Recent Research on Nonprofit Financial Literacy

September 2014


Abstract: Nonprofit organizations in the United States depend on a diverse set of funding streams to sustain their operations. This study examines the ability of nonprofits to leverage funds from the private sector during the current economic downturn within four areas receiving federal funding for community and economic development. Both survey research and individual interviews were used to examine how nonprofits within these areas are incorporating their board members and community leaders to continue services during a time of resource scarcity.


Abstract: This article divides financial issues into capacity and sustainability in two time frames: long and short. Long term emphasizes maintaining services; short term emphasizes resiliency. An organization's long-term financial capacity is sustainable if its rate of change is sufficient to maintain assets at their replacement cost. A key contribution of this study is a sustainability principle that gives managers short-term budget surplus targets needed to achieve this objective. The formulas are applied to national data to give a picture of the sector and establish benchmarks for “normal” practice. “Ordinary nonprofits” are active public charities without endowments that are not primarily membership associations or grant makers.


Abstract: Does current accumulated wealth by nonprofit organizations influence contributions from individuals? Existing research demonstrates that financial reserves aid program continuity during economic downturns. Yet donors, charity watchdogs, and policy makers voice concern about accumulated wealth in nonprofits. This empirical analysis examines whether the expected negative
relationship occurs when donors perceive accumulated wealth as excessive. The results support the conclusion that future contributions are negatively affected when wealth levels are deemed excessive. Nonprofit managers concerned that accumulated wealth will diminish donations should consider financial strategies that will allow their organizations to build modest—but not excessive—reserves.


Abstract: Operating reserves allow nonprofit organizations to smooth out imbalances between revenues and expenses, helping to maintain program output in the presence of fiscal shocks. We know surprisingly little about why nonprofits might save operating reserves and what factors explain variation between organizations' savings behavior. Findings suggest that operating reserves are reduced in the presence of concentrated public funds, access to debt, fixed assets, and endowment. However, size is not an important predictor, indicating that the lack of reserves is not limited to small nonprofit organizations but is instead a sector-wide issue. Significant numbers of nonprofits maintain no operating reserves at all. One potential explanation is that organizations discount the benefits of reserves because they are evaluated on spending, focusing instead on the “benefits of costs.” This preference for spending over reserving may also help explain the general lack of liquidity in the sector beyond operating reserves alone.


Abstract: Building on the impressive body of research on issues of nonprofit revenue choice and mix, this research empirically tests Foster and Fine’s claim that revenue concentration contributes to the growth of nonprofit organizations. Using National Center for Charitable Statistics (NCCS) digitized data (1998-2003), the authors test whether revenue concentration is a viable revenue-generating strategy that can help bolster a nonprofit’s financial capacity. Overall, study findings refute the mythology of revenue diversification; the authors find that implementing a revenue concentration strategy generates a positive growth in one’s financial capacity—in particular, a growth in one’s total revenue, over time. Contrary to the prevalent charges laid at the door of high administrative and fundraising efforts by some, the authors find that in order to support financial capacity growth, nonprofits must make positive investments in favor of administrative and fundraising support but not in the form of high executive salaries.


Abstract: This article evaluates the use of monetary accounting and other financial management tools in the governance of nonprofit organizations. Drawing on
Weber’s insights on monetary accounting, the article elaborates structural differences in the financial management of nonprofit and business organizations. The article demonstrates that the accounting and budgeting technologies used by business cannot offer substantively rational guidance to managers of nonprofit organizations. It is argued that managing for social outcomes requires nonprofits to experiment with organizational structures and processes that promote coherence between the diverse value rationalities which underpin their service aims and the allocation of the unit’s financial resources.


Abstract: Intensive interviews were conducted with CEOs and board chairs (n = 18) to explore the criteria they use to compare and contrast funding sources common to nonprofit organizations. The interview protocol used in the study is distinctive for: (1) the amount of data it generates from relatively few interviews, and (2) its power in eliciting the underlying values and assumptions of interviewees rather than imposing the researcher’s frame of reference as is the case with traditional forced-choice questionnaires and interview protocols. The nonprofit leaders who were interviewed in this exploratory study seem to employ a strategic perspective in their evaluation of funding sources, asserting to the researchers that they use evaluative criteria such as the extent to which the funding source can catalyze other resources, the alignment of the funding source with the mission of the organization, and the sustainability of the funding source over time.


Abstract: Economic theory suggests managers make decisions to allocate resources based on marginal analysis, regardless of how such allocations influence performance measures. Even so, anecdotal evidence suggests that managers of charities deviate from marginal analysis and respond to external pressure from donors to achieve desired performance measures, computed as average ratios of spending on program activities to total spending. We examine whether spending patterns reflect concern and donor pressure by comparing marginal and average spending patterns. We provide evidence that, in most instances, average spending patterns do not change when budgets increase. That is, average program ratios do not change when budgets grow. We find that when budgets decrease, however, charity managers make resource allocation decisions that decrease the average program ratio. This asymmetry suggests that charity managers are more willing to report declining program ratios when budgets decrease, but not improve program ratios when budgets increase. We also find that charities that are small, rely little on contributions, receive no government support, and report zero fundraising make resource allocation decisions that decrease the program ratio when budgets increase.
This finding suggests that some charities perceive greater pressure to conform to donor pressure than others.


Abbreviated Executive Summary: This study integrates two levels of analysis: community and organizational levels. Examining measures of financial health at the organizational level may identify organizations that are at increased financial risk; and examining aggregate variations across communities may identify underserved communities at increased risk of loss of vital social, health, and human services. The data used for this paper is drawn from the National Center for Charitable Statistics (NCCS) 2005 Digitized Data file which contains 501c(3) public charities that filed a Form 990 or 990-EZ from 1998-2003. The Digitized Data files contain variables from every line of the pre-2008 Form 990. For demonstration purposes, this paper will only examine a cross section of this data, using 2003, the most recent year in the dataset. The geographic scope for analysis is San Diego County, California. Specifically, the geographic units of analysis are zip codes. Results suggest that the majority of nonprofits would not be able to withstand a financial shock that disrupt revenue streams for any length of time. This also varies across zip codes in San Diego County with the least vulnerable organizations located in urbanized areas where needs maybe the greatest. Educational institutions, including higher education institutions, have a greater MULNA compared to human service nonprofits. Public and societal benefits may also have higher percentage of earned income or even donative income from individuals in the form of membership dues (i.e., Rotary clubs along with many fraternal organizations are categories as public and societal benefit organizations). Human service organizations, in contrast, may offer a broader range of services and thus serve a broader range of clientele. Human service organizations may also rely, to a larger extent on government and foundation grants and thus restricted revenue devoted to programs rather than any type of expenses (i.e., salary or administrative costs).


Abstract: This research paper analyzes the impact of the recent Great Recession on nonprofit organizations. More specifically, it studies the impact of the recession on their ability to raise funds and remain financially viable. The four key research questions discussed are: What has been the overall impact of the Great Recession on nonprofit organizations?; How has the Recession impacted the fundraising capability of nonprofit organizations?; How well have different types of organizations weathered the Great Recession’s impact on their revenue sources?; and What strategies have nonprofit organizations found to be useful in surviving this severe downturn? The study uses the most recent data on nonprofit financing from 2007-2010. The results
show that nonprofits as a whole have seen general declines in contributions and funding. But there are clear differences in the impact of the eleven sectors studied. Moreover, the size of the organization matters as does its main source of revenue. The paper concludes with a set of strategies that have been successful at stemming the decline in nonprofit funding. The study provides valuable insight into the ability of nonprofit organizations to survive such difficult economic times and also to reveal the various practices that have been successfully utilized for their survival.


Abstract: Governments contract with human service nonprofits to provide services in complex environments (Frahm & Martin, 2009). This article builds on the robust literature of public contracting for human services, but considers the effect of contracting on the contractor rather than the government. Using the National Survey of Nonprofit Government Contracting and Grants, conducted during the financial recession, we consider how contracting practices are harming trust. We find that human service nonprofits are more likely to cut salaries and jobs due to having government contracts, leading one to question whether the partnership mode of contracting will remain effective.


Abstract: This study examines the causes and consequences of internal control deficiencies in the nonprofit sector using a sample of 27,495 public charities from 1999 to 2007. We first document that the likelihood of reporting an internal control problem increases for nonprofit organizations that are in poor financial health, growing, more complex, and/or smaller. We then present evidence that the disclosure of weak internal controls over financial reporting is negatively associated with subsequent donor support received after controlling for the current level of donor support and other factors influencing donations. We likewise report a negative association between internal control problems and subsequent government grants. Our results suggest that donors and government agencies, important sources of capital for nonprofit organizations, react either directly or indirectly to internal control information.


Abstract: The nonprofit sector is evolving rapidly as organizations expand their focus on efficiency, sustainability, and accountability. Public agencies are changing as well, embracing collaborative public management and fostering stewardship-based contracting approaches. But how have all these developments influenced
government funding for nonprofit organizations? Which types of nonprofits procure public funds, and how do patterns change over time? Based on 200 interviews with leaders of nonprofit organizations in the San Francisco Bay Area, I argue that standard management strategies for achieving mission have become increasingly relevant for procuring government grants and contracts. Results indicate that professionalization and collaboration are consequential for receiving government support, net of prior funding, and collaboration also contributes to total support from government. Building from these results, I conclude by discussing the opportunities and challenges of public–nonprofit relations.


Abstract: This paper examines the behavioral influence of federal grants on nonprofit firms. The topic is of particular concern governments who wish to stimulate the private provision of public services. Recent research shows that grants may inadvertently reduce private sector provision, by causing a reduction in nonprofit fundraising activity. This study extends work on federal grants by examining the differential influence of incentive versus lump-sum style grants on the subsequent expenditures of recipient nonprofit firms. The paper draws detailed grant data from the Federal Assistance Award Data System (FAADS), which includes structural characteristics of the grant. Empirical results demonstrate that the structure of the grant matters a great deal. Though relatively uncommon in the data, incentive grants are particularly effective at stimulating both additional fundraising activity and output of the firm. More widespread use of incentive grants could mitigate the tendency of government grants to reduce private provision of charitable goods.


Abstract: Nonprofit organizations draw financial support from multiple sources including contributions, earned income, government support, and returns on investment, but the source of variation in income portfolios is not well understood. The authors draw on a ‘‘benefits theory of nonprofit finance’’ to illuminate the relationship between the programs and services that a nonprofit provides and the sources from which it obtains income. The authors analyze detailed revenue and expenditure data from eighty-seven Jewish Community Centers, estimating models that show significant associations between expenditures on particular types of services and the sources of an organization’s revenue. Specifically, expenditures on services of a more private goods nature are associated with greater reliance on earned income while expenditures on services of a more public goods nature are associated with greater reliance on charitable sources. Results are potentially important for nonprofit management practice because they suggest closer coordination of an organization’s resource development strategy with its programming.

Abstract: This article offers a new approach to measuring organizational financial health based on the financial sustainability model. The objective in introducing these new financial indicators is to enable nonprofits to better manage their financial health and more confidently assure their ongoing financial sustainability. Usable measures of solvency, liquidity, and financial flexibility are introduced. Some of these measures are identical to those already in use, some are adapted from other ratios, and yet others are newly-developed. Actual data from a human services nonprofit organization are used to illustrate calculation of these measures. These measures are also placed in general, immediate-term, short-term, and medium-term classes, category scores calculated, and these category scores are combined into a numerical financial health index value ($\Phi$). C-suite managers and board members may use this single index value to gauge their organization’s financial health relative to the next three years of operations. Managers may choose to remedy poor financial health by targeting improvement in individual measures or categories, and may choose to adopt written liquidity, debt, and investments policies consistent with those targets.


Abstract: This paper illustrates and provides a framework for responses nonprofit organizations may make to the economic forces of slow economic growth, high unemployment, plunging stock prices, low inflation, low interest rates, an unstable dollar, and, often, increased demand for the organizations’ services. The nature of nonprofit organizations lies behind many of these responses, and informs responses for similar for-profit businesses. Astute liquidity management enables organizations to survive and thrive in an uncertain external environment. The findings will benefit nonprofit and corporate treasury professionals, as well as those who advise these organizations through board membership or consulting arrangements.


Abstract: Nonprofit organizations are a vital part of the U.S. social safety net providing a wide range of services in the modern welfare state. While many individuals and families turn to nonprofits for help during economically challenging times, these organizations themselves often face turbulent funding environments and uncertain financial futures. Nonprofit stakeholders urge within-sector collaborations (with other nonprofits) and cross-sector collaborations (with for-profit firms and government agencies) as a means to achieve efficiencies in service delivery, stretch donation dollars, and increase the long-term fiscal sustainability of the nonprofit sector. While increased financial stability is a presumed outcome of nonprofit
collaborations, we know little about the antecedent effect of nonprofit financial vulnerability on collaboration. Using data from a survey of nonprofit executive directors in Boston, Massachusetts, this paper examines how nonprofit financial vulnerability influences nonprofit collaborations. We find that nonprofit financial vulnerability decreases the likelihood of both within- and cross-sector collaborations. Resource dependence on private funding increases within-sector collaboration with other nonprofits, while reliance on government funding increases the likelihood of cross-sector collaboration. Cross-sector board linkages also increase the likelihood of collaborations. Nonprofit stakeholders should consider these findings when promoting collaboration as a path to nonprofit fiscal sustainability.