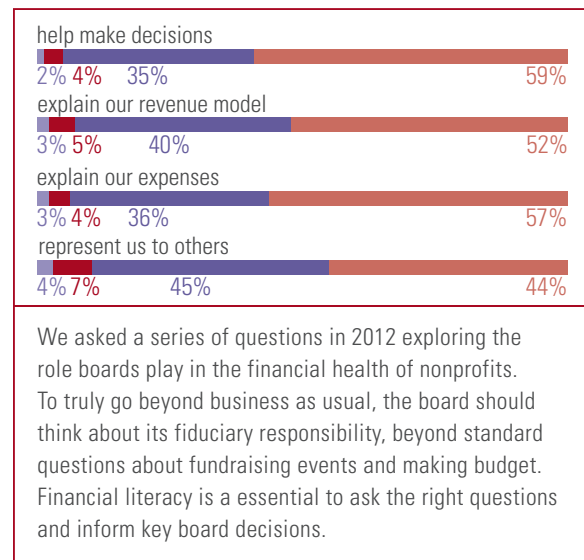
NFF's fourth annual State of the Nonprofit Sector Survey, conducted from January to February 2012, received responses from over 4,600 nonprofit leaders nationwide. The survey revealed that rising demand is overwhelming a sector still coping with a brittle economy and a barrage of funding cuts. While there are hints that some organizations may have navigated through the worst of the recession, the ever-increasing need for services suggests that our communities have not. The respondents tell a story of a sector still stretched thin, with organizations feeling distant from their funders and boards, and staff facing more work with less money and few benefits to take home.

Below, we explore some of the results for the 1,509 small organizations, with annual expenses under \$500,000, that responded to the survey. **To see full results and filter the data yourself, check out our Survey Analyzer at survey.nonprofitfinancefund.org.**

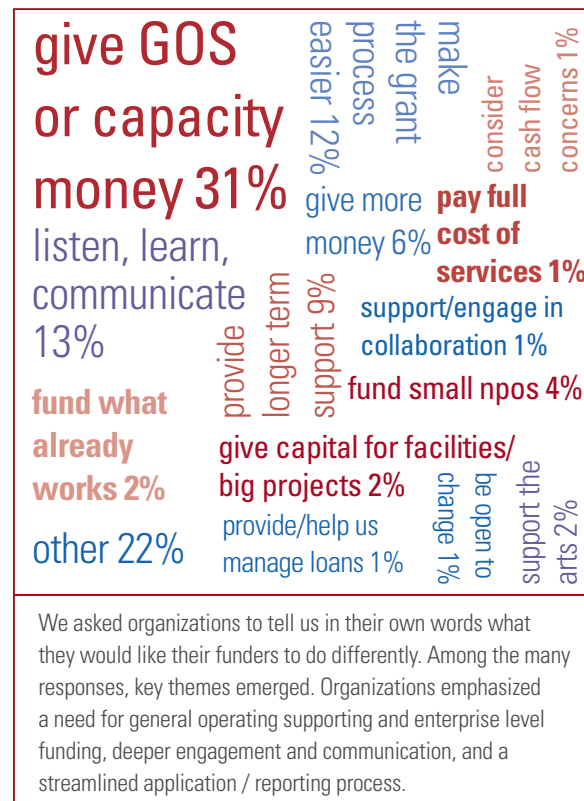
my npo can have open dialogue with funders about...



board understanding of financial data: our board can...
n/a, not at all, not enough, just right



if I could ask my funders to do one thing differently, it would be to....



NFF's 2012 Survey is generously sponsored by The Bank of America Charitable Foundation.

Special Thanks & Footnotes

The CCER Initiative was supported through Federal American Recovery and Reinvestment Act (ARRA) funding, with matching funds provided by a number of private foundations and corporations.



American Recovery and Reinvestment Act of 2009

THE F.B. HERON FOUNDATION



Prudential Foundation

DVREDF Delaware Valley Regional Economic Development Fund

WELLS FARGO

Independence foundation

THE PHILADELPHIA FOUNDATION

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Santander

1. Urban Institute National Center for Charitable Statistics. NCCS All Registered Nonprofits Table Wizard. [Show: Registered Nonprofits, By: Total Revenue Level (years 1995, Aug to 2011, Dec)]. http://www.nccsdataweb.urban.org/tablewiz/tw_bmf.php "Registered Nonprofit Organizations by Level of Total Revenue" (BMF 12/2011, 2011, Dec data.)

2. Urban Institute National Center for Charitable Statistics. "Number of Nonprofit Organizations in the United States, 1999 - 2009." <http://nccsdataweb.urban.org/PubApps/profile1.php?state=US>

3. Ibid. 1.

4. NFF awarded \$600,000 in Federal funds through the CCER program. As a Federal grantee making subawards to local agencies, NFF allocated funding and selected CCER participants per Federal guidelines. (See "Designing and Managing a Subaward Program," at [StrengtheningNonprofits.org](http://www.strengtheningnonprofits.org). <http://www.strengtheningnonprofits.org/resources/e-learning/online/designingandmanaging/default.aspx?chp=0>.) The selection process included a written Request for Proposals (RFP) and mandatory bidder's conference for organizations interested in applying. The bidder's conference explained the RFP and outlined the program goals. Interested organizations were then invited to submit a Letter of Intent, scored against a Federally approved rubric by an external review panel of volunteers. The 20 highest scoring organizations were invited to submit full proposals, scored again by the external review panel. The highest scoring organizations were awarded funding. This entire process was completed twice during a 2-year span. In an effort to ensure fairness, the external review panels and full selection process for CCER grantees did not include NFF or government officials.

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