Nonprofit Finance Fund®

Kinds of Capital

Using the right kinds of capital in the right ways helps nonprofits effectively pursue innovation and experimentation, manage risk, respond to the unexpected, and invest in revenue generating activity.

All invested capital, regardless of its specific application, should contribute to a more appropriately aligned capital structure. A healthy capital structure is critical to enabling organizations to pursue innovation and experimentation, manage risk, respond to the unexpected, and make critical investments in revenue-generating activity.

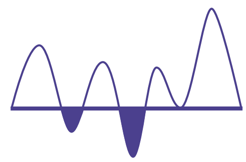
NFF defines capital and its uses in the ways described here, while acknowledging that there may be some fluidity between the types.

These capital funds can be generated in many different ways. Some of the most common include:

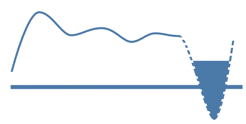
- Retained earnings from operating surpluses (i.e., "savings")
- Periodic campaigns for capital (including campaigns for facilities as well as for change capital) and targeted fundraising
- Judicious use of debt, including internal borrowing, bank or other outside debt

Working Capital
Funds to maintain ordinary business operations.

Operating Reserve
"Rainy day" fund; absorbs unforeseen funding losses or unexpected, extraordinary expenses

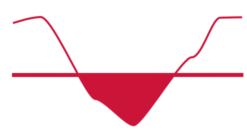


Risk & Opportunity Capital
Funds to weather the unexpected and support experimentation or course corrections.



Change capital*
For growth, downsizing and to change the size and scope of the organization.

Recovery capital
Helps recover from damaging financial shortfalls, reduce debt, or fund much-needed repairs to facilities / equipment.



Facilities & Equipment Capital
Organizations can raise funds for specific acquisitions or upgrades, or accumulate reserves to meet future needs as they arise.

Endowments
Raised capital that is often permanently restricted and generates investment income to support the organization. Investment income can be used as revenue or re-directed towards any of the types of capital described above.

*Organizations scaling rapidly may require an enterprise-level infusion of growth capital into a rigorous plan for sustainability. To learn more, visit: nonprofitfinancefund.org/capital-services/portfolio-performance-report

Nonprofit Finance Fund (NFF) unlocks the potential of mission-driven organizations through tailored investments, strategic advice and accessible insights.

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Kinds of Capital: In Depth	In Practice
Working capital is the funds on hand used to maintain ordinary business operations or cover ongoing expenses.	An education nonprofit pays for a program's costs up front and receives reimbursement later. It uses working capital to cover expenses during the gap.
Operating Reserve is a "rainy day" savings account for unexpected cash flow shortages, expenses, or losses.	A large grant that was anticipated is significantly delayed, resulting in cash shortfalls. A human services nonprofit uses its operating reserve to cover operating expenses during the delay.
Risk & Opportunity capital allows organizations to absorb risk and pursue opportunities, be they artistic or organizational in nature. It can be used to help weather unexpected internal or environmental challenges and to invest in experimentation or course corrections.	A community-based organization that has experienced historical challenges in recessionary environments budgets and manages annually for operating surpluses that can be set aside into a board-designated cash reserve to be spent for unanticipated and adverse events.
Change capital funds improvements in efficiency or quality of program or operations and/or adjustments to the size and scope of the organization. It is an investment in the alignment of an organization's fixed costs to its reliable, recurring revenue. It is spent down as needed with the explicit expectation that it will lead to improved recurring net revenue (i.e., surplus) to sustain delivery of programs.	Two human services nonprofits are considering a formal collaboration that would combine their programs in one space. The planning and implementation periods will span three years and require an infusion of several million dollars, to be spent down to cover temporary deficits while the partners make investments in joint development and marketing capacity that will generate future net revenue.
Recovery capital helps restore an impaired capital base by replenishing depleted working capital and facilities capital and by reducing or restructuring debt and other obligations. Some nonprofits require recovery capital before they can effectively use change capital.	A community-based organization has several years of deficits, which depletes its cash and requires it to take on debt. Future operating surpluses will not likely be sufficient to pay off its liabilities. The organization requires a targeted fundraising campaign for recovery capital.
Facilities & Equipment capital represents funds earmarked for investments in new fixed assets, including such items as: real estate, costumes and sets, technology and other major furniture or equipment. The funds may be raised expressly for specific acquisitions or upgrades, as well as accumulated in reserve to meet future needs.	A theatre renting its performance space launches a $5 million capital campaign and secures $2 million in bank financing to purchase and build a permanent home. For long term durability, management incorporates into the campaign fundraising for a facility reserve to pay for future repairs and replacements and a risk reserve to cover anticipated early revenue shortfalls/ expense overruns in the early days of operating in a larger space.
Endowments typically represent donated capital that is kept intact (and grown) to generate investment income. The corpus of an endowment is typically permanently restricted, though NFF encourages nonprofits to prioritize raising flexible forms of capital since endowments need to be large to generate adequate annual income and may compete with other fundraising efforts.	After building its major donor base over many years, a symphony launches a campaign to raise an unrestricted, but board-designated, endowment. The target amount for the board-designated endowment will yield annual investment income to support a small percentage of the symphony's operating budget.

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