

## Adapting to an Outcomes-Based World: What Every Nonprofit Needs to Know

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**Nonprofit Finance Fund**

Presented for:



# Nonprofit Finance Fund (NFF): Where Money Meets Mission



**Dedicated to keeping nonprofits in balance and in business.**

## **Serving thousands of nonprofit and funder clients since 1980**

- \$280 million in loans; \$100 million in New Markets Tax Credits; over \$1 billion in capital leveraged for nonprofits
- 500+ Nonprofit Business Analyses; 200+ nonprofit finance workshops
- Formed hundreds of strategic partnerships to advance nonprofit sector

## **Nationwide network of experts in nonprofit finance**

- Lending
- Financial advisory services and workshops
- Financial advocacy across the nonprofit sector

## **Serving nonprofits nationwide from five local offices**

- Northeast: Boston, New York
- Mid-Atlantic: Philadelphia
- West Coast: San Francisco, Los Angeles

*"[NFF is]... arguably the most influential voice in the ongoing effort to reshape thinking and practice about nonprofit capitalization."*

*– The Nonprofit Times*

## State of the Sector

- Adapting to the new reality

## Intellectual Capital

- Building outcomes measurement

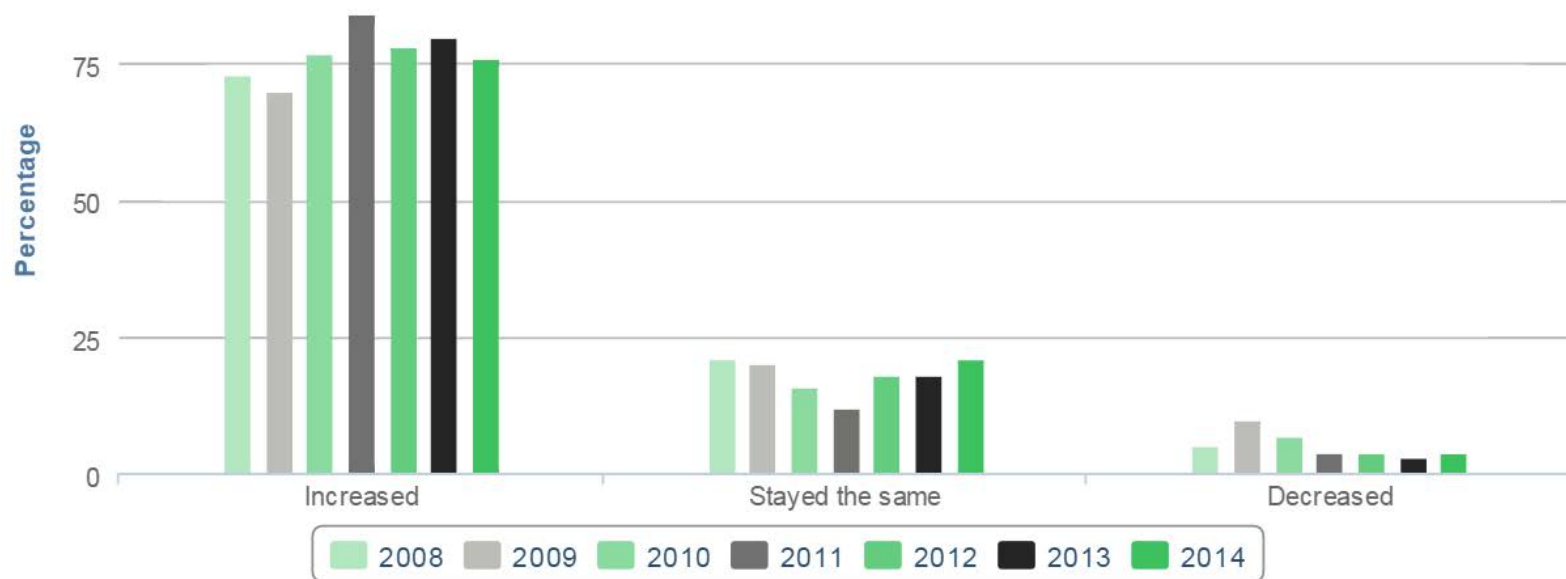
## Financial Capital

- Understanding the full cost of doing business
- Determining financial resources needed to fund adapting to the new reality

# A Frayed Safety Net: Seventh Year of Increasing Demand for Services

**5,451 (MA=302) leaders** responded to NFF's 7<sup>th</sup> State of the Sector Survey

- 29% Human Service
- 17% Arts/Culture/Humanities
- **76% (MA=78%) of respondents reported an increase in demand for services**, the 7th straight year of increased demand
- **52% (MA=49%) were unable to meet demand in 2014**—the same percentage anticipate not being able to meet 2015 demand



# 53% of Nonprofits Subsist with Three Months or Less Cash on Hand

## Financial results in 2014 were similar to past years:

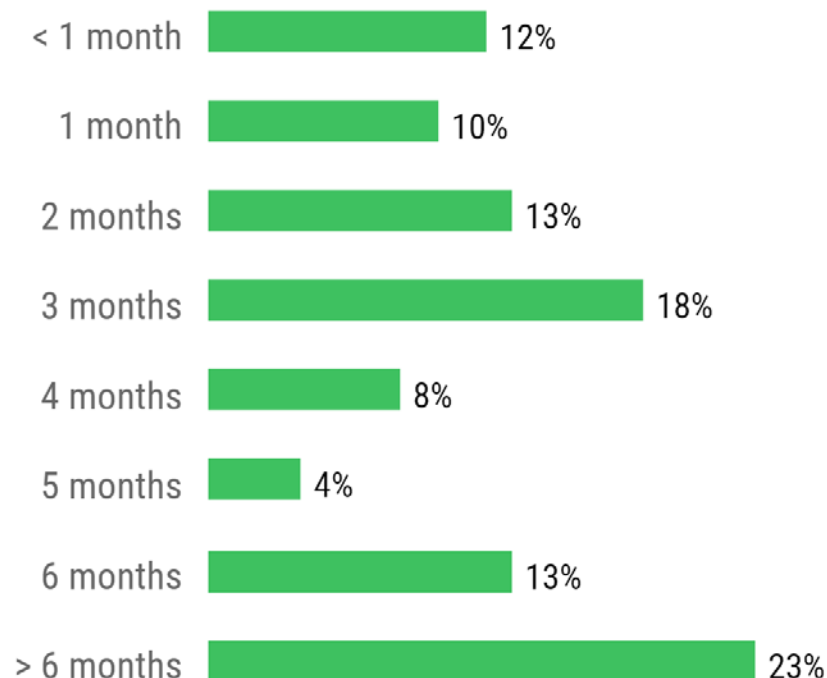
- 24% had a deficit
- 29% broke even
- 47% had a surplus

## ...and these deficits were largely unplanned:

- 57% unplanned
- 43% planned

### Months of Cash Readily Available

Number of respondents: 4439



**Achieving long-term financial sustainability was the #1 challenge identified by 32% of survey respondents**

# The Funding Environment is Changing

	Status quo of...	Emerging practices of...
Government	<ul style="list-style-type: none"><li>■ Cost reimbursement</li><li>■ Annual contracts</li></ul>	<ul style="list-style-type: none"><li>■ Investing in “What works”</li><li>■ More Pay for Performance &amp; increasing Pay for Success efforts</li></ul>
Philanthropy	<ul style="list-style-type: none"><li>■ No expectations of return on funds disbursed</li><li>■ Old money, high net worth individuals and institutions</li><li>■ Motivated by altruism</li></ul>	<ul style="list-style-type: none"><li>■ Impact investing: expectation of financial &amp; social return</li><li>■ New money, younger, living donors &amp; family foundations</li><li>■ Purchasing social outcomes</li></ul>

- **Let's examine the challenges and opportunities of this changing funding environment**
  - There is a growing “investment mindset” in the funding of social programs.
  - Why is the idea of “investing” in the social sector a good or bad thing?

# The Funding Environment is Changing

## Challenges

- Understanding true costs & capacity
- Measurement can be complex
- Evaluation and metrics not yet “standardized”
- Evidence/data is still nascent for certain programs and interventions

## Opportunities

- New funding/revenue streams during a time of government retrenchment
- Scaling potential of effective programs
- Multi-year contracting/capital
- Transparency and efficient use of public and philanthropic dollars



## State of the Sector

- Adapting to the new reality

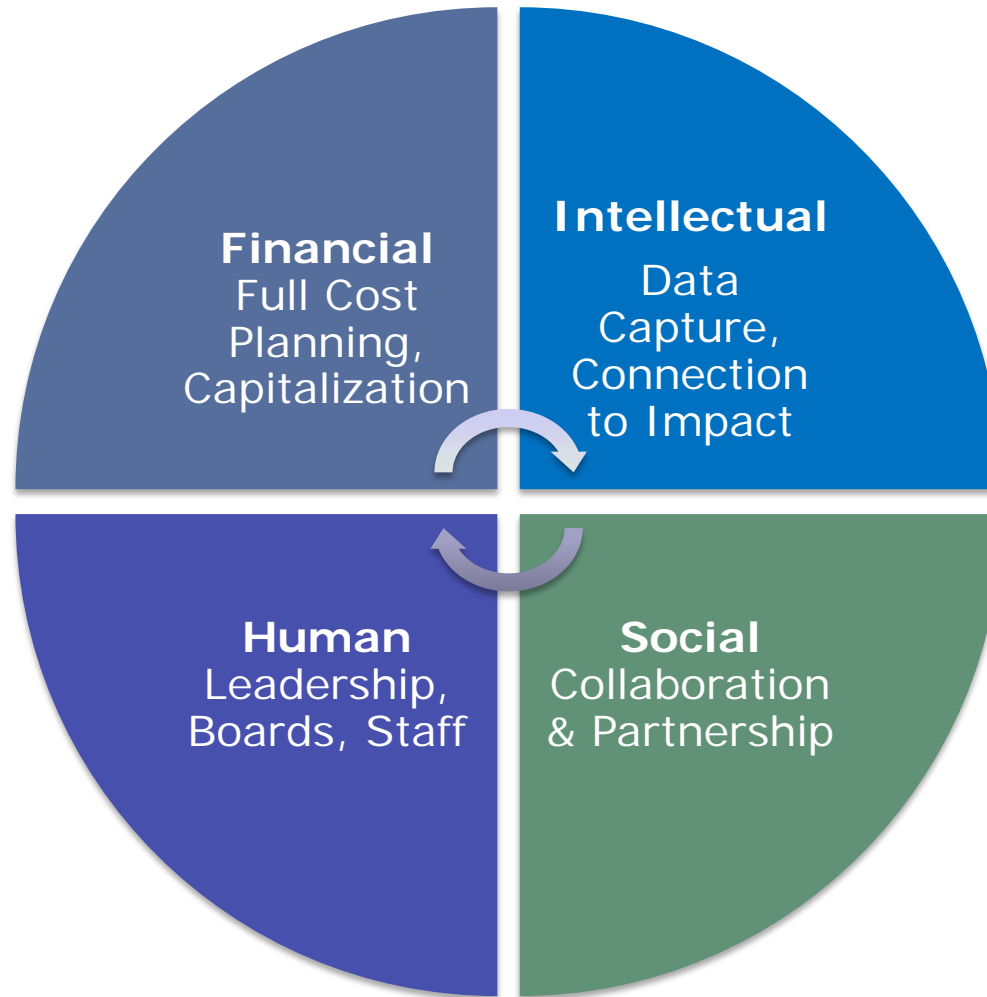
## Intellectual Capital

- Building outcomes measurement

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# Building Organizational Capacity to Succeed in an Outcomes-Based World



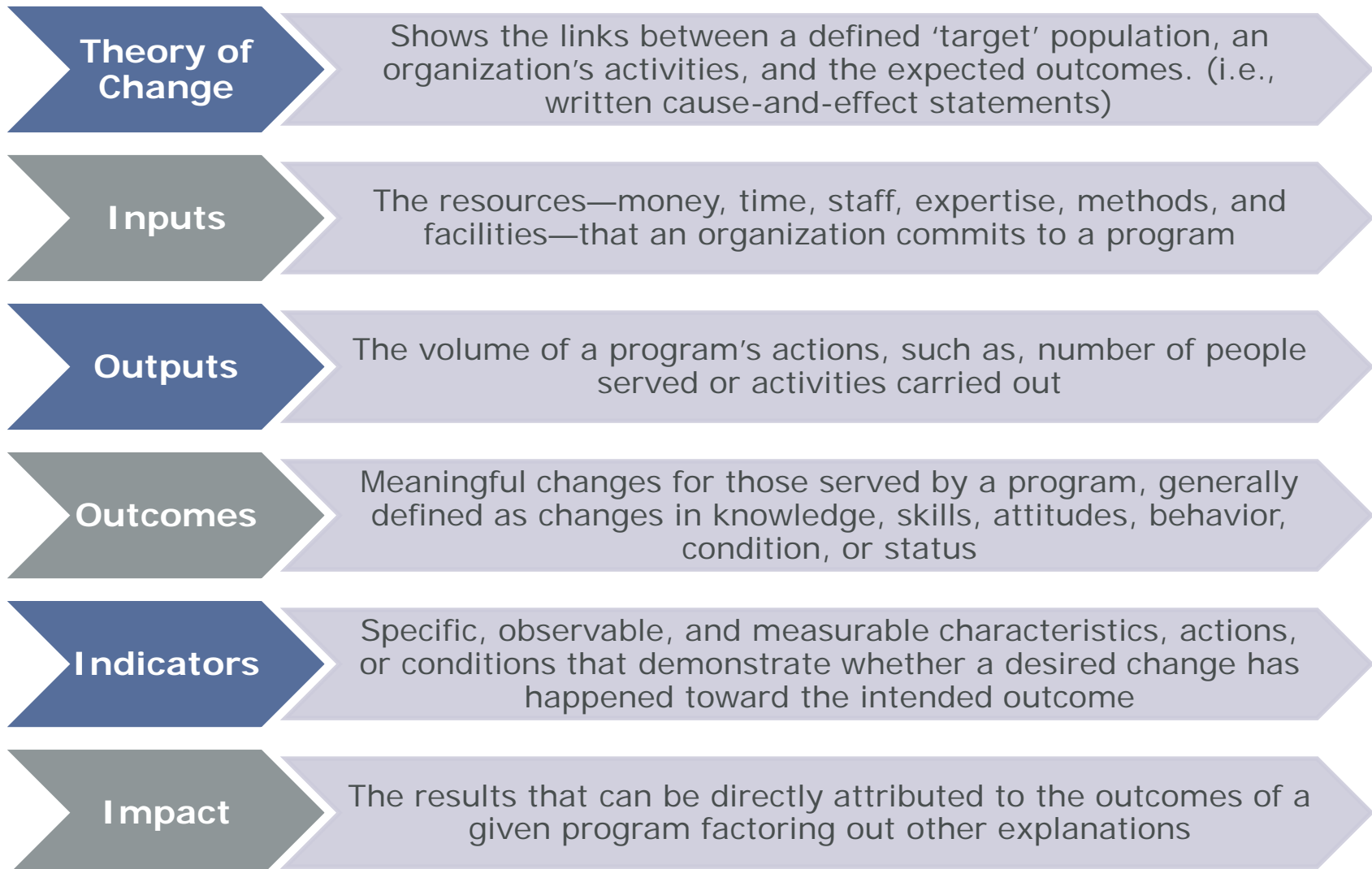
# NPOs and Funders Alike Seek Meaningful Data on What Works

- **35%** (MA=29%) of NFF's 2015 survey respondents reported that **more than half of their funders require certain outcomes** for funding
- **39%** (MA=36%) reported an **increase in the number of funders asking for outcomes to be measured**
- **Only 3%** (MA=1%) reported that funders always cover impact measurement costs; **69%** (MA=77%) said **costs were rarely or never covered**

**"Every ounce of our effort on assessing social outcomes should be with one end in mind: helping nonprofits deliver greater benefits to those they serve."**

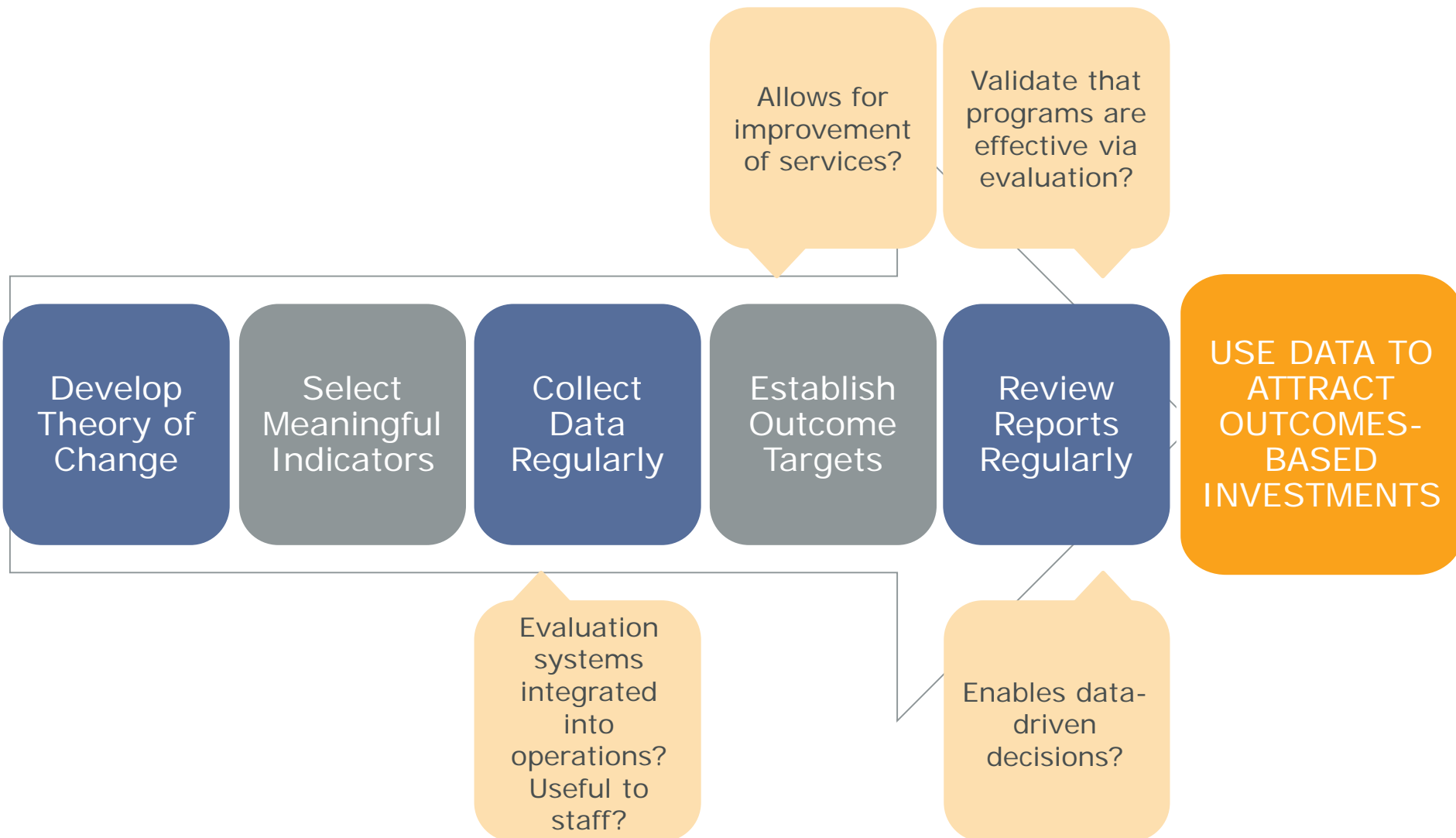
*Source: Leap of Reason, Mario Morino*

# Outcomes Measurement: Basic Definitions



*Adapted From: Leap of Reason, Mario Morino*

# Where is Your Organization on the Outcomes Measurement Continuum?



# Action Steps: Outcomes Measurement

- **Assess** where your organization is on the “Outcomes Measurement Continuum”
- **Define specific benefits and costs** to building outcomes measurement capabilities for your organization
- **Identify steps** to build and improve your measurement systems and enabling **shift in culture**
- **Engage funders** in the process of building an outcomes measurement system, **build in evaluation** as a part of the cost of delivering services

# Exercise: Assessing Your Organization's Strengths and Gaps

<b>Strengths</b>	Example: We have a defined theory of change and have chosen impact indicators
<b>Gaps</b>	Example: Technology gap, weak culture of data driven performance mgmt

# Exercise: Building Your Roadmap Action Items

## INTELLECTUAL CAPITAL –OUTCOMES MEASUREMENT

What are my goals for building capacity in this area?	What concrete actions will I take to build capacity?	Who will be accountable for this in my organization?	What outside resources will I need? What funders can I involve?	What is the timeframe? 3 months, 6 months, one year?



## **What are the benefits?**

- Real-time information to enhance front-line service delivery
- Build a competitive advantage in attracting capital through the ability to quantifiably demonstrate outcomes with funders/investors

## **What are the costs, what will it take?**

- Upfront investment of resources to build or improve systems
- Ongoing investment of resources to manage data collection and reporting
- A cultural shift to using data in feedback loops to inform decision making

# Performance Management: Words of Caution

- **See the forest from the trees**
  - It can be easy to be bogged down in creating the perfect system, but keep in mind the big picture:
    - Not all societal benefit can be measured.
- **Boldly advocate for your methodology**
  - There will always be flaws, government/funders will always require different metrics, but:
    - the best “defense” is a strong, consistent, organizationally-led performance management system.
- **Numbers can lie**
  - Be wary of creating a system that is only about numbers
  - They can be manipulated to get the “right” answer to game the system.
  - Manipulation can take the form of unintentional creaming (only working with clients that will produce the best outcomes) to outright fraud.

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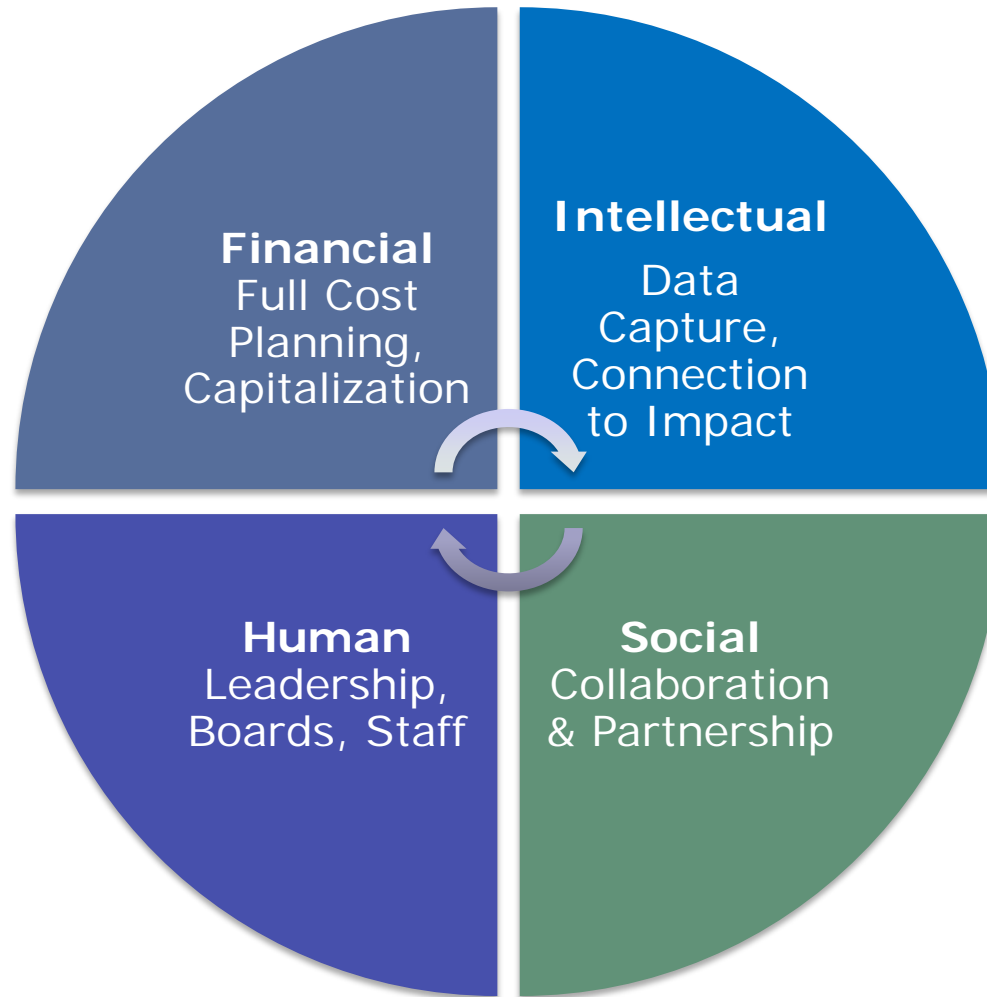
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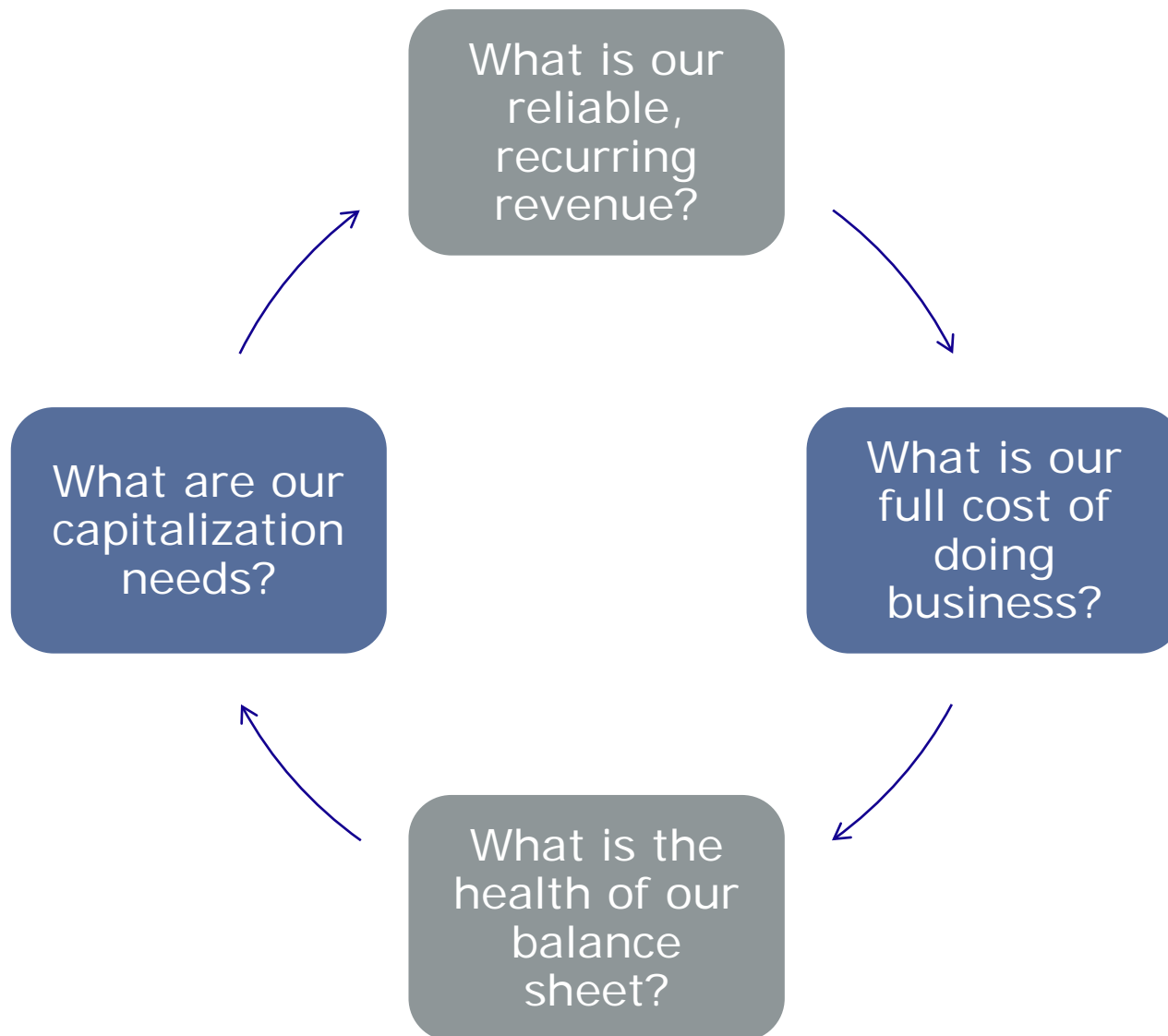
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# Building Organizational Capacity to Succeed in an Outcomes-Based World



# Building the Sustainable Nonprofit Enterprise

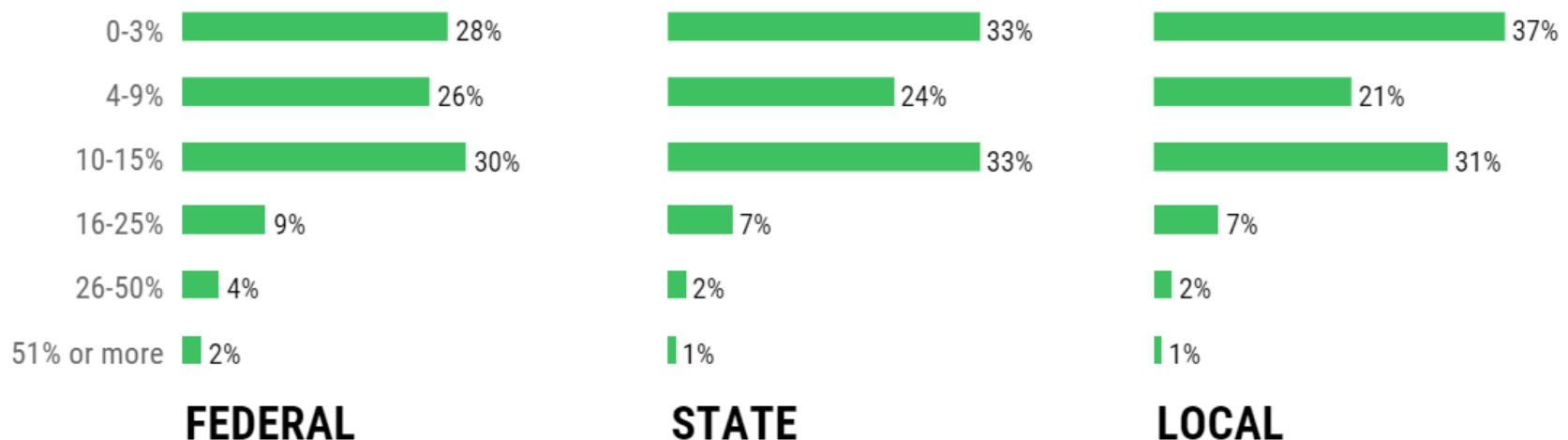


# The Funding Environment is Changing

## ■ The majority of the time, government funders do not cover the full cost of projects they fund:

- 52% said Local governments Never cover full costs
- 50% said State governments Never cover full costs
- 53% said Federal governments Never cover full costs

## ■ Average indirect cost rate paid by government



# Nonprofits Need Profits: Understanding “Full Costs”

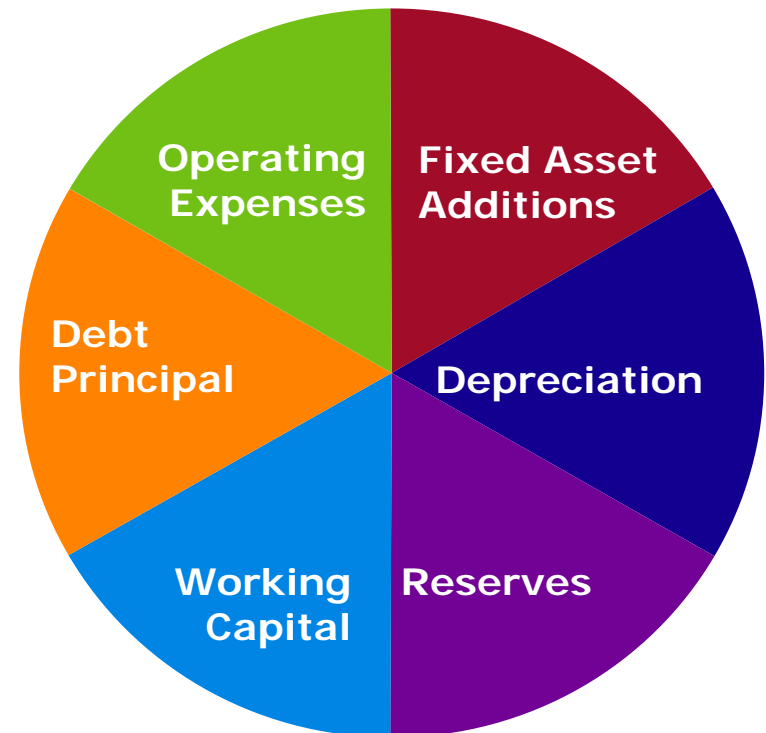
**Like any organization, nonprofits need to cover the full cost of delivering programs**

- Tax Status vs. Business Model
- Full costs > Operating Expenses

## **Full costs include:**

- Total operating expenses
- Depreciation allocation
- New capital investments
- Debt
- Savings for the future

What is our  
full cost of  
doing  
business?



# Considering the Cost of Adaptation to Outcomes Measurement

An organization **changes** when it takes on an outcomes based financing transaction. This impacts expenses in two ways:

## One time, upfront expenses

- Consultants
- Feasibility studies
- Technology investments

## Additional annual expenses

- New staff
- Program supplies
- Evaluation costs
- Higher audit fees

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Resources from outcomes based transactions **may not cover all** upfront expenses and recurring annual expenses in full.



# Determining Financial Resources Needed for Adapting to the New Funding Environment



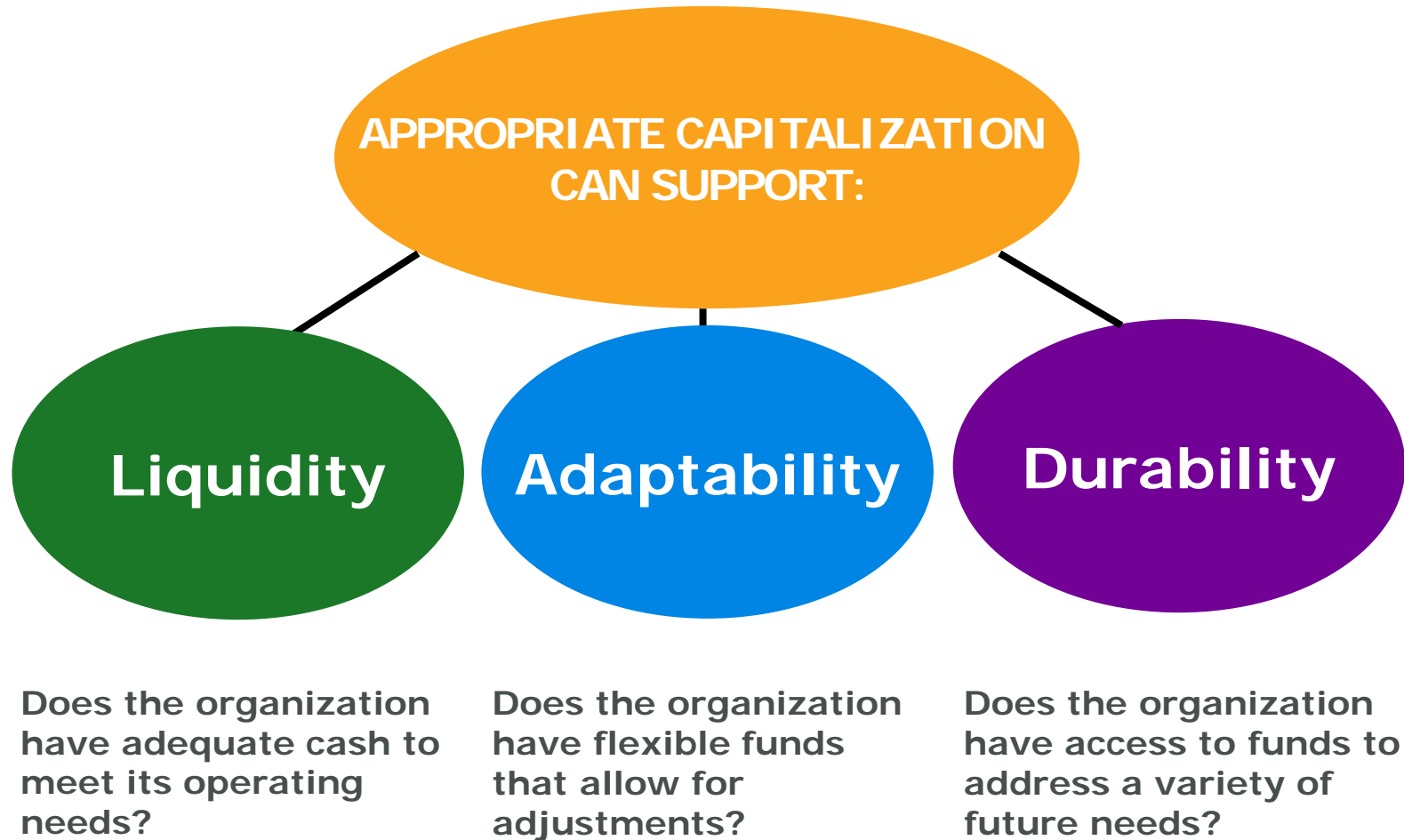
## **Revenue** funds Regular Operations

- Found on the income statement
- Covers cost of regular programs and operations
- *Keeps the lights on!*

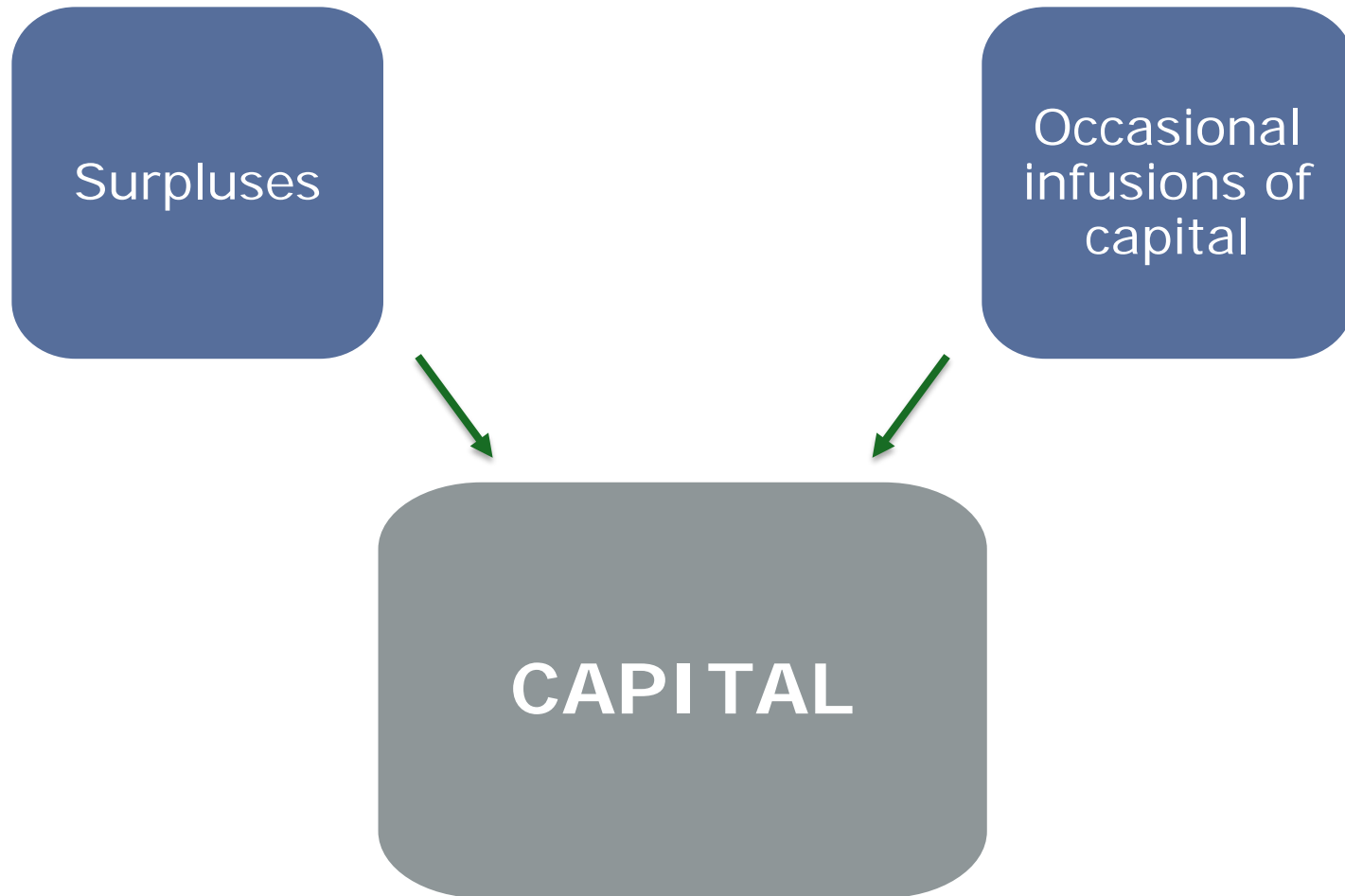
## **Capital** is for Liquidity, Adaptability, Durability

- Found on the balance sheet
- Tends to be episodic in nature
- Can be for initial investment in measurement, recovery, expansion, contraction, quality improvements and more
- Has a long-term view
- *Builds reliability of future revenue*

# Capital Serves Various Purposes



# Capital Comes From Two Primary Sources



# Different Kinds of Capital Address Different Needs

Needed By...		Capital Uses	Function	Addresses:
ALL		<b>Working Capital</b>	Funds to maintain ordinary business operations during cash flow challenges that arise from predictable business cycles	<b>Liquidity</b>
		<b>Operating Reserve</b>	"Rainy day" fund; absorbs unforeseen funding losses or unexpected, extraordinary expenses	<b>Liquidity</b>
MANY, PERIODICALLY		<b>Risk &amp; Opportunity</b>	Supports pursuit of promising new ventures; allows organizations to take advantage of new opportunities	<b>Adaptability</b>
		<b>Recovery</b>	Allows an organization to address a historical mistake or chronically undercapitalized operations	<b>Adaptability</b>
		<b>Change</b>	Funds investments in infrastructure and capacity associated with changes in business model, may cover deficits until programs and operations can support themselves	<b>Adaptability</b>
SOME		<b>Facilities &amp; Equipment</b>	Supports acquisitions or upgrades, or can be used to accumulate reserves to meet future facility and equipment needs	<b>Adaptability, Durability</b>
		<b>Endowment (board designated)</b>	Provides ongoing operating funds through investment income	<b>Durability</b>

# Supporting the Present & Building for the Future: Adaptability to the 'New Normal'

What can we do to both improve the current reality and build toward a better future?

Nonprofits	Funders
<ul style="list-style-type: none"><li>■ Understand the full costs of your services</li><li>■ Describe those costs to funders effectively</li><li>■ Measure outcomes to inform programs</li><li>■ Be proactive in adapting to the changing funding environment</li></ul>	<ul style="list-style-type: none"><li>■ Learn the full cost of services your grantees provide</li><li>■ Commit to funding full costs and long-term sustainability</li><li>■ Help pay for investments in measurement and for results</li></ul>

# Thank You!

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**NFF Pay For Success Learning Hub** - A platform for education, best practices sharing and information dissemination on the potential benefits and challenges of Pay for Success Financing in the United States

[www.payforsuccess.org](http://www.payforsuccess.org)

**2015 State of the Nonprofit Sector Survey Analyzer**

[survey.nonprofitfinancefund.org](http://survey.nonprofitfinancefund.org)

**“Thriving in an Outcomes-Based Market”** - How the *Center for Employment Opportunities* became a data-driven service provider, doubled its reach and participated in the first state-sponsored Social Impact Bond.

[www.aspeninstitute.org/sites/default/files/content/docs/pubs/ThrivingOutcomesBasedMkt.pdf](http://www.aspeninstitute.org/sites/default/files/content/docs/pubs/ThrivingOutcomesBasedMkt.pdf)

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