“We’re in the Money”
New approaches to Nonprofit Income Strategy

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Nonprofit Income Strategy

Main topics:

- Stages in developing an income strategy
- Characteristics of sources of support
- Investment cases for income sources
- Identifying the most likely forms of support
- Screening likely forms of support

- A case study
- Half-day counterpart of full day workshop
- Credits: Gronbjerg, Pratt, Young

Nonprofit Income Strategy

Key Concepts:

- Real Value of a source of support
- Real Costs
- Real Investment case

  (Real vs Financial only)
- Programs → benefits → support

Nonprofit Income Strategy

Stages in developing an Income Strategy

- Define programs and their operating costs
- ***Identify most likely forms of support***
- ***Screen these forms of support: prevalence and nonprofit's values***
- Do market research: $ value and direct and start-up costs
- ***Develop investment cases: "real" value and costs***
  : $ value and costs
- Test support
- Make decision: Invest….or quit.

Nonprofit Income Strategy

Context:

- Overall strategic review or planning exercise
- New income opportunity
- Purposes:
  - Add a new source
  - Invest more in a current source
  - Divest the nonprofit of a current source
  - Start-up

Nonprofit Income Strategy

Stages in developing an Income Strategy

- Define programs and their operating costs
- ***Identify most likely forms of support***
- ***Screen these forms of support: prevalence and nonprofit's values***
- Do market research: $ value and direct costs
- ***Develop investment cases: "real" value and costs***
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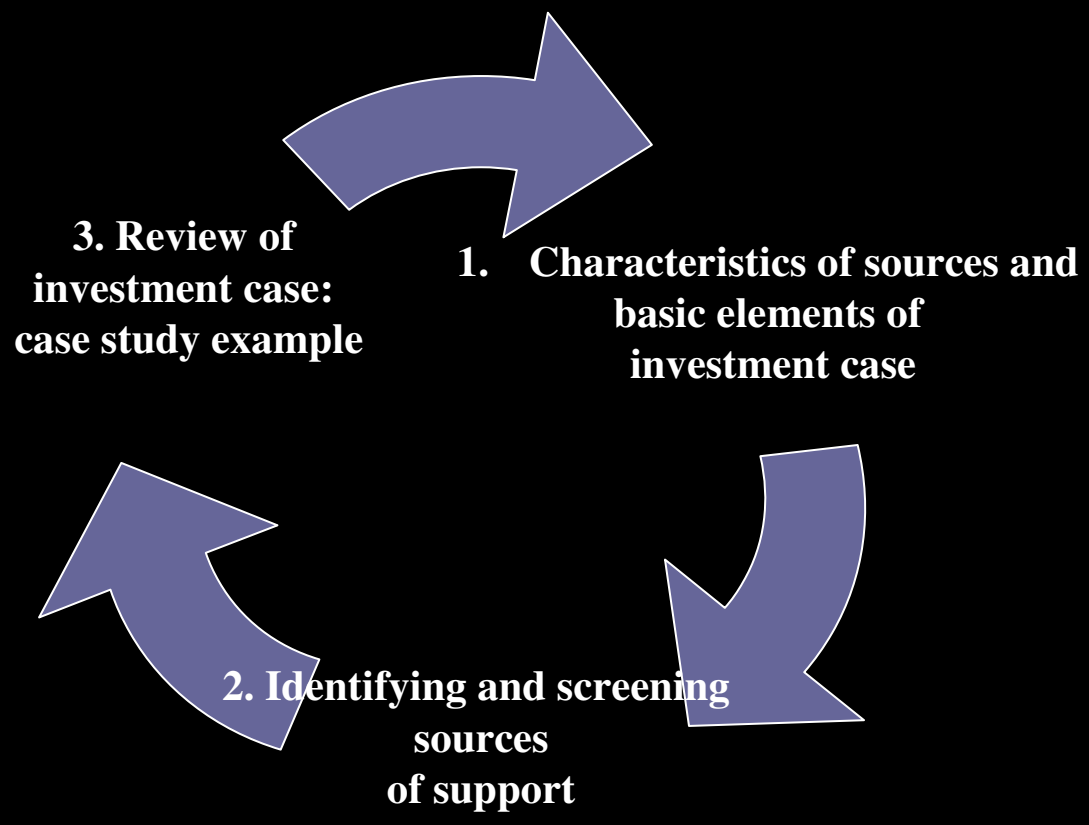
Nonprofit Income Strategy



Nonprofit Income: Forms of Support

Contributions	Government Funds	Earned (Fee) Income	In-Kind Support	Investment Income
Individual giving; some memberships	Grants	Fees for service, some memberships	Volunteer & pro bono work	Returns on endowment
Bequests	Contracts	Sales/ commercial venture income	Gifts of real estate	Interest on operating funds
Corporate and Foundation grants	Reimbursements	Royalties and license fees	Art and other collections	Program-related investments
Special events	Credits & vouchers	Rental income	Partnerships with others	

Dimensions of Sources of Support: **Value**

- Potential gross $ value: amount of activity that source "buys" = $ amount or $ value of gift-in-kind, adjusted by…..
- Value attracted ('crowded-in') e.g. work of art
- ….and value displaced ('crowded-out') e.g. govt. funding vs. donations
- Additional direct mission impact e.g. client buy-in

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Dimensions of Sources of Support: **Costs**

- Direct costs
- Start-up costs
- Hidden transaction costs:
  - Attracting and managing *relationships*
  - Managing *independence and external control*
  - Managing *reliability*
  - Managing *extra resources*

Dimensions of Sources of Support: <u>Costs</u>

Costs:

- Direct operating expenses
  - People
  - Materials
  - Services
- Start-up capital and working capital:
  - New people, facilities, equipment
  - New skill sets
  - New systems and processes

Dimensions of Sources of Support: <u>Costs</u>

Hidden Transaction Costs:

- Attracting and Managing relationships with, source(s) of support
  - Payers and potential payers
  - Messages aimed at payers
  - Internal mechanics and behavior

- Managing independence and external control
  - Strategic alignment
  - Balance of restricted with unrestricted
  - Negotiation of specifications
  - Reconciling external requirements with nonprofit's values

Dimensions of Sources of Support: Costs

Hidden Transaction Costs:

- Managing Reliability:
  - Planning inflows and outflows and mix of sources
  - Building a reserve
- Managing the extra resources:
  - Extra reporting relationship
  - Controlling fixed costs

Dimensions of source of support: small individual donations (mailing program)

Value:

- Low value per donor, but accumulating…
- Crowd-in/crowd-out depends on other sources
- No accompanying mission value

Costs:

- Operating costs 10 to 30 % of money raised
- Start-up costs can be high: people and systems and securing first donors

Dimensions of source of support: small individual donations (mailing program)

- Hidden transaction costs:
  - Managing relationships depends on cause and nonprofit's culture: can be issues around images and messages used. Time taken up can be low or high.
  - External control costs low – no or few restrictions
  - Managing reliability low – repeat donations
  - Managing extra resources can be high – large-scale mailing is substantial operation

Dimensions of source of support: government contracts

Value:

- Potentially very high value
- Crowd-in/crowd-out depends on other sources, but often crowds out
- Accompanying mission value possible: policy influence

Costs:

- Direct operating costs relatively low
- $ start-up costs can be very low, though if nonprofit new to govt. funding, new systems may be required

Dimensions of source of support: government contracts

- Hidden transaction costs:
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Assessing dimensions of sources of support

'Non-dollar' values will vary by nonprofit:

- Field of operation – nature of funders
- Attractiveness of cause
- Current income profile
- Organizational capacity

Assessing dimensions of sources of support

Worksheet One: Rating non-dollar value and costs

Please:

- Read Mental Health Recovery (MHR) case study
- Rate at least two of the listed types of support
- Share results and your reasoning with others in group
- Be prepared to share your results and reasoning with the wider group

Nonprofit Income Strategy

Stages in developing an Income Strategy

- Define programs and their operating costs
- ***Identify most likely forms of support***
- ***Screen these forms of support: prevalence and nonprofit's values***
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Identifying most promising forms of support

1. Describe portfolio of programs/activities that address mission
2. *Assess the kinds of benefits generated by each program*
3. *Identify potential sources of support, based on types of benefit*
4. *Adjust this potential portfolio by assessing for prevalence and "fit"*
   - *Customary forms of support in field*
   - *Values of nonprofit*

Nonprofit Income: Forms of Support

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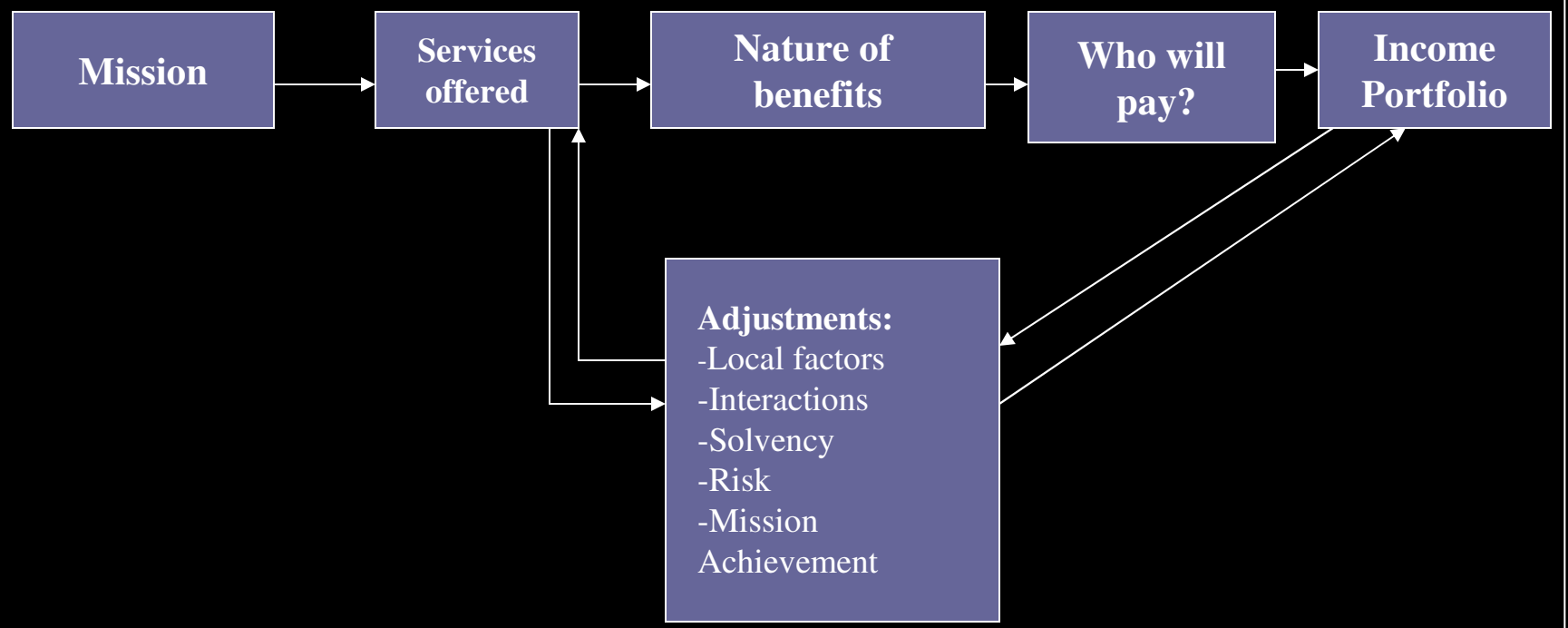
Aggregate Income Sources by Sub sector, 2000 (Nonprofit Sector Research Handbook, 2006)

	Fees	Gifts	Gov't Grants	Investment Income
Health	85%	4%	3%	3%
Human Services	49%	19%	23%	3%
Education	47%	17%	10%	6%
Arts	29%	41%	10%	6%
Religion	27%	57%	3%	4%
Environment	22%	51%	10%	5%
Public Benefit	21%	42%	16%	7%
International	9%	68%	17%	2%

Origins of a nonprofit's support



Identifying most promising forms of support: Sources of Income and the Nature of Benefits

- **Private benefits**
- **Group benefits**
- **Public benefits**
- **Trade or exchange benefits**

- **Accrue to service consumers willing and able to pay *fees***
- **Accrue to specific constituencies associated with causes that donors wish to support *with gifts and grants***
- **Accrue to the general public, supportable by *public financing***
- **Accrue to organizational partners in a *quid pro quo* relationship**

Sources of Income and the Nature of Benefits: Private benefits

- Nonprofit service or activity generates direct benefit to individual
- Individual can be excluded from service
- Examples:
  - Health care
  - Counseling
  - Theater performance
- Type of payment: fee in direct exchange for service

Sources of Income and the Nature of Benefits: Public benefits

- Nonprofit activity or service generates benefit that, once produced, everyone gets.
  - Clean air
  - National Defense
- Nonprofit activity produces benefits that have political support and mandate:
  - Workforce Development
  - Support for veterans
- Types of payment:
  - Federal/State/Local grants and contracts
  - Vouchers
  - Medicaid and Medicare

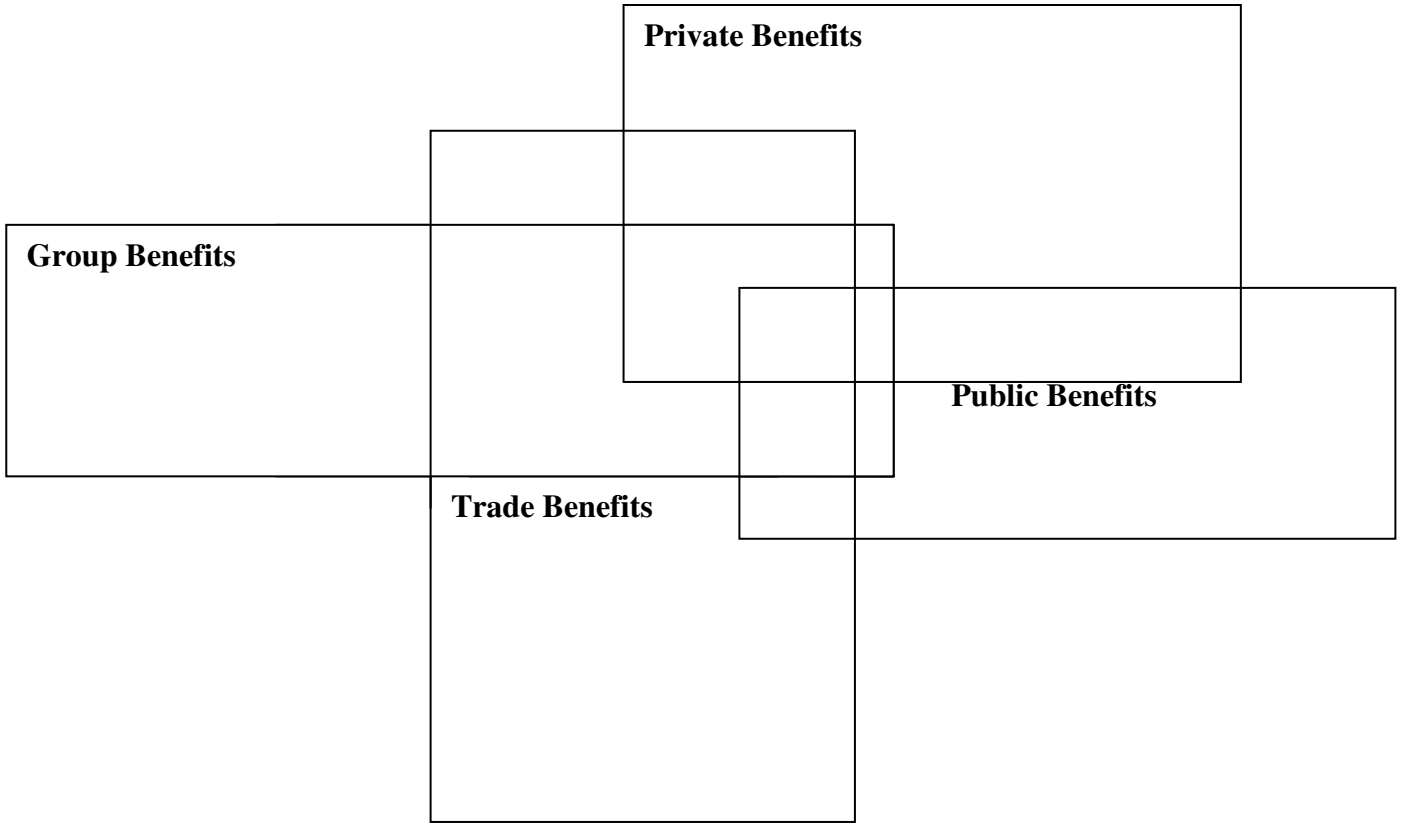
Sources of Income and the Nature of Benefits: Group Benefits

- Number of people or a community benefit, and difficult to exclude, but.. benefits not sufficiently widespread or popular to attract public funds
- Examples:
  - Research into rare medical condition
  - Support for victims of disasters
  - Avant-garde theater
- Who pays?: people with affinity or interest, or brief/policy to support a given area.
- Types of payment:
  - Donation
  - Bequest
  - Grant

Sources of Income and the Nature of Benefits: Trade benefits

- Activity generates economic or social benefit for third party (other organization or individual not in receipt of service)
- Examples:
  - Traders who retain customers because of nonprofit transport scheme for seniors
  - Advocacy coalition: exchange of one nonprofit's resources for another's staff
  - Corporations that buy nonprofit's reputation to increase their own sales
- Types of payment:
  - Membership/affiliation
  - Barter
  - Sponsorship

Benefit Combinations and Income Portfolios



Identifying most promising forms of support: nonprofit services and benefit and income combinations

Income combo	Example	Why?
Fees only	Gift shop	Consumer benefit only
Gifts only	Rare disease research	Benefits those afflicted or at risk
Gov't only	Offender rehab services	Increases public safety
Fees & gifts	Performing arts	Private benefits to attendees; collective benefits to art lovers
Fees & gov't	Pre-school care	Private consumer and general public benefits
Gov't & gifts	Monitoring environmental quality	Benefits to outdoor enthusiasts and general public
Fees, gifts & gov't	University education	Private student, collective alumni, and general public benefits

Identifying most promising forms of support

Case Study Worksheet Two

Please:

- Review MHR case study
- As a group, complete the worksheet. Be as specific as you can
- Be prepared to report your group's finding's back to other session participants

Identifying most promising forms of support

Significant potential sources: screen against:

- Customary forms of support in field
  - Reduces costs of securing and maintaining relationship
  - Issue of competition
- Values of nonprofit
  - Acceptability to key constituents

⇓

Most promising sources for new investment

Identifying most promising forms of support

MHR Significant potential sources:

- Fees – self-pay and insurance
- Individual Donations
- Contracts with rehabilitation services in other jurisdictions
- Partnerships with other nonprofits

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Framework for Decision-Making

For each Source, or expansion in income generation from a source:

- Value (direct $ value, ‘crowd-in’ value, added mission value, minus ‘crowd-out’)

versus

- Direct operating expenses, start-up capital and working capital and hidden transaction costs.

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Nonprofit Finance: Decision-making and diversifying income streams

- Protection against risk
  - Loss of program?
  - Loss of nonprofit?
- Myths
  - Need to diversify across sectors
  - Always improves bottom line
- Critical factors
  - Payers who are independent of (not positively related to) each other
  - Unrestricted income
  - Overall risk strategy
- Most favorable benefit/cost analysis: largest number of independent payers vs. lowest extra investment

Alliance for Nonprofit Management

"We're in the money:" new approaches to nonprofit income strategy

Case Study: **Mental Health Recovery (MHR)**

Mission

MHR was started in the late 1960s out of a church basement by someone who believed passionately that people with mental illness are not permanently sick and can be fully contributing members of society. After two or three years funded by private donations, the organization's supporters managed to write in to some state legislation a mandate to provide recovery-based services. County funding for the bulk of its activities followed soon after.

MHR's Mission is to support people in Fractious County and surrounding areas who have mental illness because of substance abuse, to recover fully and to live independently; and to help create an environment in which people recovering from mental illness are fully accepted by the local community.

Programs

MHR runs programs in Day Care, Community Outreach and Employment and undertakes some lobbying and advocacy on behalf of people with mental illness.

- **Day Care**. Service users attend one of three centers strategically located across the county for between two and five days a week. They can make their own way to the centers, but most are collected by MHR staff in small buses. Two of the centers are housed in properties owned by commercial real estate companies, the third by a millionaire businesswoman who dabbles in real estate. While attending the service, members receive personal care and support with medication; life-skills training; computer skills training; and art therapy. They also participate in a range of therapeutic group discussions. All members have a personal recovery plan.
- **Community Outreach.** Qualified MHR staff visit people with mental illness in their own homes. They provide personal care, support with medication, 1:1 counseling on handling daily life, social skills coaching, help with claiming benefits, and work with each individual on setting personal goals.
- **Employment.** MHR runs teams of employment specialists. These specialists work with individuals to prepare them for work, providing advice on anything from self-presentation and timeliness to interviewing skills; they advise potential employers on how to employ someone with a mental illness, in terms of the accommodations and management style required; and they act as job brokers, matching job-ready individuals with mental illness together with specific opportunities in the workplace.
- **Lobbying and advocacy.** MHR undertakes some advocacy work: at the county level in order to make sure its voice is heard in any discussions about service quality required in county contracts, and, of course, to protect its income streams; and at the state level in order to influence legislation about mental illness.

Although there is nothing in their mission statement to this effect, until now MHR have met the needs of those who do not have the means to pay for assistance.

There are some other nonprofits in the area that address related challenges. One of them offers support to people with addictions; there are three homelessness agencies; and two nonprofits provide people with mental illness with residential services.

Funding

MHR has a $6.1 million annual budget and its funds come primarily from a large contract with Fractious County, two employment contracts with Rehabilitation departments (DRS) in two other jurisdictions, and from a popular golf tournament organized by its Board fundraising committee.

	$million
County contract:	
Day Service	3.2
Community Outreach	1.3
Total	**4.5**
DRS contracts:	**1.3**
Net proceeds of golf tournament	**0.3**
TOTAL	**6.1**

Review

Fractious County depends on property taxes for 60% of its budget. As these decline in the current property market, they have frozen human service contract levels. News is now filtering through that some services, like those to people with developmental disabilities, can expect cuts of 10 to 15% in contract payments for the year July 2009 to June 2010. The board and senior management at MHR are now worried enough to begin a review of the nonprofit's income portfolio.

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Funding Source Investment Case ***Assessing the benefits and costs of sources of support.***

Value/Cost	Source One	Source Two	Source Three	Source Four
Potential Gross $ Value				
Adjustments: ▪ **"crowd-in"** ▪ **"crowd-out"** ▪ **direct mission impact**				
Adjusted Gross Value				
Direct Costs of generating funds				
Predicted Net $ Value				
Start-up and new working capital needed				

Hidden Transaction costs:
 	
• **Attracting and managing new relationship**
 	
• **Managing independence/control:**
  ▪ **External**
  ▪ **Internal**
 	
• **Managing Reliability**
  ▪ **Planning**
  ▪ **Building Reserve**
 	
• **Managing the extra resources**				

OVERALL RATING OF VALUE OF SOURCE TO NONPROFIT				

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Case Study: **Mental Health Recovery (MHR)**

Worksheet One: Rating non-dollar value and costs

Current Funding

MHR has a $6.1 million annual budget and its funds come primarily from a large contract with Fractious County ($4.5 million,) two employment contracts with Rehabilitation departments (DRS) in two other jurisdictions ($1.3 million,) and from a popular golf tournament organized by its Board fundraising committee ($0.3.)

New sources of revenue

Please rate the following aspects of value and cost, using a scale of 1 to 6, where 1 = no effect/nothing, and 6 = Very high.

Type of support / Type of value/cost	Individual Donations	Foundation Grants	Fees for Service	Advocacy coalition
Value				
Crowd-in				
Crowd-out				
Direct mission impact				
Hidden Transaction Costs				
Attracting and managing new relationships				
Managing independence/control externally and internally				
Managing reliability: planning and reserve building				
Managing the extra resources				

National Center on Nonprofit Enterprise ***"We're in the money:" new approaches to nonprofit income strategy*.**
Case Study: Mental Health Recovery (MHR) Worksheet Two : Identifying benefits and types of support

Program: _____

Kind of Benefit	**Types of person, group,organization that benefit**	**Ways in which individuals, groups,public, organizations, benefit**	**Who pays for these benefits**	**How these benefits are paid for**
Private: Accrue to service consumers willing and able to pay fees			**Service consumers:**	**Fee/ Price for service/product:**
Group: Accrue to specific constituencies associated with causes that donors wish to support with gifts and grants			**Donors:** **Foundations:**	**$gift, time volunteered or goods-in-kind:** **Grant/loan:**
Public: Accrue to the general public, supportable by public financing (contracts and grants)			**Branch of govt.:** **State:** **County/City:**	
Trade/Exchange: Accrue to organizational partners in a quid pro quo relationship			**Partner organizations:** **Individuals:**	**Contract payments:** **Barter:**

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