

## 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

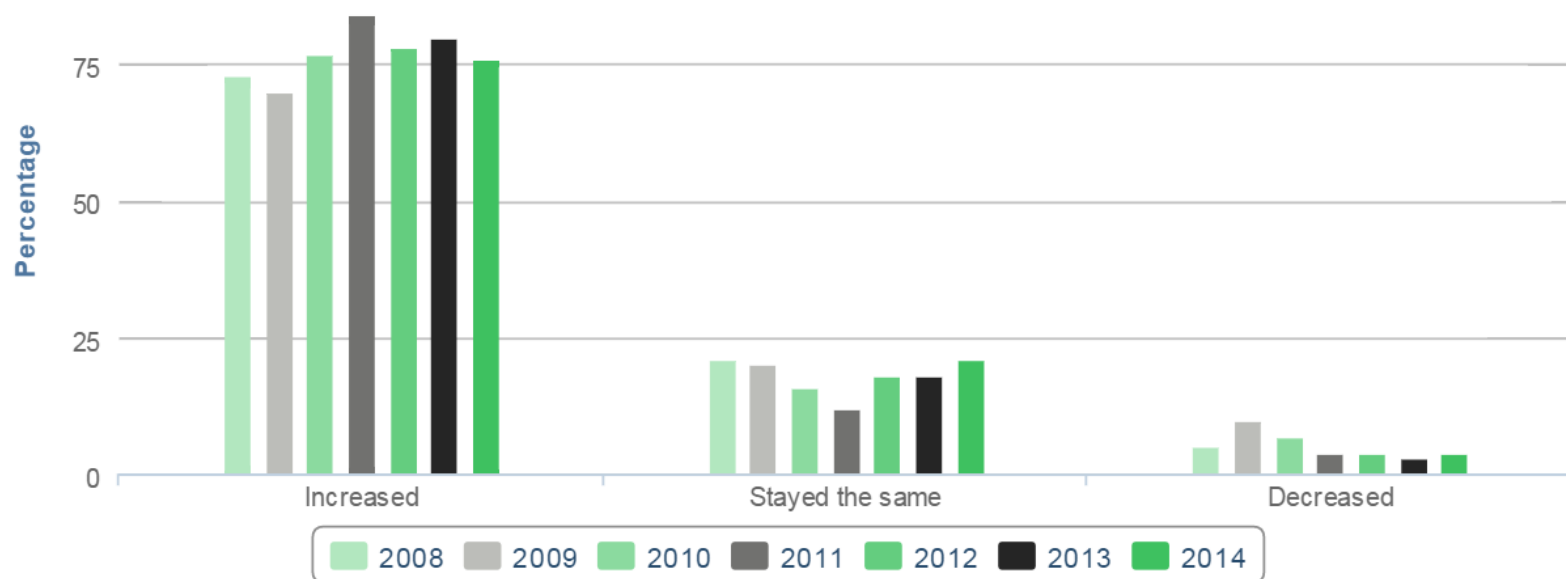
## Financial Capital

- 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

- **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

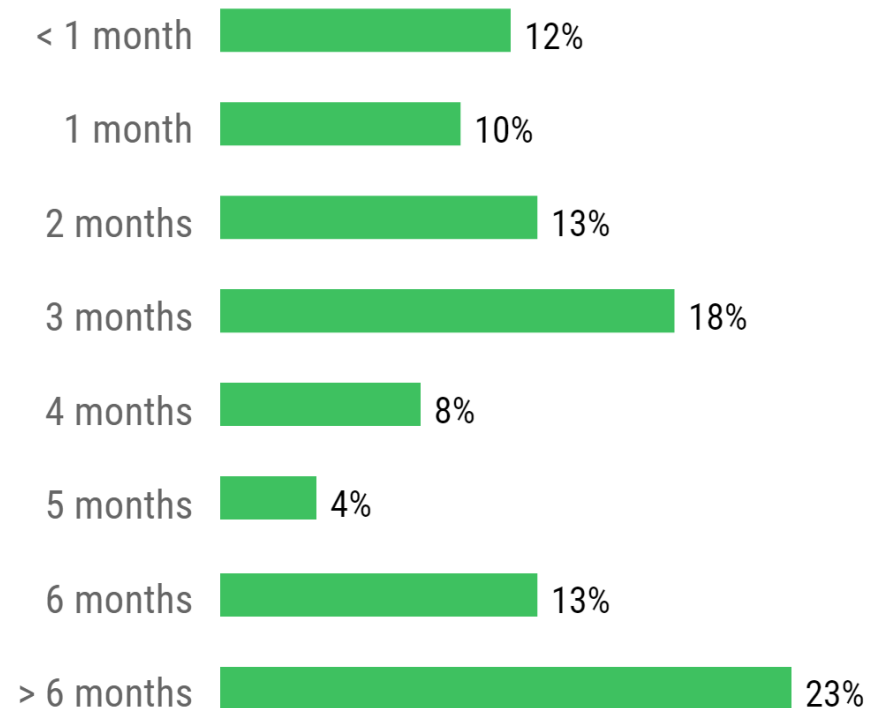
## Financial results in 2014 were similar to past years:

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

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

### Months of Cash Readily Available

Number of respondents: 4439



# 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><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>▪ Investing in “What works”</li><li>▪ More Pay for Performance &amp; increasing Pay for Success efforts</li><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>
Philanthropy		

- **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?

# NPs 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*



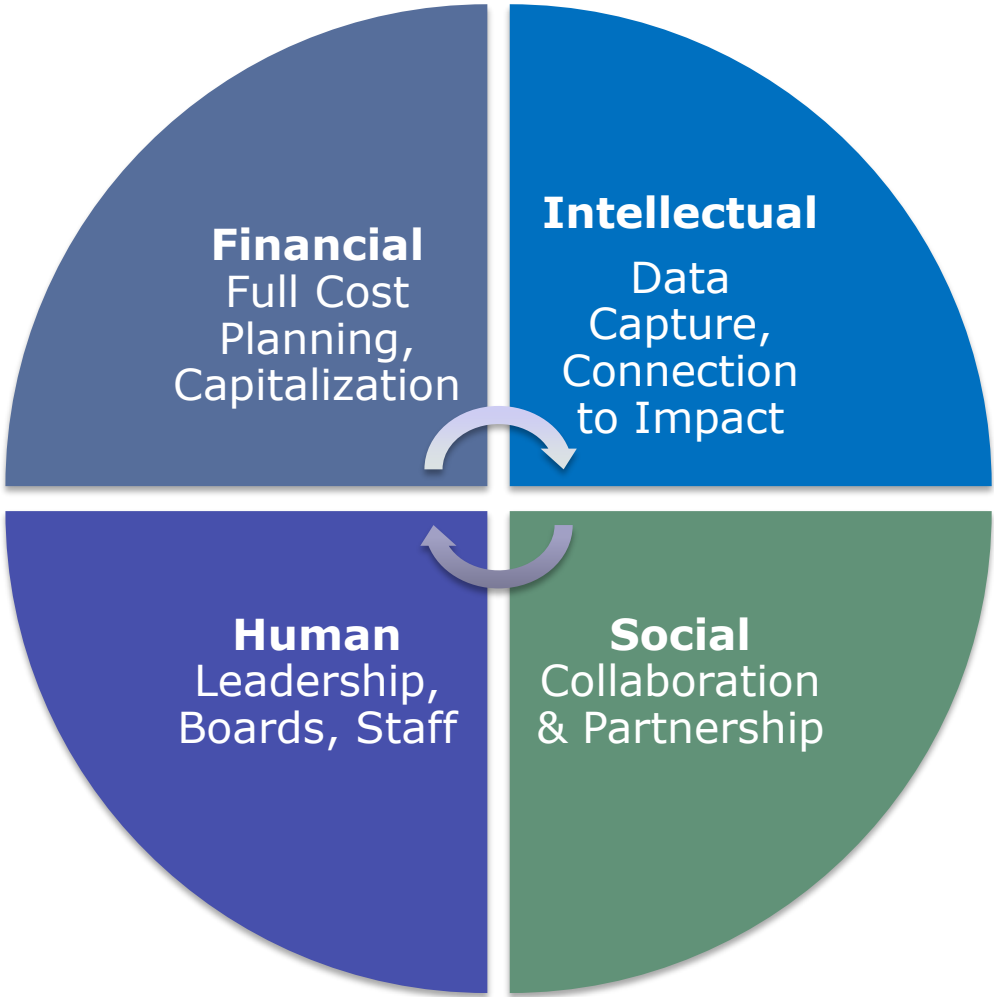
## Challenges

- 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

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



## State of the Sector

- Adapting to the new reality

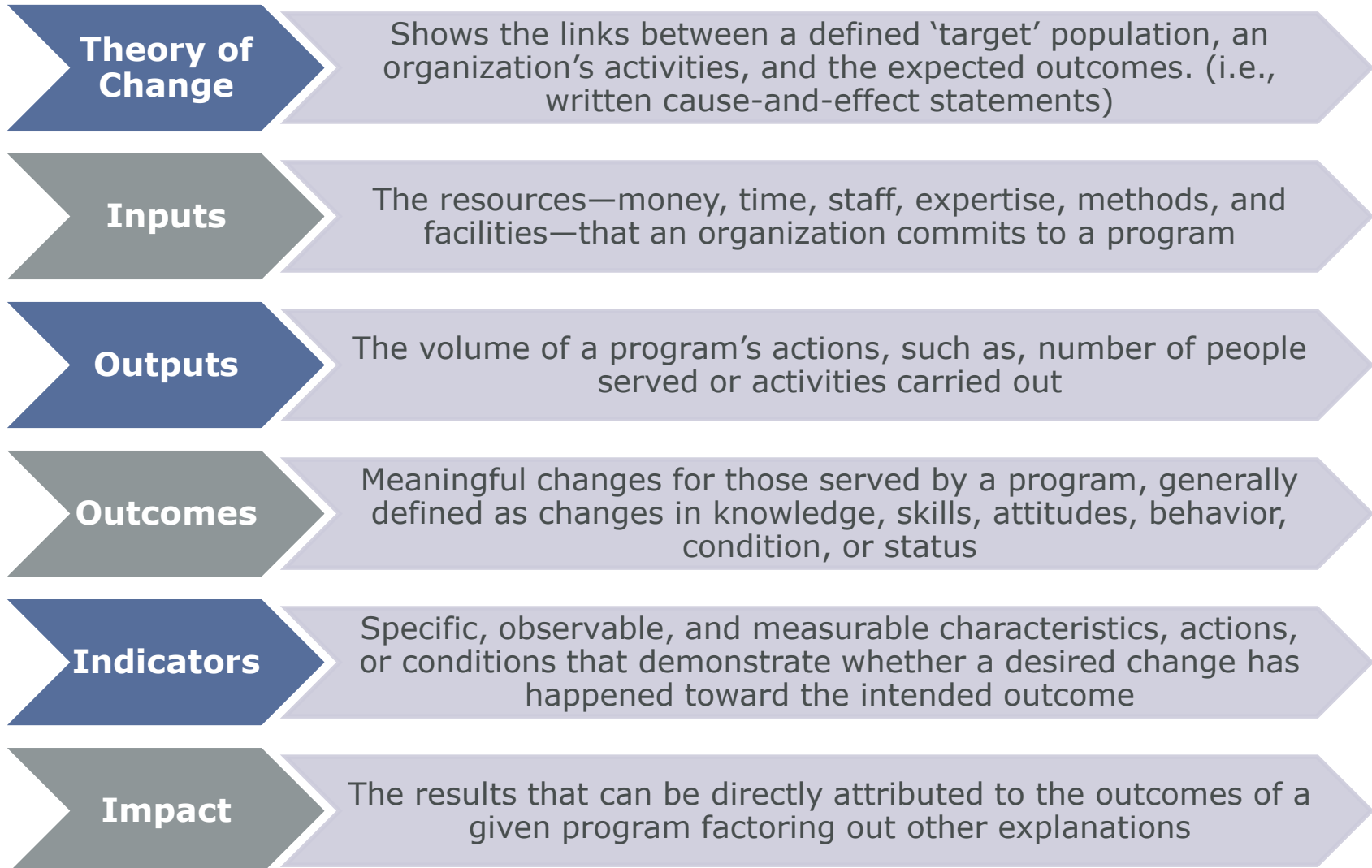
## Intellectual Capital

- Building outcomes measurement

## Financial Capital

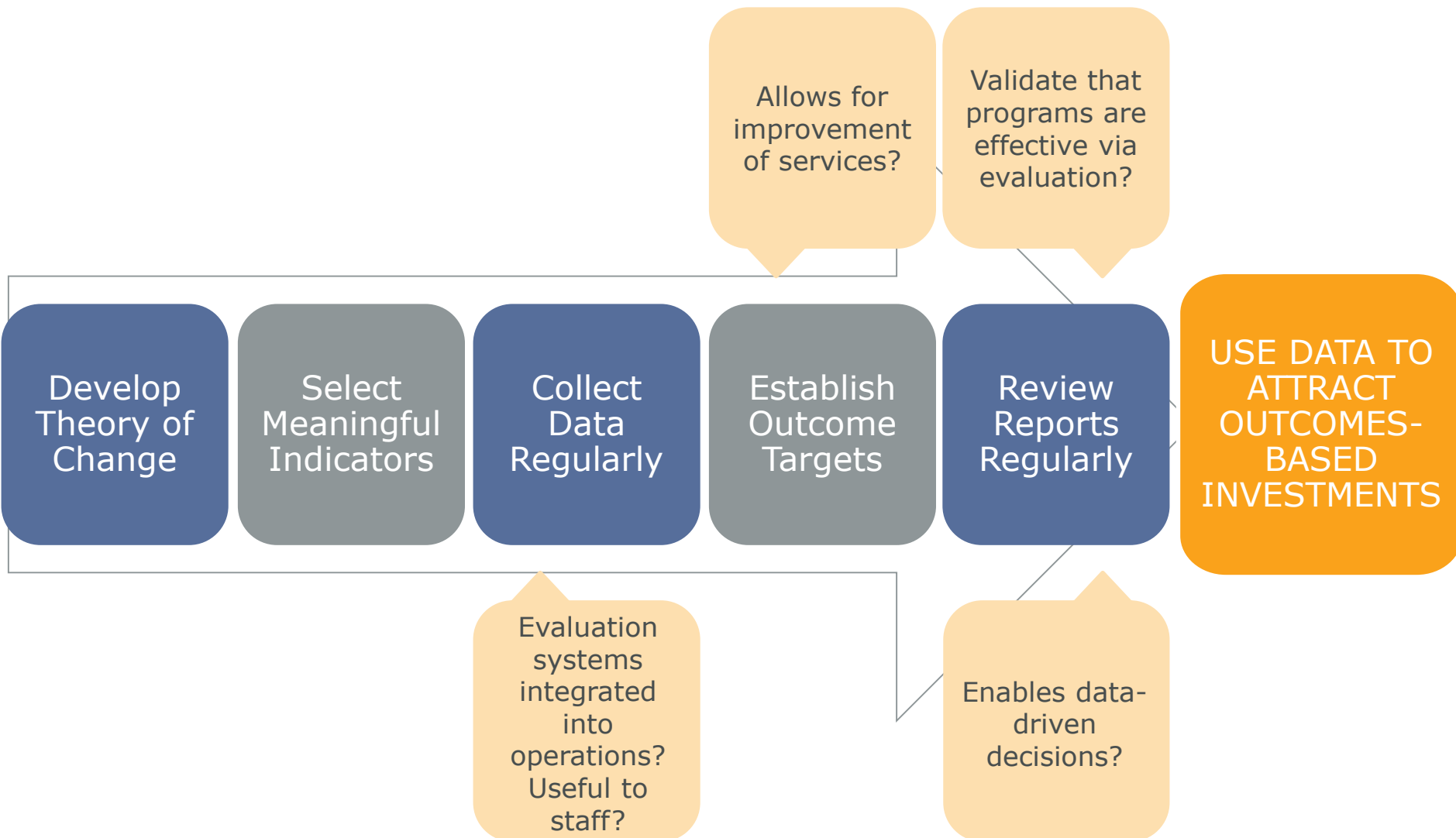
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# Outcomes Measurement: Basic Definitions



*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, lacking culture of data-driven performance management

# 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?**

**Goal #1:**

**Goal #2:**

**Goal #3**



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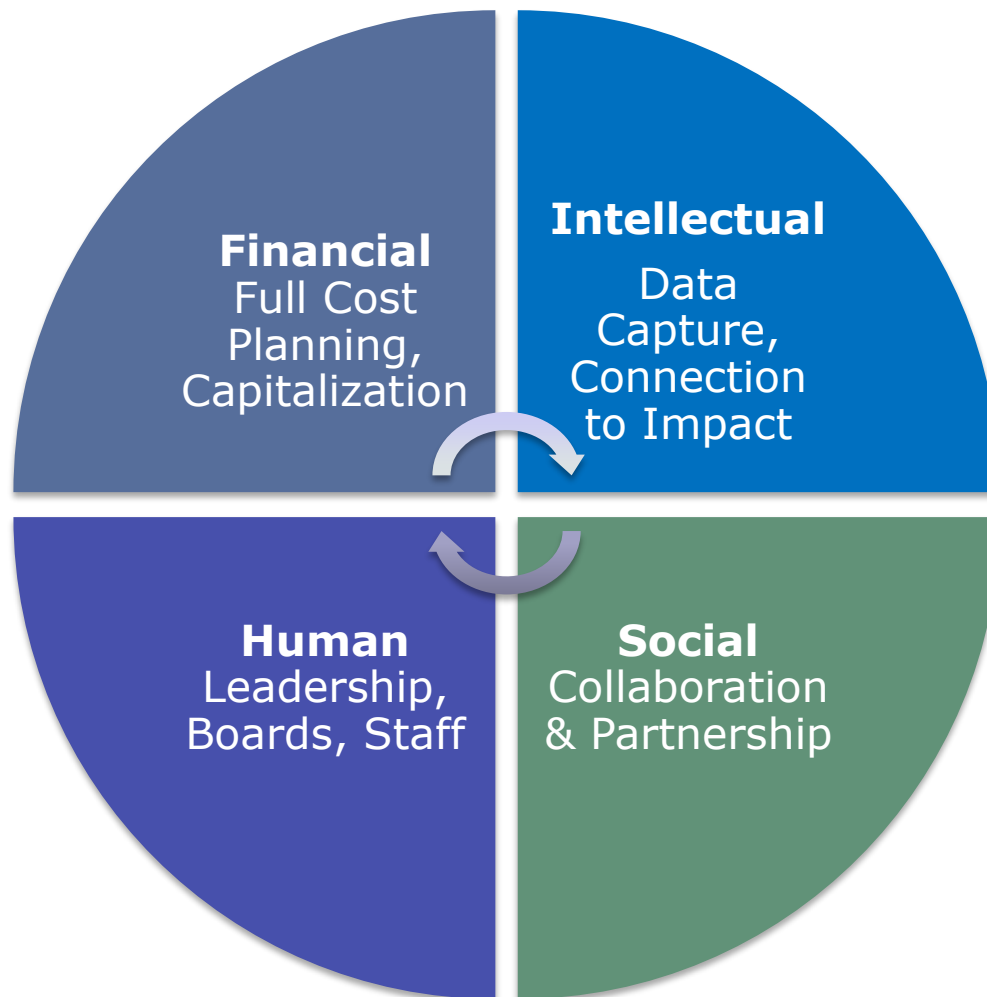
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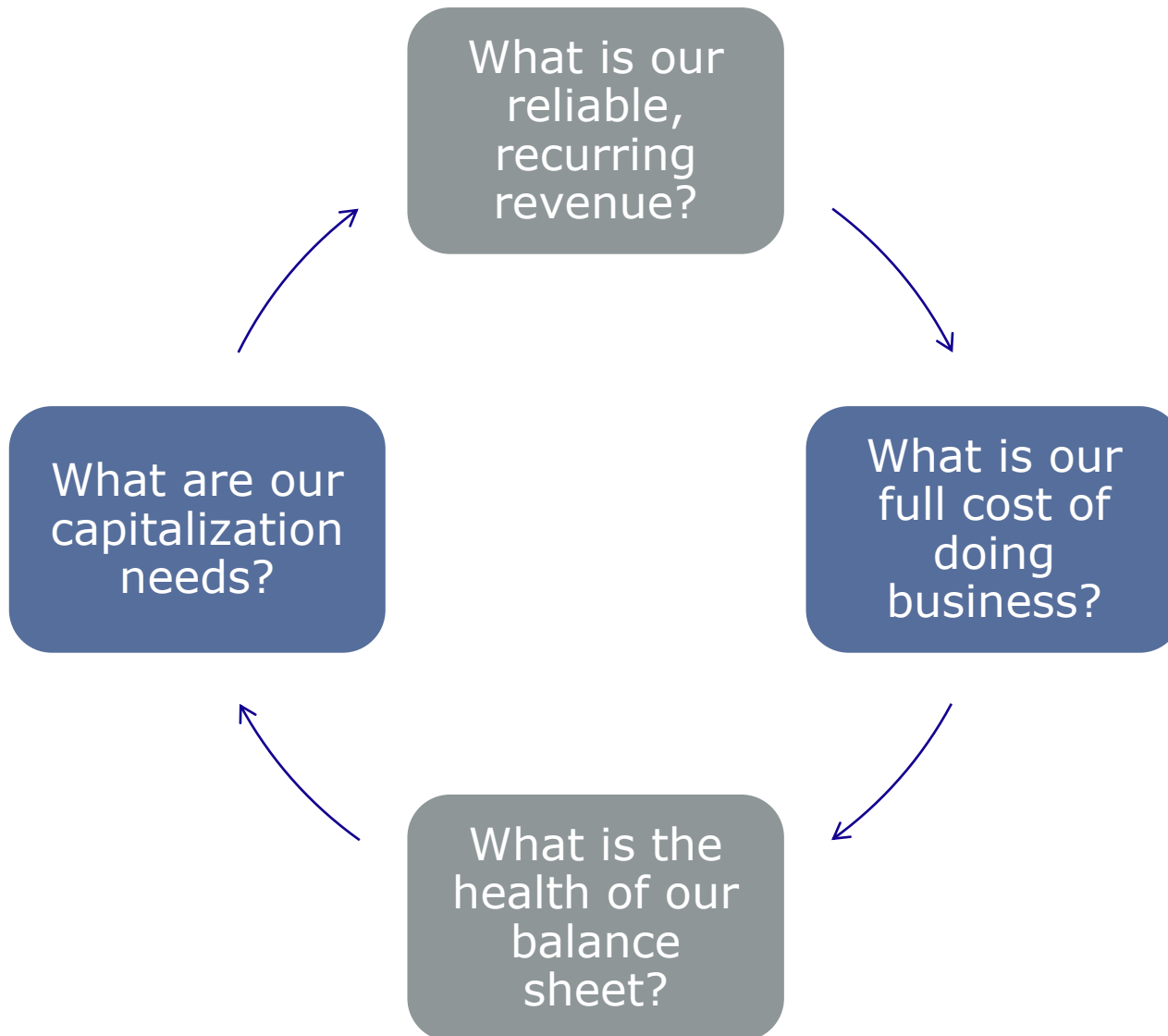
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# Building Organizational Capacity to Succeed in an Outcomes-Based World



# Building the Sustainable Nonprofit Enterprise

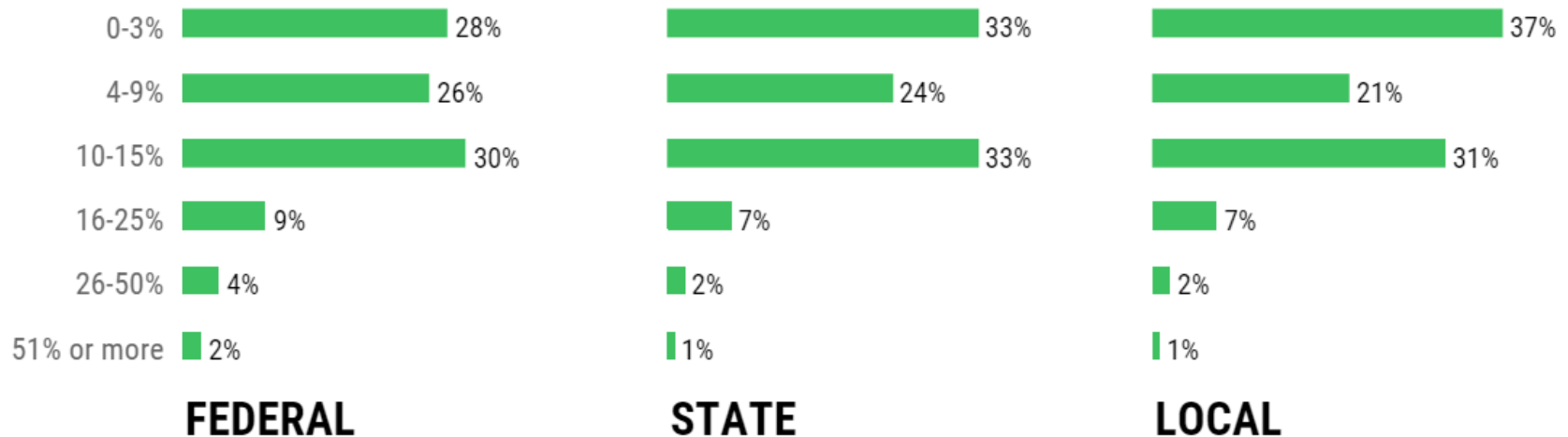


# The Funding Environment is Changing

## ■ 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”

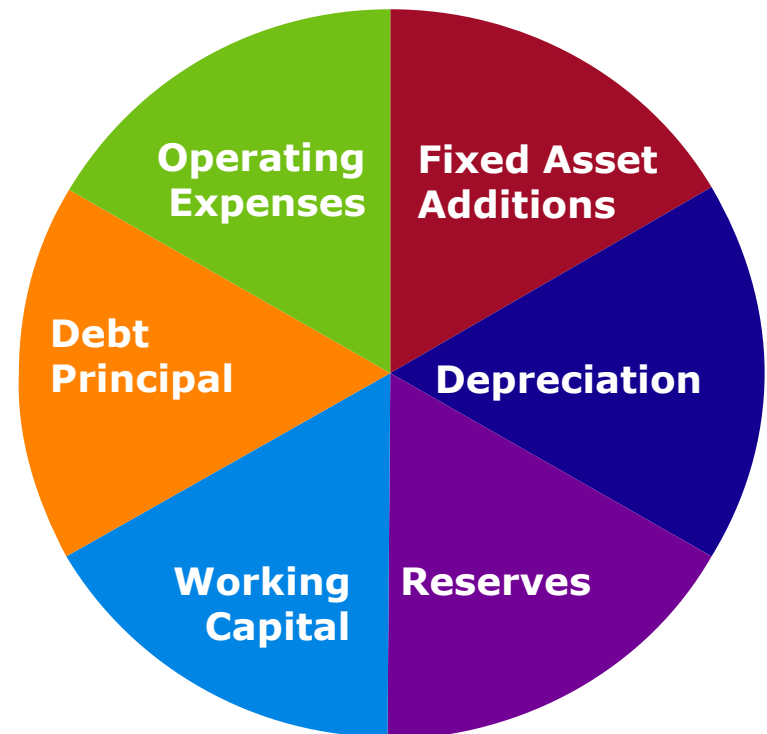
**Like any organization, nonprofits need to cover the full cost of delivering programs**

- 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

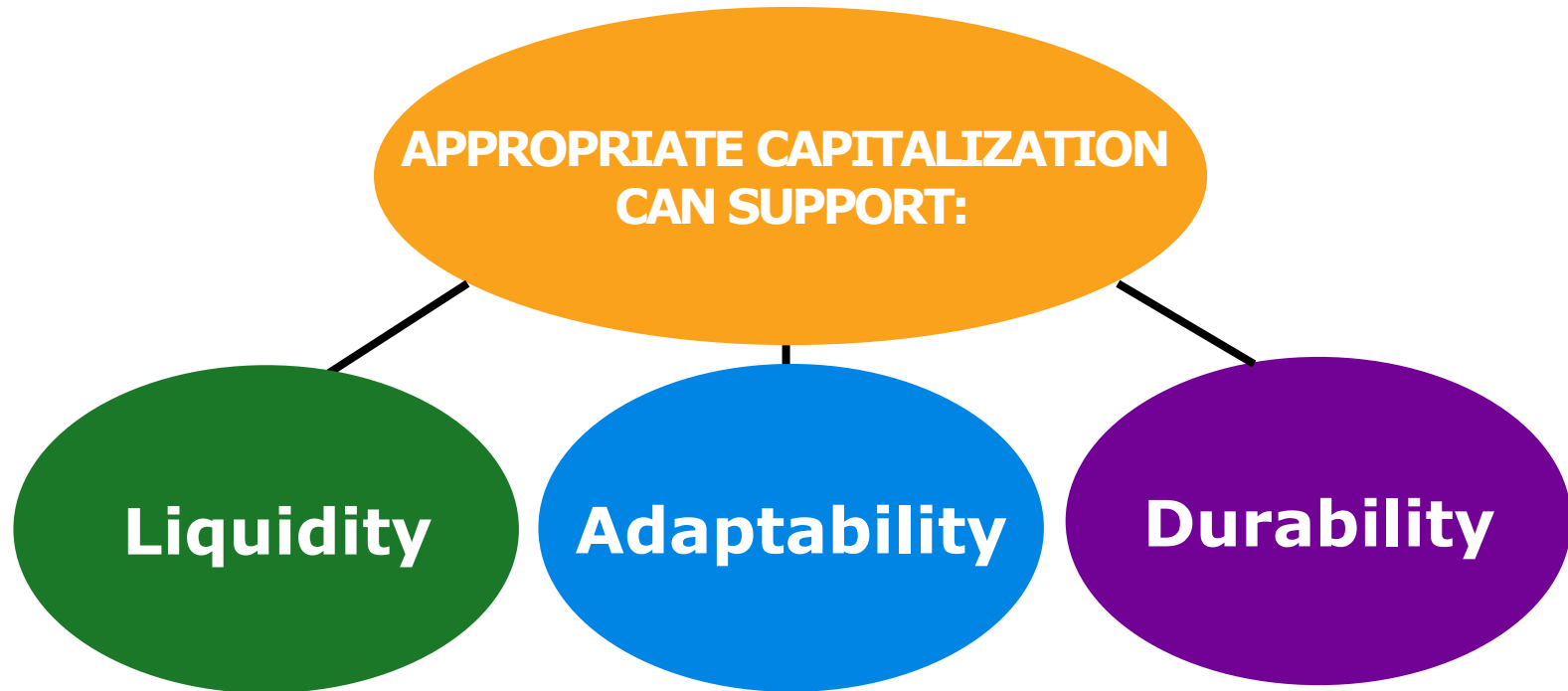


## **Revenue** funds Regular Operations

- Found on the income statement
- Covers cost of regular, ongoing 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*

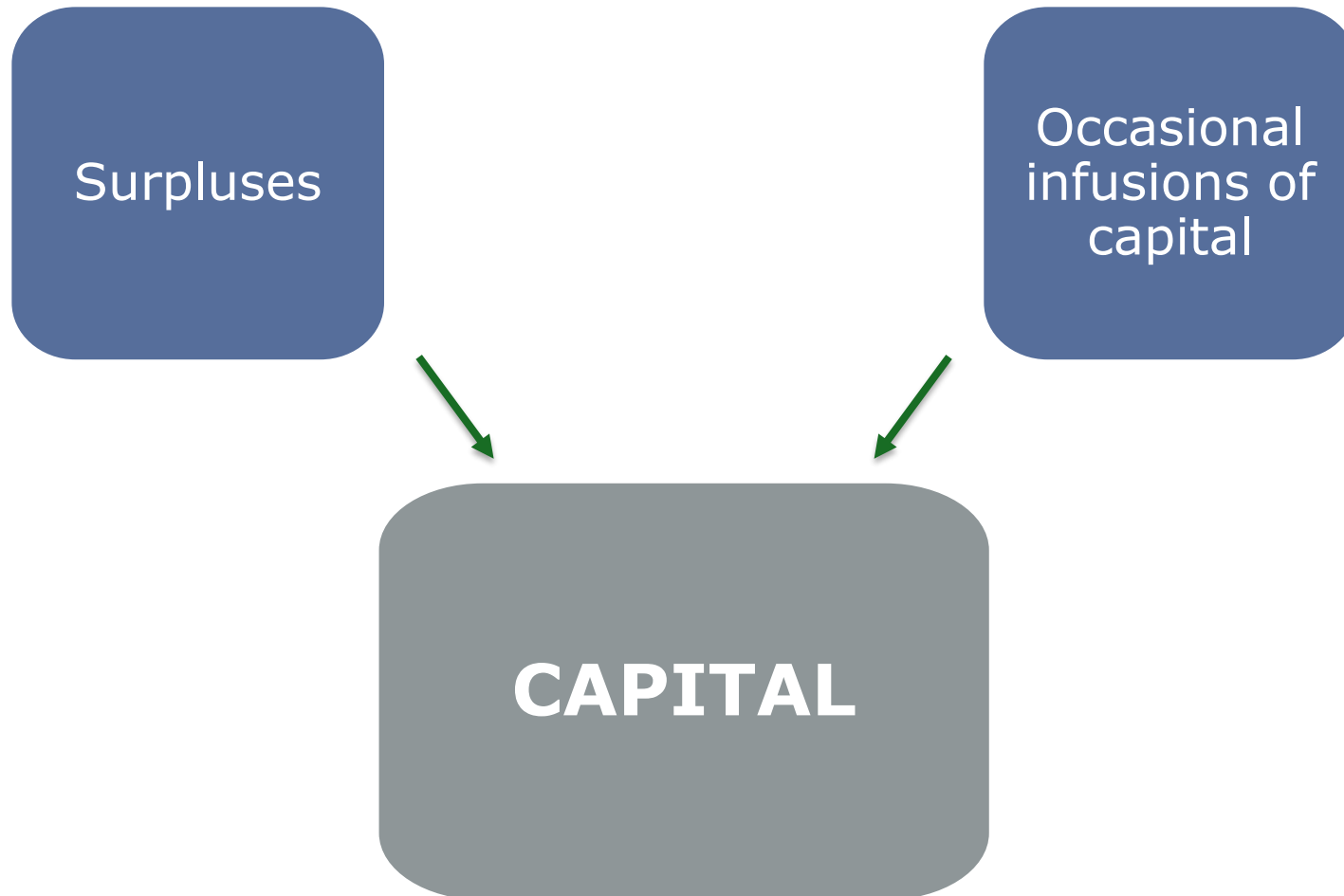


**Does the organization have adequate cash to meet its operating needs?**



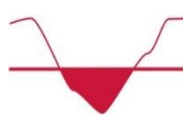


**Does the organization have flexible funds that allow for adjustments?**

**Does the organization have access to funds to address a variety of future needs?**

# Capital Comes From Two Primary Sources



# Different Kinds of Capital Address Different Needs

Needed By...	Capital Uses	Function	Addresses:
ALL	 Working Capital	Funds to maintain ordinary business operations during cash flow challenges that arise from predictable business cycles	<b>Liquidity</b>
	 Operating Reserve	"Rainy day" fund; absorbs unforeseen funding losses or unexpected, extraordinary expenses	<b>Liquidity</b>
MANY, PERIODICALLY	 Risk & Opportunity	Supports pursuit of promising new ventures; allows organizations to take advantage of new opportunities	<b>Adaptability</b>
	 Recovery	Allows an organization to address a historical mistake or chronically undercapitalized operations	<b>Adaptability</b>
	 Change	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	 Facilities & Equipment	Supports acquisitions or upgrades, or can be used to accumulate reserves to meet future facility and equipment needs	<b>Adaptability, Durability</b>
	 Endowment (board designated)	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?

<b>Nonprofits</b>	<b>Funders</b>
<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>

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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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