

Passion & Purpose

Restructuring, Repositioning and Reinventing:
Crisis in the Massachusetts Nonprofit Sector

A CALL TO ACTION

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Foundation
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May 2009

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Preface

In June of 2008, when the Boston Foundation published its first major report on the state of the nonprofit sector in Massachusetts, called *Passion & Purpose*, one of the goals was to explore ways to enhance this powerful sector's financial viability and maximize its impact. The data in the report uncovered the strength and the vulnerabilities of the sector. With \$87 billion in revenues, \$207 billion in assets, and close to 450,000 workers, the Massachusetts nonprofit sector emerged as a major economic force. But the impact of the sector's growth—combined with a lack of growth in financial support and increasing community need—had taken its toll, resulting in a weakening economic condition. By 2007, the sector had just about recovered from the recession that started in 2001 and worsened after 9/11. We had no way of knowing, of course, that the next recession was just around the corner—and that it would be the most serious economic downturn since World War II.

Our current national calamity must be seen in the context of a fiscal crisis in Massachusetts, which some are calling the worst in the state's history. With so many nonprofits heavily dependent on state funding—especially those organizations that serve the most vulnerable people in our community—this will only exacerbate the sector's fiscal distress.

Passion & Purpose sounded a very serious alarm about how economically vulnerable the sector is, and issued a clarion call to the state's nonprofits—especially those that are small and medium-sized—to consider innovative, even bold strategies to buoy their fiscal health. Now the hard times are most definitely here and it is crucial that nonprofit organizations and their stakeholders work very quickly—and together—to take bold actions to ensure their survival.

The Boston Foundation is deeply committed to working with our partners to discover opportunities within this crisis. In this spirit, it has allocated \$500,000 for Technical Assistance & Capacity Building—and provided support to the Massachusetts Nonprofit Network to coordinate the flow of information about federal stimulus funds.

The Foundation also hosted 14 workshops in February and March of 2009, attracting some 300 participants representing 190 organizations, to discuss topics such as financial management, leadership, contingency planning, and fundraising in tough economic times. And the Foundation is supporting and encouraging mergers and alliances among nonprofits through \$150,000 in technical assistance and grants to organizations serving the AIDS/HIV community, several theater groups, and a number of housing and community development organizations.

It will take time, courage and ingenuity, but I am optimistic that, working together, the Commonwealth's remarkable nonprofit sector will reinvent itself from within, which it has done before—and not only weather the perilous times we find ourselves in, but emerge from them stronger and more resilient so that they can fulfill their crucial, irreplaceable role in our communities and neighborhoods.

Paul S. Grogan
President and CEO
The Boston Foundation

Background

Passion & Purpose: Raising the Fiscal Fitness Bar for Massachusetts Nonprofits was released as an *Understanding Boston* report in the spring of 2008. It describes Massachusetts' 36,000 nonprofits by linking them to their value propositions in three broad categories. The first is *Grassroots*, representing small groups with budgets of \$250,000 or less and missions that encourage civil society through action and volunteerism. The second category is *Safety Nets*, or organizations with budgets between \$250,000 and \$50 million that provide crucial services and enhance the quality of our lives. The third is *Economic Engines*, or large institutions with more than \$50 million in annual expenses that contribute mightily to the economic health of the entire region. The report serves as a primer about the sector and invites a 'call to action' to the nonprofit sector and its stakeholders to improve the financial health of the state's nonprofit sector through restructuring, repositioning and reinvention.

The Commonwealth's nonprofits generate \$87 billion in revenue annually, represent \$207 billion in assets, and employ close to 450,000 workers. While the report confirms the vital importance of the nonprofit sector to the Commonwealth's civic, social and economic health, and highlights its significant economic impact, it also paints a detailed picture of a sector that is underfunded, overstretched and vulnerable to cuts by a state government that faces increasing financial constraints itself.

In recent years, the number of public charities in the state has virtually doubled, despite almost no growth in population or funding sources. Some 40% of the sector loses money every year, with Safety Net organizations—especially those with budgets ranging from \$250,000 to \$1 million—in greatest distress.

The coming years present a sobering financial picture—where the impact of the economic recession, declining government revenues and a scaled back philanthropic sector will extend the crisis being faced by nonprofits beyond typical downturns. But the nonprofit community's capacity for deep introspection, amazing resilience and history of innovation suggest the potential of a hopeful future for the sector.

The goal of the 2008 *Passion and Purpose* report was to strengthen the sector so that it would be better positioned to deal with tough challenges. There was no way of knowing that the hard times would come less than six months after the report was released. Its 'call to action' recommendations—designed to strengthen the Massachusetts nonprofit sector through restructuring, repositioning and reinventing—are even more urgent today.

Introduction

In less than a year, the global economic crisis—which has thrown federal, state and local economies into a state of distress—has speeded the timetable for achieving some of the bold changes called for in *Passion and Purpose*, including new levels of collaboration, mergers and consolidations, and increased advocacy on behalf of the sector as a whole. This white paper is designed to inform an ongoing discussion about the ways in which the recession is affecting nonprofits nationally—and in Massachusetts—and begin to explore potential “utility of trouble” responses on the part of nonprofits, their funders and their stakeholders. The goal is not only to weather this storm, but to emerge stronger than ever.

On December 1, 2008, the National Bureau of Economic Research, which decides whether the economy has fallen into recession, announced that the United States had indeed been in recession since December of 2007. Pronouncements since that day, by members of the Obama administration and by economic experts, suggest that the recession may be with us for quite a while to come. What are the ramifications of this for nonprofits and funders?

According to the *Guide to Navigating the Financial Crisis*, developed by the Nonprofit Finance Fund (NFF), the nonprofit sector may have felt the effects of the recession earlier than other sectors—and may take longer to recover. Signs of the recession have included: immediate downward pressure on government, philanthropic and “discretionary” individual revenue sources; limited and/or more expensive access to credit; and increasing demand for basic and critical human services.

A recent national survey of some 950 nonprofit professionals by the NFF presents some of the challenges facing a sector that is continually being asked to do more than less. Half of those surveyed expected that the recession will have long-term or permanent negative effect on their organizations:

- Only 12% expect to operate above break-even this year;
- Just 16% anticipate covering their operating expenses in 2009 and 2010;
- 31% don’t have enough operating cash in hand to cover more than one month of expenses, and another 31% have less than three months’ worth; and
- 93% of lifeline organizations anticipate an increase in demand in 2009.

As nonprofits look to foundations for increased funding to weather the storm, the statistics are bleak. While foundations still held more than \$530 billion at the end of 2008, nearly \$150 billion in charitable resources has been lost in a single year. According to the Foundation Center’s latest estimates, 2009 giving will decrease in the range of the high single digits to low double digits, with two-thirds of foundations expecting to reduce their giving. With foundation assets down 22%, some 74.2% of community foundation respondents anticipate reducing their giving in 2009, compared to 67.7% of independent foundations and 51% of corporation foundations. Looking ahead, the Center forecasts that foundation giving appears likely to decline further in 2010.

The State of Massachusetts Nonprofits

In January of 2009, Management Consulting Services—itself a victim of the recession—conducted a survey of nonprofits in Massachusetts to gauge the impact of the economic crisis on the nonprofit sector in the Commonwealth. The survey found that two-thirds of the sector is experiencing fiscal distress: 67.6% of respondents anticipate a decrease or delay in their funding and donations—and 30% expect revenues to decrease more than 10% during the current fiscal year.

These lowered financial expectations must be viewed in the context of higher demand for services. A 2008 Nonprofit Finance Fund survey that looked at individual states tells us that 76% of Massachusetts nonprofits reported seeing an increase in demand for their services last year. And most of the respondents (86%) anticipated a significant increase in the need for services in 2009. The survey also reported on the fiscal health of the Commonwealth's nonprofits, finding that: 16% of them had no cash available; 14% had enough cash to cover just one month of expenses; and only 22% had enough cash to cover more than six months of expenses.

The survey asked the state's nonprofits what special actions they have taken or plan to take in 2009, finding that: 65% have developed a "worst case scenario" contingency budget; 42% have reduced staff or salaries; 42% have frozen all hires and current staff salaries; 23% have reduced benefits; 7% have collaborated with another organization to reduce administrative expenses; and 8% have merged with another organization.

Some of these actions are driven by the fact that Massachusetts nonprofits are seeing a decrease in government funding, with 17% reporting that they are experiencing longer than usual delays in receiving funds. Recent news about additional Massachusetts revenue shortfalls suggests that the state will be forced to make deep cuts to programs for years to come.

According to a May 6, 2009 article in *The Boston Globe* by Matt Viser, several economic specialists have advised state officials to prepare for at least four years of budget cuts, prompting Senate President Therese Murray to say: "It's uglier than we thought. We decimate our human services and education systems, or we try to come to some kind of revenue [solution]." The article reported that, "...the problems are expected to be so widespread, the solutions so elusive, that the state may have to rethink the size of its commitment to big-ticket programs such as its landmark health care coverage plan, aid to cities and towns, and education funding..."

Impact of the State Budget

The state is facing the most severe fiscal crisis in memory. According to the Massachusetts Budget & Policy Center, when the budget process began in January, the state faced a gap of some \$3.5 billion, even after more than \$700 million in cuts and savings in FY09. This gap was caused, in the short term, by declines in tax revenue as a result of the recession. In January, the amount of tax revenue the state expected to receive in FY09 was about \$2 billion less than the amount anticipated. In addition, the state was expecting virtually no tax revenue growth in FY10, while the cost of providing the same level of services the state provided in FY09 was expected to increase by about \$1.5 billion because of inflation and case load changes.

To close this gap, the Governor and the House proposed a combination of spending reductions, new revenues, the use of federal stimulus money and, in the case of the Governor, reserves.

Including the FY09 cuts, both the Governor and the House recommended more than a billion dollars in cuts, about a billion dollars in revenue and some \$1.5 billion in federal stimulus funds.

On May 6th, the Governor announced a new estimate for FY10 tax revenue that is almost \$1.5 billion below the January estimate. This means that the Senate will need to raise more revenue or implement more cuts than the House or the Governor.

While cuts made earlier this year were concentrated in health care, human services and higher education, this budget proposal will particularly affect lower income communities, which rely most on local aid. The proposal would reduce unrestricted local aid by 16.4%. It is important to note that while several areas show very modest cuts or modest increases, level funding wouldn't be enough to avoid reductions in services. In some areas of human services for instance, there is the additional issue of caseloads increasing as the economy deteriorates and more people need services.

Utilizing the “Utility of Trouble”—Some Emerging Trends

For years, foundation leaders and experts in the nonprofit field have suggested that the sector has grown to be too large and diffuse—and desperately needs to consolidate. The current economic crisis presents nonprofit organizations with an opportunity to radically change practices that have hobbled their ability to be effective in meeting their goals.

A number of respondents to the 2008 Nonprofit Finance Fund survey of America's nonprofits expressed interest in exploring new ways to manage through the current crisis and beyond: 58% reported that they would like to conduct scenario planning; 52% wanted help communicating their financial picture to their boards and/or funders; and 34% were interested in program profitability analysis, with an eye to greater fiscal health.

In its *Guide to Navigating the Financial Crisis*, the NFF suggests that nonprofit leaders need to start asking tough questions about program, finance and management. The Guide also makes suggestions to nonprofits, encouraging them to conduct a review of their financial assets, engage in contingency planning with board members and funders about how to respond to higher demand for services, and avoid large investments in fixed assets and infrastructure.

Restructuring, Repositioning and Reinventing

The ‘call to action’ recommendations that were expressed in last year's Boston Foundation report *Passion & Purpose* emerged from conversations with numerous nonprofit stakeholders and were aimed at improving nonprofit financial health and the alignment of money and mission for greater social impact. They were structured around three powerful concepts—restructuring, repositioning and reinventing. Today, as the nonprofit sector operates within the context of an altered economy, embracing these recommendations is more urgent than ever.

The report challenged the Massachusetts nonprofit sector to seriously consider mergers, strategic alliances and collaborations as a strategy to strengthen organizational balance sheets, enhance offerings, and create economies of scale and efficiency. The work has already begun.

To support nonprofits struggling through tough times, the Boston Foundation held 14 workshops in the spring of 2009 that were offered at no cost to all nonprofits from across the state— attracting some 300 participants from 190 organizations. Geared toward executive directors,

board members and senior managers, workshop titles included: *Coping with the Stresses of the Recession: Tips and Techniques for Managing the Finances of Your Nonprofit*; *Managing Your Organization in Hard Times*; and *Strengthening the Fundamentals of Fundraising*. Interestingly, the finance-oriented workshops were undersubscribed, while those that focused on fundraising were over-subscribed. Participants reported that they learned a great deal in the sessions—but also found it very helpful to share stories and ideas with other nonprofit staff and board members. A number of organizations reported that they were in the process of developing contingency plans based on various financial scenarios.

Clearly, the recession is sparking fresh ways of thinking and new alliances. In Roxbury, Dorchester and Mattapan, nonprofit, community and political leaders have created a task force to examine the organizations in those neighborhoods and analyze their operations in order to discover new models of service delivery, highlight where redundancies occur and possibly identify some nonprofits that are simply not powerful enough to struggle through the recession. Actions of the Nonprofit Stabilization and Recovery Working Group amount to a call for innovation that starts with increased networking among nonprofit leaders to find ways that they can partner, collaborate or engage in other entrepreneurial thinking. Other groups, like the Massachusetts Council of Human Service Providers, are exploring new revenue models for the Human Services sector with an eye toward social enterprise strategies. Community Development Corporations hit hard by the dual impact of the economy and the housing crisis are exploring new organizational models and innovative strategies to bolster their impact and increase their viability.

The economic crisis has led several organizations to pursue creative and timely mergers. One that received national press coverage is between two Boston-area nonprofits that serve the Latino community: Centro Latino de Chelsea and Concilio Hispano. Both organizations were facing significant reductions in funding and Concilio was lacking a leader—and understaffed in other areas. Centro Latino wanted to expand, but lacked the resources. Then Juan Vega, Centro's Executive Director, read *Passion & Purpose*, the Boston Foundation's report on the nonprofit sector, which encouraged nonprofits to consolidate and merge in order to strengthen their capacity to serve their constituents. On April 1, 2009 the two organizations merged and became Centro Latino Inc., based in Chelsea. Previously Centro Latino de Chelsea had a \$1.5 million budget and Concilio's budget was around \$1 million. The new organization—with a budget of \$2.4 million and leaner more cost-effective administrative operations—will be able to expand its services, providing health, educational and workforce training services to 7,000 people in Latino and immigrant communities in at least two-dozen cities and neighborhoods.

Consolidation is a strategy that is being seriously considered for three of the Boston area's leading HIV/AIDS organizations: AIDS Action Committee, JRI Health and Cambridge Cares About AIDS. The three organizations are hoping to increase the effectiveness of their service delivery operations to people living with AIDS, and to find some efficiencies in the system. After a period of analyzing research and data findings, the three groups are edging closer to a proposal about how to move forward.

A recent analysis by The Bridgespan Group of 11 merger filings in four states: Massachusetts, Arizona, Florida and North Carolina, found that more than 3,300 organizations reported engaging in at least one merger or acquisition between 1996 and 2006. The survey indicates that 20% of nonprofits say that mergers will play a role in their survival during the recession.

Looking to Stimulus Funding for Support

Nonprofit leaders are also organizing, with the assistance of the Massachusetts Nonprofit Network, a state-wide association of nonprofits to lobby for the sector's fair share of national stimulus funds. While the public perception of the American Recovery and Reinvestment Act of 2009 (ARRA), usually referred to as the "Economic Stimulus Package," may be that it focuses on building roads and bridges and private sector investments, in reality the vast majority of ARRA funding is ideally suited to the enormously broad nonprofit sector for the delivery of services. The first goal of the stimulus package is to inject significant federal funding into our national economy to save or create jobs and to assist those most impacted by the recession. The second goal is to ensure that the bulk of the federal government's spending is used to make major investments in transportation, environmental protection, technological advances in science and health and other infrastructure improvements that will provide long-term economic benefit to the country.

Of the \$787 billion that will be spent nationally through ARRA over the next two years, \$370 billion will be distributed through formula and block grants to the states. An additional \$85 billion will be distributed through a competitive grant process—through which the federal government will issue grants to organizations to perform certain functions—and another \$65 billion will be distributed through direct contracts—through which the federal government hires a particular entity to perform a service of some kind.

Over the next two years or so, Massachusetts will receive some \$8.7 billion in federal stimulus funds, plus an additional \$5.2 billion through tax benefits to residents of the Commonwealth. ARRA funding is targeted for specific purposes—and the bulk of the funding will be distributed by federal agencies, primarily through existing programs and mechanisms. While much is still undecided about funding opportunities, deadlines for applications to the federal government are quickly approaching. The Massachusetts Nonprofit Network is monitoring prospective funding streams for nonprofit organizations in Massachusetts, including deadlines for applying for funding as they become available. It is suggested that leaders of nonprofit organizations visit the Network's website, at www.massnonprofitnet.org, regularly for updated information.

A Call to Action

Whether the recession stretches through the rest of 2009 and into 2010, or ends earlier than expected, the nonprofit sector in Massachusetts should take advantage of the current atmosphere of urgency to embrace the recommendations of the *Passion & Purpose* report and consider a whole host of innovations that will serve it well during hard times and allow it to flourish in better times. The state's nonprofit sector simply must embrace change. There is a tremendous amount of creative thinking going on across the country and throughout Massachusetts about what "change" means and how to go about achieving it. The larger context is that there may never be a more important time for stakeholders to come together around a common agenda.

Through innovative service delivery, collaborations, mergers and other alliances and economies, nonprofit leaders are thinking beyond their own organizational goals and focusing on the tremendous need that exists in the community for their unique services. If the sector continues to come together in creative partnerships, as it has been, and engages in an open exchange ideas, it will emerge stronger than ever.

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