POINT OF VIEW

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THE FINANCIAL HEALTH OF PHILADELPHIA–AREA NONPROFITS

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This report, *The Financial Health of Philadelphia-Area Nonprofits*, was commissioned earlier this year by The Philadelphia Foundation with the intention of presenting actionable information for nonprofit organizations, their leaders, funders, policymakers and the general public. This report follows a 2010 nonprofit study commissioned by The Philadelphia Foundation.

Residents of the five Pennsylvania counties of Greater Philadelphia rely on nonprofit organizations in many facets of everyday life and community. As nonprofits go, so go the services and amenities that impact quality of life, often health and safety. It is with this latter point in mind that The Philadelphia Foundation has focused much of its efforts over the last decade on "organizational effectiveness" – examining, promoting and funding sound fiscal, governance and leadership practices, especially among organizations serving the most vulnerable.

This report demonstrates that there is much more work to be done to strengthen nonprofit organizations in our area. Moving from "getting by" to "getting strong" requires that more attention and talent be dedicated to financial resilience by executives, boards and funders. Approximately 40% of organizations are not generating positive operating margins and will therefore find it difficult to focus on improving service outcomes. Seven percent of nonprofits are technically insolvent, yet neither the organizations themselves nor the wider community have a clear understanding of what it would meant for them to fail, or the implications of that failure for the populations they serve.

The authors, as experienced consultants, suggest sound approaches for addressing financial risks within organizations. They also suggest that funders self-critically examine the extent to which their restrictions on "overhead" or "administration" are contributing to the fragility of nonprofits. The groundwork is also set for more segmented or granular examinations of the region's nonprofits, as others may wish to pursue in response to this study. This report is a good start.

We want to thank the authors and Nadya K. Shmavonian, the Director of the Nonprofit Repositioning Fund, for all they did to bring this report to fruition.

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EXECUTIVE SUMMARY

As nonprofit organizations in the five Pennsylvania counties of Greater Philadelphia (Bucks, Chester, Delaware, Montgomery and Philadelphia) emerge from the financial crisis of the last decade and head into a very different and hard-to-forecast political and economic environment in the future, financial discipline, smart growth and strong governance are more important than ever. Accordingly, many nonprofit executives and governing boards are asking new questions about the organizations they govern. What risks do we face?[1] How risky are we in relation to our peers? Are we doing the right things to understand and mitigate our risks? How should we balance financial risk against programmatic reward? What should we do to reduce the potential hardships from financial distress?

Unfortunately, very few nonprofits have processes in place to address these issues of financial risk management. However, our research suggests that this can and must change.

- Nonprofits in the Philadelphia five county area are fragile: roughly 7% are technically insolvent (i.e. liabilities exceed assets); over 20% have less than one month of cash reserves (i.e. virtually no margin for error); and over 40% have net operating margins of zero or less. In aggregate, we believe that fewer than 40% of nonprofits can be characterized as financially strong. Yet our experience in other geographies suggests that many executives and governing boards don't fully understand the financial condition of their organizations or how they compare to peers.
- Practices such as scenario planning, benchmarking and self-rating, as well as setting explicit financial stability targets, can improve risk management. While we have seen a few organizations already doing these things, most are not.
- Distressed nonprofits have very limited ways to recover, so executives and governing boards must do all they can to reduce the risk that their organization becomes distressed in the first place. And they must take prompt, decisive action if it does.

In what promises to be a continuously volatile market for nonprofit organizations, we believe that executives and governing boards must make dramatic improvements in financial risk management over the next few years in order to bring more stability to vital programs and the communities they serve.

National concerns about risk and financial stability among nonprofits have been increasing recently, motivated by some high-profile nonprofit failures, the potential impact of rising interest rates, regulatory changes to health and human services systems, and rising real estate costs, to name a few factors. These concerns have only sharpened since the 2016 election, as nonprofits grapple with increased uncertainty around government funding levels and sources, and the possibility that tax code changes will reduce incentives for philanthropic funding. While planned dissolutions can be a responsible decision for some organizations to make, we can all agree that unanticipated closures in bankruptcy do not represent adequate fiscal stewardship of nonprofit organizations.

This report introduces important fiduciary steps that organizations can take to manage their financial health and their financial risks better. These recommendations build upon a similar 2016 study on how to adapt private sector risk practices to New York nonprofits that was conducted by SeaChange Capital Partners, Oliver Wyman, and GuideStar. We have attempted to identify actions that will be high-impact and potentially transformative over time, but that are also practical and can be implemented now. We believe that the opportunity to create stronger, more stable nonprofits is real – but also that the risks of inaction are real, and substantial. Organizations that do not adopt risk management practices may find themselves in an increasingly precarious situation.

1 By "risk" we mean unexpected events and factors that may have a material impact on an organization's finances, operations, reputation, viability, and ability to pursue its mission

THE SCALE OF THE CHALLENGE: HOW "RISKY" IS THE ENVIRONMENT FOR GREATER PHILADELPHIA'S NONPROFITS?

Our analysis of the financial results of Philadelphia-area nonprofits illustrates just how fragile many nonprofits are. It should provide useful context for nonprofit executives and board members to understand their organizations' absolute and relative risk profile. It should also help funders to better understand the challenging dynamics facing the region's nonprofits. An important point of context must be added: this report is based upon 2014 IRS Form 990 data that pre-dated the 2015 Pennsylvania budget impasse, a difficult passage from which many executives in hard-hit fields (i.e., health and human services) suggest their organizations have not fully recovered.

The last time the Philadelphia five-county region was studied, in a 2010 study conducted by The Philadelphia Foundation,[2] there were over 15,000 nonprofits in the region, with 242,000 reported employees and more than $11 billion in annual wages, providing critical services to a large number of area residents. Of the 15,000, roughly half file tax returns in some form (with others exempted due to factors such as religious status), and of the filers, roughly 20% file full 990 tax forms. This paper is based on the analysis of the data from Form 990, captured in the GuideStar database.

The analysis excludes organizations categorized as educational institutions and hospitals & care organizations (as indicated by NTEE codes beginning with "B" or "E" codes) since the operating models for these entities are different than direct service organizations – which are the focus of this report. Educational institutions and hospitals tend to generate revenues on a fee-for-service basis, and as a result, may have greater access to funding from capital markets and contingent funding sources. In aggregate, in 2014, the 990 filers included in the analysis had revenues of slightly over $16 billion, and operated with a positive net income margin of roughly 11% (when including revenues from asset sales and investment income.) Margins have been stable to improving; the equivalent figure in 2010 was only 3%.

The "balance sheet" of these nonprofits also looks reasonably healthy – in aggregate. There are three important measures of a nonprofit's risk-bearing capacity that executives and governing boards should keep in mind: 1. Cash to cover immediate needs; 2. Unrestricted net assets as the best measure of a nonprofit's "equity" that is available to bear losses or make investments; and 3. Operating reserves (the portion of the equity that is available in the short term, calculated as net unrestricted assets less fixed assets.). On average, Greater Philadelphia nonprofits don't look too bad on these metrics. The median nonprofit in the region, for example, has over three months of cash in the bank. While this ratio is substantially lower than the six-month cash reserve level that many nonprofit experts suggest is appropriate, it at least suggests a modest degree of financial cushion.

2 *It Matters… But Is It Working?* A White Paper Series on Our Region's Nonprofit Sector Fiscal Health & Sustainability, The Philadelphia Foundation, drawing from demographic research about the nonprofit sector in Southeastern Pennsylvania, conducted by the Economy League of Greater Philadelphia, July 2010.

In aggregate and on average, then, the picture is relatively positive. However, the health – and riskiness – of the region's nonprofits are of greater concern when viewed at the individual organizational level. The very different circumstances facing individual organizations (and within different fields) become much clearer when the industry-level data are disaggregated.

- **Roughly 7% of the region's nonprofits are technically insolvent** (i.e., their liabilities exceed their assets), and in fields such as health and human services, the insolvency rate is almost double the overall average. Many of these organizations are limping from payroll to payroll with less than a month of cash, effectively borrowing from vendors (by delaying payment) and/or dipping into restricted funds. These organizations have no capital for investment and no ability to consider a thoughtful wind-down given the lack of resources to fund the associated one-time costs.
- **Many organizations have virtually no margin for error** While the nonprofit community as a whole has slightly more than three months of cash in the bank, roughly a quarter of nonprofits have a month or less of cash. And even this actually overstates the real cushion for weaker organizations, since much of the available cash is restricted to certain purposes. At best, fewer than 40% of organizations appear to be financially strong, with more than six months of cash or operating reserves.
- **As noted previously, while the total nonprofit community earned an average net income margin of 11%, the median nonprofit had a margin of only 2.8%**. And over 40% of nonprofits actually had a zero or negative operating margin – in other words, almost half of area nonprofits are running at a loss or at least producing no surplus.
- **Most nonprofits are small but the large ones provide the vast majority of services:** 69% have operating budgets less than $1 million; 19% are between $1 and $5 million; and 4% are between $5 million and $10 million. Only 8% have budgets of $10 million or above. There are fewer than 50 organizations of more than $50 million in the five counties.

  However, the smallest 50% of the organizations contributed less than 5% of total service provision while the largest 10% provided almost 85%. And while there is some evidence of economies of scale operating in larger nonprofits (for example, they tend to have slightly lower overhead expenses, expressed as a percentage of revenue), 20% to 30% of the largest organizations still have negative margins and very limited cash and operating reserve cushions. While these large organizations are, on average, less likely to encounter distress than are small organizations, there are still many large organizations in very precarious positions – and the cost to society of distress at these large organizations, in terms of potential disruption to critical services, is substantial.
- **Nonprofits differ greatly in their reliance on philanthropy.** The median level of philanthropy is about 18% as a percentage of total revenue, but this figure varies greatly by field and size. The median health and human services nonprofit earns only 4.7% of revenue from philanthropy, compared with nearly 50% for the average environmental and arts, culture and humanities nonprofit. Similarly, the median "very small" (<$1MM) organization receives 24% of revenue from philanthropy, the median very large nonprofit less than 1%. The largest organizations, delivering the most services, and particularly focused on health and human services, are least supported by philanthropy, and most supported by earned revenue associated with government contracts.

- **The sector is painfully exposed to even modest reductions in government funding.** A 5% reduction in government funding (if evenly distributed across the sector) would result in nearly 20% of nonprofits that currently earn a surplus moving into deficit. For some of these institutions, the deficits would be modest relative to their available financial resources, but for the 20% of those worst-impacted by the reduction (i.e., roughly 20% x 20% = 4% of current surplus-earning nonprofits) the deficits would lead to insolvency in 5 years.

- **"Overhead"** *and administrative expense performance also vary widely across different nonprofits.* Overhead, typically defined as the sum of all administrative and fundraising (i.e., non-program related) expenses, is a difficult issue for nonprofits. Many funders want to see their dollars directly support program expenses, rather than overhead; at the same time, nonprofits have a legitimate need to spend responsibly to create financial systems, IT infrastructure, HR capabilities, and other "administrative" capabilities necessary to support the organization over time. The data suggests that the median Greater Philadelphia nonprofit allocates about 11% of its expenses to administration.

  This figure is comparable to what we have observed in other geographies, and has been stable over the last five years. As with other metrics, though, the median does not show that there is considerable variation across institutions. The 30th percentile spends only 5.9% on administrative expense, and the 70th percentile spends 18%. More remarkably, the bottom 10% of nonprofits claim to spend nothing on administration (which is likely an illustration of something we all know to be true – 990 data isn't perfect!), while the top 10% allocate 36% of expenses to admin. There is no "right" answer for what overhead spending should be, but new research advocates adopting benchmarking by sector to guide overhead management (for additional discussion on this topic, please see Bridgespan's 2016 report, "Pay-What-It-Takes Philanthropy").[3] Nonprofit executives and governing boards should be aware of how their organization's expenses compare to peers, and prepared to argue why their specific level of spending is neither so low as to starve the organization of needed administrative support, nor so high as to represent inefficiency or waste.

- **Sub-fields exhibit very different characteristics.** In particular, as noted already, the health and human services field appears weaker than other nonprofits on almost every metric of financial health. To illustrate: the cash on hand ratio for the median Philadelphia-area nonprofit is over three months, at 3.4. The same ratio at the median Philadelphia-area health and human services nonprofit, meanwhile, is half that level, at 1.7. Again, these 2014 data precede the Pennsylvania budget impasse, which disproportionately affected nonprofits working in fields that are particularly dependent on government funding, like health and human services (although larger institutions such as hospitals may have greater access to credit lines, as well as more predictable fee-for-service revenue streams).

- **Geographic differences don't seem to matter as much as we expected.** Urban Philadelphia and the suburban and exurban areas of the surrounding four counties obviously have very different economic and demographic characteristics. The data on nonprofit health across the five counties, however, shows remarkably little variation. (We've also analyzed the differences among states nationally, and between major urban areas and the rest of the country, and – somewhat surprisingly – have observed relatively little variation in nonprofit health metrics across any of those boundaries.)

3 Please see: https://ssir.org/up_for_debate/article/pay_what_it_takes_philanthropy; or https://ssir.org/images/articles/2009FA_feature_Gregory_Howard.pdf

We are not suggesting that nonprofit organizations should earn consistently large surpluses. After all, the organizations exist to pursue programs, not to build up internal resources. However, the profound under-capitalization and small scale of most organizations impedes necessary investments and makes prudent risk management all the more important. Yet, greater scale is not a panacea. For example, a large, well-run nonprofit organization with economies of scale might be able to earn a surplus of 1% on revenue in a typical year if it relies principally on government contracts. However, even after five years the resulting retained surplus would amount to less than three weeks of expenses. This is not enough to support appropriate investments in technology or infrastructure or to provide a cushion against unforeseen risks. Larger nonprofits typically have a lower proportion of revenue coming from private philanthropy. They are therefore more reliant on government contracts. Beyond a certain tipping point, even the most efficient organizations will not necessarily have sufficient private funds to offset the deficit from their government funding.

THE TRACK RECORD: HOW NONPROFITS HAVE DEALT WITH RISK

The sector's overall fragility means that many nonprofits will experience financial distress. In a 2016 study of nonprofits in New York City, SeaChange and Oliver Wyman interviewed executive directors, board members, and funders of nonprofits that had struggled. Some went bankrupt. Others were rescued at the 11th hour by other organizations. Others "saw the writing on the wall" early enough to enter into an orderly merger or dissolution. Across the discussions, several themes emerged, as did some "worst practices", themes that will likely resonate for nonprofit executives and funders in the Greater Philadelphia region. Among the factors reported by these distressed organizations (not universally, but frequently):

1. The organizations were fragile to begin with. Before the crisis hit they had limited resources and several years of deficits that had eroded whatever resources had once been in place.
2. The organizations had a longstanding challenge in recruiting and retaining a strong chief financial officer.
3. The crisis was precipitated by an event: the departure of the executive director; the non-renewal of an important funder; a change in government priorities or in the nature of government funding; a very meaningful (25-50%+) increase in scale; a real estate project that was large compared to the operating budget; or the emergence of a contingent liability (e.g., a Medicaid audit).
4. The organizations failed to do explicit scenario planning despite facing inherently uncertain situations. They did not pay enough attention to contingencies and milestones. Organizations were surprised by crises that could have been foreseen.
5. Trustees were not made fully aware of important long-term trends in financial performance or the operating environment. Important trends were masked by an exclusive focus on annual budgets, and year-to-date and year-over-year "rearview mirror" comparisons.
6. Trustees did not get timely, actionable information at the appropriate level of detail (i.e., by contract, program, or project) before or during the early stages of the crisis.
7. Trustees took too long to realize that there was a problem and then delayed taking action even after they had decided it was necessary. Executive directors and trustees suffered from magical thinking, particularly with respect to fundraising.

THE CONTEXT: STRUCTURAL CHALLENGES

In order to manage financial risk, nonprofit executives and governing boards should be fully aware of the dynamics that make nonprofits particularly vulnerable to economic challenges, differentiating factors that for-profit executives do not always appreciate before they join a nonprofit board. These include, but are not limited to:

- **Tackling the hardest problems:** Many nonprofits address economically intractable and politically unappealing problems that are labor intensive and inherently inefficient. Board members may be faced with systemic conditions that can be far more difficult to address than any they have seen before.
- **Cost-minus funding:** Most nonprofit funding, especially in health and human services, comes in the form of government contracts or restricted grants that virtually guarantee a deficit. Government contracts also create working capital depletion because funding arrives after expenses are paid. These funds are also subject to unpredictable delays in payment.[4]
- **Inflexible funding:** In the nonprofit world, a dollar isn't a dollar – it's usually a dollar with lots of strings, costs and restrictions attached. Typically, a large portion, or all, of grants and contract revenues are required to be allocated to program expenses. This imposes a huge administrative burden on nonprofits, as every penny of program spending needs to be documented. It also leaves nonprofits scraping to pay for critical functions like IT, finance, and executive management that do not qualify as "program" expenses – but are in fact vital to the health and survival of the institution.
- **One-way bets:** Nonprofits face contingent liabilities that can swamp them financially. These include government claw-backs for disallowed expenses, after-the-fact audits, and unilateral retroactive rate reductions.
- **Zero-sum philanthropy:** The total supply of philanthropy is largely fixed.[5] Large organizations working in the most difficult issue areas will always be overwhelmingly reliant on government funding. Similarly, arts and culture organizations that are more reliant upon philanthropy, face great competitive challenges. And finally, while philanthropy may be flat – or even decline – when the economy is unpredictable, human need often rises, placing greater demand upon social service agencies.
- **Cost disease:** Nonprofits often provide face-to-face, labor-intensive services that do not become more efficient with technology – as a result, costs often rise faster than revenue. The real costs of these services has risen substantially over time and is likely to do so in the future.[6] There are few, if any, magic bullets in this arena.

4 Advocates for the nonprofit sector are working to educate government about the risks these contracts impose on nonprofits and to advocate for changes. While trustees should hope that these efforts are successful, they cannot shirk their governance responsibility for risk management on the basis that "it's the government's fault."

5 Philanthropy as a percentage of GDP has moved within a very tight band for at least the last 45 years (see https://philanthropy.com/article/The-Stubborn-2-Giving-Rate/154691), and philanthropy per nonprofit has actually fallen, as the number of nonprofits has grown faster than GDP and the population. Nevertheless, many nonprofits underinvest in development or have boards that do not recognize the vital role they must play in raising unrestricted funds.

6 See http://www.amazon.com/The-Cost-Disease-Computers-Cheaper/dp/0300179286 for a fuller explanation of this phenomenon

- **Recruiting and retention:** Nonprofits face structural challenges in recruiting and retaining high-quality staff in technical skill areas such as finance, accounting, and technology. Factors driving this situation include the small size of many organizations, the challenge in providing career development, and competition from higher-paying for-profits.
- **Gales of creative destruction:** Nonprofits operate in a dynamic environment. Challenges include demographics, funding fashions, political priorities, real estate costs, and low working capital. The weak financial position of many nonprofits can make it difficult to anticipate and respond to these and other challenges.

It is no surprise that many nonprofits are *always* living close to the edge. A common response to these challenges is to attempt to raise more unrestricted private philanthropic dollars. This solution won't work, at least not for the community as a whole. Experience shows that the amount of available private philanthropy is relatively fixed – it varies little year to year, and has demonstrated no ability to grow at a faster rate than GDP. While individual nonprofits may succeed in their mission of raising more, the sector in aggregate won't. And it is just as unlikely that public sources of support will increase any time soon. What does this mean for nonprofit leadership and governance, and what can be done to better anticipate and manage risks in this challenging environment?

ONE PATH FORWARD: MORE ROBUST AND SYSTEMATIC RISK MANAGEMENT

Enterprise Risk Management in for-profit companies and our interviews with nonprofit executives suggest a set of best practices for nonprofit risk management. They are in use at several leading nonprofits, and each one can make a real difference to any organization that adopts it. These practices presume a level of staff and board oversight that may present a challenge, particularly to very small organizations. They are introduced here as best practices that can be adopted by nonprofits, because without increased fiscal rigor, many distressed nonprofits will be compromised in their ability to deliver upon their missions.

This material is presented with the hope that nonprofit executives and board members as well as funders can face into fiscal challenges proactively, and manage to them more aggressively. In cases where from a practical standpoint the practices cannot be fully implemented, executive directors and governing boards should apply the mindset behind the practice to the greatest extent possible. Development of these skills will be critical to the nonprofit sector's success. These risk management practices can serve as the basis for board and staff development among the region's nonprofits. Even if imperfectly adopted, the conscious act of engaging in these processes will obviate any organizational tendency toward 'head in the sand' leadership and governance practices.

PRACTICES OF AN ORGANIZATION WITH HEALTHY RISK MANAGEMENT

1. **Governance and Accountability for Risk Management:** Oversight for risk management is part of the board's legal duties of care, loyalty, and obedience. It should be an explicit responsibility of a board fiduciary committee such as the audit and/or finance committee,[7] with an appropriate dedication of time to the task. One leading organization reports that roughly 10% of total board discussion now revolves around risk; another told us that a recent Board meeting, scheduled for an hour and a half, had to be extended when the first hour was consumed by an unplanned risk discussion! The committee responsible for risk must have direct communication with the finance function and with staff who have time to ask "What if?" It should report to and elicit input from the full board. It should ensure that the board sets the right tone by communicating a commitment to risk management throughout the organization. This should be part of its strategy, culture, and pursuit of the mission.[8] Organizations can be well served by an explicit financial risk tolerance statement, a process that is similar and of parallel importance to the mission and vision statements. It needs to indicate the limits for risk-taking and their willingness to trade short-term program impact for longer-term sustainability. A thoughtful risk tolerance will reduce the likelihood that an organization is either cavalier about risk or paralyzed by excessive risk aversion. The exercise of articulating this statement is, in and of itself, a vital step toward practicing "eyes wide open" fiduciary and strategic governance.

7 Some specialized risks – for example data/cybersecurity – might be located in other committees. Unlike financial institutions, even the largest nonprofits do not face the range of risks that would merit a dedicated "risk committee."

8 For a discussion on the importance of "tone" and of risk management in the for-profit setting see http://www.wlrk.com/webdocs/wlrknew/AttorneyPubs/WLRK.24301.15.pdf.

2. **Scenario Planning:** Organizations should keep a running list of the major risks they face. For each, they should indicate its likelihood and the expected loss (probably in terms of unrestricted net assets) if it occurs. Then they should consider actions to reduce the likelihood of it occurring and mitigate the damage if it does. The list may include a wide range of a wide range of possible risks depending on the organization. Examples include lease renewal, cost overruns on a capital project, the non-renewal of an important funder, and leadership succession. (For further discussion of this topic, please see Stanford Graduate School of Business's study, "2015 Survey on Board of Directors of Nonprofit Organizations", which noted that "Two thirds (69 percent) [of nonprofits] do not have a succession plan in place for the current executive director or CEO. Three quarters (78 percent) could not immediately name a successor if the current executive director were to leave the organization tomorrow."[9]

3. **Recovery and Program Continuity Planning:** Organizations should have plans for how to maintain service in the event of a financial disaster. Large organizations should also consider developing "resolution plans" or "living wills" to expedite program transfer. (These concepts were developed in the banking industry, where regulators determined that having an institution fail abruptly would cause too much disruption for its customers and for the broader financial system, and hence required that each major institution determine in advance a plan for an orderly unwind and shut down or sale of their operations.) These living wills should be discussed in advance during stable times with government agencies and partners so everyone is prepared to act in a crisis.

4. **Environmental Scan/Competitive Landscape Assessment:** On an annual basis, organizations should brief governing boards about longer-term trends in the operating environment. They should consider the potential benefits of exploring various forms of organizational redesign in response, such as collaborations, mergers, acquisitions, joint ventures, partnerships, outsourcing, managed dissolutions, and divestments. This should become a routine strategic consideration for nonprofit boards.

5. **Benchmarking and Self-rating:** Organizations should compare their financial performance to peers on an annual basis using IRS 990 data (or another source of systemic nonprofit financial information). They should also ask umbrella groups to collect more detailed and timely information from the peer group. Another option is to use a self-rating tool to combine financial measures into an overall indicator of organizational health. Funders can play a role in supporting and routinizing the practice of benchmarking by field of practice.

6. **Financial Stability Targets:** Organizations should have targets for operating results. An example might be not having two consecutive years of deficits. They should also have targets for cash, unrestricted net assets, operating reserves, and access to credit. Board members should develop contingency plans for when minimum targets are not met. Since earning the requisite capitalization is so difficult, organizations should think creatively about how to build the necessary reserves. Ideas might include one-time capital campaigns and pledged funds from board members for use in a crisis. Organizations should put in place monitoring and governance processes to ensure that reserves are not used to fund operating deficits.

9 2015 Stanford Graduate School of Business study, 2015 Survey on Board of Directors of Nonprofit Organizations

7. **Reporting and Disclosure:** Larger organizations (i.e., those with budgets > $10 million) should summarize their financial and programmatic results in a short plain-English version of the management discussion and analysis section of the SEC's Form 10-K. This report should also cover their opportunities and risks in the context of internal and external conditions. Creating this type of report would give a sense of urgency to the underlying processes. It could also help reassure stakeholders such as board members, banks, and regulators that the organization is doing all it can to ensure long-run sustainability.

8. **Board Composition, Qualifications, and Engagement:** Risk management requires a functioning partnership between capable management and a strong board that includes a critical mass of experienced, educated and engaged individuals. Organizations serious about risk management must redouble their effort to recruit board members with a wide range of experience and a diversity of thought processes and backgrounds. They need to empower high-functioning committees. They also need to ensure ongoing education for both new and existing board members. Board members cannot participate in meaningful risk management unless they consider the organization's financial fundamentals and drivers, such as critical contracts and their allowed and disallowed cost structures. They also must know the distinction between direct/indirect and allowed/disallowed costs. Many organizations, particularly large, complex ones, would benefit from having an experienced nonprofit executive on their board with firsthand experience of the programs and the associated funding streams.

While it is understood that few smaller nonprofits will be able to implement all of these practices, all will benefit from spending more time anticipating and preparing for risks, based upon the guidance provided here.

A CALL TO ACTION

What to do? For every group of constituents, there are a few hard but simple actions to consider.

1. Look at these regional data with your own organization in mind. Where does your organization fit among your peers? Awareness is the first step toward action.
2. Make every effort to adopt the risk management practices and develop the associated capabilities recommended in this report.
3. Be prepared to face into the reality that stronger risk management still does not guarantee survival. But knowledge is power. Knowledge may lead your organization to explore – in a timely and directive manner – consolidation, mergers and acquisitions, divestments, and orderly wind-downs as a normal part of a vibrant nonprofit sector, just as they are in the for-profit sector.

The alternative to these practices can be tragic, though, when distress causes an organization to lose the capacity to make wise choices. This can result in exposing vulnerable people to the risk of disrupted services or research. It can also mean that hardworking staff lose paychecks or pensions and that board members are exposed to personal liability for unpaid payroll taxes, etc. And in bankruptcy, everybody loses as scarce philanthropic assets are squandered on transaction costs. Similarly tragic are "zombie" nonprofits that are too weak to provide effective or efficient services and use whatever resources they can muster for organizational survival.[10]

Unfortunately, distressed or zombie nonprofits have few options for recovery. Unlike for-profits, they cannot attract funders with reduced price, seniority, or other advantageous terms. Nor are there any specialized nonprofit turnaround funders to evaluate and assume financial risks. In fact, most private funders run at the first sign of trouble, creating a nonprofit version of a run on the bank. A nonprofit's best hope, if trouble comes, is to hobble along. This can mean hollowing out the program, freezing salaries, reducing headcount, borrowing from vendors, using restricted cash for impermissible purposes, and begging existing supporters (including board members) for support. The potential for impact becomes almost nil.

When nonprofits encounter serious financial distress, therefore, board members and executive directors must have the will to act, and to act quickly – even if that means a substantial restructuring, wind-down, or merger of their programs. Both "triggers" – i.e., distress conditions that will trigger a strategic response – and specific contingency action plans should be defined and committed to in advance.

10 Since creditors cannot put a nonprofit into involuntary bankruptcy and many nonprofits are too small for creditors to bother with, the zombie state can continue for a protracted period

For funders, the call to action is simpler. Nonprofits simply cannot build necessary reserves when substantially all revenue comes in the form of restrictive grant and cost-minus contracts. Funders must begin to explore more sustainable funding models – more flexible and less restrictive terms, provision of general operating support to vital nonprofit partners, addition of specific overhead funding vehicles, or creation of "rescue" funds to shore up distressed nonprofits. Without these steps, too much vital capacity is likely to fail out of the system in the coming years, with too much adverse impact on the collective good of society.

Funders – both public and private – can also play a vital role in encouraging nonprofits to consider the three action steps outlined in this section. Funders have more power to normalize these strategic practices than is sometimes recognized. The questions funders ask in proposal reviews, the follow-up questions they ask on site visits and grantee reporting, the ancillary technical assistance they provide to the nonprofit community, and the sometimes difficult and direct conversations they can have with their grantee partners are all inestimably powerful tools for strengthening nonprofit risk management in an otherwise very uncertain climate.

Philadelpia Area Nonprofits Financial Health at a Glance

Almost $16BN in revenue

11% margin (net income) in aggregate...

...but **40% of nonprofits** have zero or negative operating margin

Average of **10 weeks of expenses** on hand as cash in the bank

... but over **20%** of organizations **have less than one month of cash** on hand

7% of institutions are technically insolvent...

... but the number of **insolvent institutions almost doubles**, to **13%**, in fragile sectors such as Health and Human Services

A **5% reduction** in government funding will push **nearly 20%** of nonprofits from surplus to deficit – and drive almost **5% to insolvency** in less than **5 years**

APPENDIX: PHILADELPHIA-AREA NONPROFITS

Exhibit 1: Aggregated Financial Information (in Millions)

INCOME STATEMENT	2010		2011		2012		2013		2014	
Revenue, gains and other support										
Program Revenues	$6,228	53%	$6,547	49%	$7,505	57%	$8,734	59%	$9,588	60%
Contributions	$5, 117	43%	$5,813	44%	$4,906	37%	$5,182	35%	$5,458	34%
Investments, rental, special events and other	$352	3%	$385	3%	$385	3%	$447	3%	$503	3%
Net gain (loss) from asset sales	$149	1%	$593	4%	$291	2%	$370	3%	$488	3%
Total Revenues, Gains and Other Support	**$11,846**	**100%**	**$13,338**	**100%**	**$15,647**	**100%**	**$14,733**	**100%**	**$16,037**	**100%**
Expenses										
Program	$10,074	88%	$10,599	88%	$10,684	88%	$11,526	88%	$12,687	88%
Total supporting services	$1,411	12%	$1,484	12%	$1,451	12%	$1,542	12%	$1,665	12%
Management and general	$1,256	11%	$1,330	11%	$1,285	11%	$1,374	11%	$1,490	10%
Fundraising	$155	1%	$154	1%	$167	1%	$168	1%	$176	1%
Total expenses	**$11,485**	**100%**	**$12,083**	**100%**	**$12,135**	**100%**	**$13,068**	**100%**	**$14,352**	**100%**
Net Income	**$361**	**3%**	**$1,255**	**9%**	**$952**	**7%**	**$1,666**	**11%**	**$1,685**	**11%**
Program Economics										
Program expenses Less:	$10,074		$10,559		$10,684		$11,526		$12,687	
Program revenues and fees for service	$(6,228)		$(6,547)		$(7,505)		$(8,734)		$(9,588)	
Program-level philanthropy need	$3,846		$4,052		$3,179		$2,792		$3,098	
Add: Management and general expenses	$1,411		$1,484		$1,451		$1,542		$1,665	
Pre-philanthropy deficit	$(5,258)		$(5,536)		$(4,630)		$(4,334)		$(4,764)	
Add: Net philanthropy	$5,117		$5,813		$4,906		$5,182		$5,458	
Operating surplus / (deficit)	-$141		$277		$276		$848		$694	
Add: Gain/(loss) on investments and asset sales	$502		$978		$676		$817		$991	
Net income	**$361**	**3%**	**$1,255**	**9%**	**$952**	**7%**	**$1,666**	**11%**	**$1,685**	**11%**

BALANCE SHEET	2010	2011	2012	2013	2014
Assets (Selected)					
Cash and savings	$2,582	$2,726	$2,576	$2,837	$3,189
Pledges, grants and other rec	$1,799	$1,575	$9,086	$9,074	$8,814
Accounts rec	$1,097	$1,176	$1,205	$1,390	$1,375
Securities and investment	$13,050	$14,927	$15,929	$18,653	$20,923
Intangibles and other	$1,736	$2,858	$1,734	$2,028	$2,106
Fixed asset	$7,752	$14,203	$7,765	$8,396	$8,675
Total assets	**$27,142**	**$29,999**	**$38,294**	**$42,377**	**$45,081**
Liabilities (Selected)					
Accounts payable	$2,736	$2,880	$2,903	$3,190	$3,463
Tax exempt bond	$1,957	$2,098	$1,891	$2,374	$2,452
Secured mortgage and notes payable	$1,549	$1,698	$1,681	$1,820	$1,766
Other liabilities	$4,314	$4,203	$11,672	$12,056	$11,573
Total liabilities	**$10,556**	**$10,878**	**$18,147**	**$19,440**	**$19,254**
Net assets (Selected)					
Temporarily restricted net assets	$1,487	$1,676	$1,639	$1,658	$1,845
Permanently restricted net assets	$1,636	$1,757	$1,785	$1,901	$2,116
Un-allocated net assets	$4,538	$5,126	$5,146	$5,429	$8,680
Net assets	**$16,585**	**$19,121**	**$20,147**	**$22,937**	**$25,827**
Total liabilities and net assets	**$27,142**	**$29,999**	**$38,294**	**$42,377**	**$45,081**

RATIOS (MONTHS)	2010	2011	2012	2013	2014
Receivables	3.03	2.73	10.18	9.61	8.52
Payables	2.86	2.86	2.87	2.93	2.90
Cash	2.70	2.71	2.55	2.60	2.67
Unrestricted net assets	10.81	12.11	13.24	14.66	15.48
Operating reserves	3.72	3.99	4.15	3.86	3.73

Exhibit 2: Insolvency indicators

INSOLVENCY (LIABILITIES ARE GREATER THAN ASSETS)					
Percentage of nonprofits that are insolvent by major industry group and year	**2010**	**2011**	**2012**	**2013**	**2014**
Arts, Culture and Humanities	6%	4%	5%	4%	5%
Community Capacity	4%	4%	4%	4%	5%
Environment and Animal-Related	3%	4%	1%	4%	2%
Health and Human Services	12%	12%	12%	13%	13%
Other	9%	7%	7%	6%	5%
Philanthropy	5%	6%	4	3%	3%
Religious Institutions	12%	7%	6%	7%	5%
Science, Technology and Social Sciences	7%	8%	8%	8%	9%
Youth Development	5%	6%	5%	5%	5%
Total	**9%**	**8%**	**7%**	**7%**	**7%**
Percentage of nonprofits that are insolvent by size and year	**2010**	**2011**	**2012**	**2013**	**2014**
Very Small (<$1MM)	7%	6%	6%	6%	6%
Small ($1–5MM)	11%	10%	10%	11%	10%
Medium ($5–10MM)	15%	13%	11%	11%	14%
Large ($10–50MM)	8%	9%	8%	7%	9%
Very Large ($50MM+)	5%	2%	11%	10%	8%
Total	**9%**	**8%**	**7%**	**7%**	**7%**
Percentage of nonprofits that are insolvent Health and Human Services, by size and year	**2010**	**2011**	**2012**	**2013**	**2014**
Very Small (<$1MM)	11%	11%	12%	13%	12%
Small ($1–5MM)	14%	13%	12%	16%	14%
Medium ($5–10MM)	21%	21%	13%	11%	19%
Large ($10-50MM)	8%	11%	10%	10%	11%
Very Large ($50MM+)	5%	5%	16%	14%	12%
Total	**12%**	**12%**	**12%**	**13%**	**13%**

Exhibit 3: Liquidity/Debt ratios (2014)

MONTHS OF RESERVES BY TYPE									
Aggregate Distribution (2014)	**10%**	**20%**	**30%**	**40%**	**50%**	**60%**	**70%**	**80%**	**90%**
1. Cash	0.2	0.7	1.4	2.4	3.4	5.1	7.5	12.0	23.4
2. Equity Proxy	0.0	0.0	0.1	1.9	4.1	7.6	13.3	29.4	74.2
3. Operating	-10.8	-0.6	0.0	0.7	2.2	4.3	7.7	15.9	49.1
4. Investments	0.0	0.0	0.0	0.0	0.0	0.0	0.0	5.4	37.4
5. Cash and Investments	0.3	1.1	2.2	3.5	5.5	8.8	14.4	27.7	76.1
Health and Human Services Distribution (2014)	**10%**	**20%**	**30%**	**40%**	**50%**	**60%**	**70%**	**80%**	**90%**
1. Cash	0.1	0.3	0.6	1.1	1.7	2.6	3.8	6.0	11.2
2. Equity Proxy	-3.0	0.0	0.8	2.0	4.0	6.6	10.7	20.9	63.6
3. Operating	-10.5	-0.9	0.0	1.0	2.1	3.7	6.4	11.7	30.9
4. Investments	0.0	0.0	0.0	0.0	0.0	0.0	0.0	1.1	12.2
5. Cash and Investments	0.1	0.5	0.8	1.6	2.6	3.9	6.3	11.1	28.3

Exhibit 4: Nonprofit marginal analysis

NONPROFIT MARGINAL ANALYSIS (NET INCOME / REVENUES)									
Distribution (2014)	**10%**	**20%**	**30%**	**40%**	**50%**	**60%**	**70%**	**80%**	**90%**
Arts, Culture and Humanities	-25.1%	-9.2%	-2.4%	0.7%	4.3%	8.0%	13.4%	21.3%	34.3%
Community Capacity	-21.8%	-8.7%	-4.3%	-0.2%	2.5%	6.8%	12.9%	20.9%	33.0%
Environment and Animal-Related	-10.9%	-4.0%	-0.6%	1.7%	4.7%	9.7%	15.9%	25.2%	36.5%
Health and Human Services	-24.7%	-8.8%	-3.0%	-0.4%	1.1%	3.0%	5.9%	10.5%	23.6%
Other	-14.6%	-7.1%	-0.9%	1.6%	3.6%	6.9%	12.2%	20.6%	42.4%
Philanthropy	-18.5%	-5.1%	-1.3%	1.4%	4.2%	7.8%	12.0%	22.7%	36.0%
Religious Institutions	-42.7%	-9.6%	-1.1%	3.5%	7.7%	11.7%	24.3%	47.3%	60.9%
Science, Technology and Social Sciences	-10.4%	-3.6%	-0.1%	2.4%	4.0%	6.2%	9.5%	13.9%	25.4%
Youth Development	-22.5%	-9.3%	-2.4%	0.9%	3.3%	7.9%	16.8%	30.9%	51.9%
Total	**-21.5%**	**-7.8%**	**-2.3%**	**0.4%**	**2.8%**	**5.9%**	**10.2%**	**18.7%**	**34.2%**
Distribution (2014)	**10%**	**20%**	**30%**	**40%**	**50%**	**60%**	**70%**	**80%**	**90%**
Very Small (<$1MM)	-25.8%	-10.1%	-3.2%	0.5%	3.7%	7.8%	13.0%	23.1%	42.3%
Small ($1–5MM)	-20.4%	-7.1%	-2.4%	0.0%	1.8%	3.9%	6.7%	12.3%	25.2%
Medium ($5–10MM)	-6.1%	-2.6%	-0.5%	0.4%	1.3%	3.3%	4.8%	8.1%	14.3%
Large ($10-50MM)	-9.1%	-3.2%	-0.9%	0.5%	2.1%	3.5%	5.2%	11.0%	20.9%
Very Large ($50MM+)	-3.7%	-0.5%	0.3%	0.7%	1.2%	2.7%	4.1%	8.6%	21.2%
Total	**-21.5%**	**-7.8%**	**-2.4%**	**0.4%**	**2.8%**	**5.9%**	**10.4%**	**19.0%**	**36.0%**

OPERATING INCOME MARGIN (NET INCOME LESS ASSET SALES AND INVESTMENTS / REVENUES)									
Distribution (2014)	**10%**	**20%**	**30%**	**40%**	**50%**	**60%**	**70%**	**80%**	**90%**
Arts, Culture and Humanities	-28.3%	-12.3%	-4.1%	-1.0%	2.3%	7.0%	11.3%	18.9%	30.6%
Community Capacity	-22.0%	-9.9%	-4.7%	-0.3%	2.3%	5.7%	11.7%	20.0%	31.4%
Environment and Animal-Related	-16.6%	-5.3%	-2.3%	1.1%	3.5%	8.3%	13.6%	21.4%	32.5%
Health and Human Services	-25.6%	-10.2%	-3.5%	-0.9%	0.6%	2.4%	4.8%	8.9%	18.3%
Other	-23.9%	-11.4%	-4.2%	0.0%	2.1%	4.1%	8.4%	15.3%	26.0%
Philanthropy	-20.3%	-9.6%	-3.0%	0.0%	2.1%	6.0%	9.2%	14.5%	31.8%
Religious Institutions	-55.4%	-18.3%	-7.2%	-1.2%	2.8%	6.6%	12.2%	24.6%	47.5%
Science, Technology and Social Sciences	-10.8%	-4.3%	-0.6%	1.8%	3.4%	5.6%	7.7%	11.8%	20.9%
Youth Development	-31.4%	-16.2%	-4.9%	-2.0%	1.8%	4.2%	9.1%	19.9%	40.8%
Total	**-24.7%**	**-10.3%**	**-3.7%**	**-0.4%**	**1.8%**	**4.4%**	**8.3%**	**14.6%**	**27.8%**
Distribution (2014)	**10%**	**20%**	**30%**	**40%**	**50%**	**60%**	**70%**	**80%**	**90%**
Very Small (<$1 MM)	-30.8%	-12.5%	-4.6%	-0.5%	2.5%	6.0%	10.6%	18.5%	33.4%
Small ($1–5MM)	-23.5%	-10.2%	-4.0%	-1.2%	0.8%	2.9%	5.1%	9.4%	20.1%
Medium ($5–10 MM)	-8.0%	-3.4%	-1.0%	-0.1%	0.8%	1.8%	3.8%	6.6%	11.5%
Large ($10-50 MM)	-11.5%	-5.4%	-1.7%	-0.2%	1.4%	2.6%	4.0%	7.3%	16.5%
Very Large ($50 MM+)	-6.4%	-1.9%	0.0%	0.4%	0.8%	1.4%	3.6%	6.5%	15.4%
Total	**-24.7%**	**-10.3%**	**-3.7%**	**-0.4%**	**1.8%**	**4.4%**	**8.3%**	**14.6%**	**27.8%**

Exhibit 5: Distribution of nonprofits by size and sector (USD 000s)

DISTRIBUTION OF SPEND BY SIZE AND SECTOR (2014 FUNCTIONAL EXPENSES)

In USD 000s

Distribution (2014)	10%	20%	30%	40%	50%	60%	70%	80%	90%
Philanthropy	$32	$75	$124	$209	$306	$487	$734	$1,359	$2,687
Environment and Animal-Related	$56	$98	$185	$237	$338	$553	$839	$1,436	$2,199
Religious Institutions	$54	$96	$164	$193	$266	$351	$472	$1,210	$1,867
Science, Technology and Social Sciences	$91	$153	$372	$503	$1,213	$2,348	$5,593	$9,004	$22,964
Other	$39	$100	$165	$229	$327	$517	$856	$1,684	$4,559
Community Capacity	$92	$146	$201	$252	$340	$466	$716	$1,182	$2,799
Youth Development	$60	$120	$179	$226	$294	$403	$577	$908	$1,787
Arts, Culture and Humanities	$50	$126	$201	$264	$375	$508	$786	$1,365	$3,413
Health and Human Services	$111	$213	$329	$505	$795	$1,219	$2,085	$5,405	$14,677
Entire sector	**$66**	**$138**	**$207**	**$287**	**$418**	**$634**	**$1,038**	**$1,916**	**$6,254**

Distribution (2014)	10%	20%	30%	40%	50%	60%	70%	80%	90%
Very Small (<$1MM)	$44	$93	$143	$191	$238	$305	$393	$514	$714
Small ($1–5MM)	$1,133	$1,255	$1,380	$1,565	$1,798	$2,076	$2,483	$2,995	$3,812
Medium ($5–10MM)	$5,383	$5,681	$5,991	$6,311	$6,711	$7,029	$7,815	$8,564	$9,391
Large ($10-50MM)	$11,295	$12,429	$13,728	$15,389	$17,468	$20,004	$23,002	$26,315	$31,079
Very Large ($50MM+)	$56,265	$59,948	$67,440	$70,404	$75,837	$99,906	$128,442	$182,676	$339,442
Entire sector	**$66**	**$138**	**$207**	**$287**	**$418**	**$634**	**$1,038**	**$1,916**	**$6,254**

Exhibit 6: Distribution of aggregate nonprofit expenditure by size and sector

PERCENTAGE OF TOTAL SEGMENT EXPENSE					
Distribution (2014)	**<10%**	**10%<x<20%**	**20%<x<30%**	**30%<x<40%**	**40%<x<50%**
Arts, Culture and Humanities	$858	$2,685	$5,541	$7,372	$10,478
Community Capacity	$2,851	$6,552	$9,675	$12,469	$16,424
Environment and Animal-Related	$269	$904	$1,560	$2,597	$3,360
Health and Human Services	$4,913	$15,230	$25,637	$39,662	$62,793
NO_NTEE	$774	$1,992	$4,307	$5,993	$7,747
Other	$303	$1,277	$2,438	$3,593	$5,040
Philanthropy	$238	$906	$1,785	$2,599	$4,553
Religious Institutions	$368	$955	$1,609	$2,490	$2,988
Science, Technology and Social Sciences	$223	$778	$1,624	$3,095	$5,782
Youth Development	$870	$2,603	$3,973	$5,634	$7,213
Total	**$11,667**	**$33,883**	**$57,879**	**$85,507**	**$126,379**
Percentage of entire sector	**0.1%**	**0.3%**	**0.5%**	**0.7%**	**1.0%**
Distribution (2014)	**50%<x<60%**	**60%<x<70%**	**70%<x<80%**	**80%<x<90%**	**90%<x<100%**
Arts, Culture and Humanities	$14,339	$21,058	$34,875	$67,472	$467,492
Community Capacity	$21,645	$32,040	$52,084	$97,372	$897,660
Environment and Animal-Related	$4,975	$7,603	$13,805	$20,442	$102,854
Health and Human Services	$92,978	$151,756	$316,328	$884,877	$5,316,036
NO_NTEE	$11,139	$16,420	$31,486	$95,082	$1,950,975
Other	$7,924	$13,416	$23,400	$50,303	$567,326
Philanthropy	$7,065	$10,376	$17,799	$32,341	$1,630,951
Religious Institutions	$3,971	$5,804	$10,090	$20,647	$365,651
Science, Technology and Social Sciences	$9,292	$27,826	$47,572	$102,415	$154,440
Youth Development	$9,711	$13,291	$19,976	$34,856	$11,580,918
Total	**$183,040**	**$299,589**	**$567,414**	**$1,405,807**	**$11,580,918**
Percentage of entire sector	**1.3%**	**2.1%**	**4.0%**	**9.8%**	**80.7%**

Exhibit 7: Philanthropy as a percentage of revenues by size and sector

DISTRIBUTION OF PHILANTHROPY AS A PERCENTAGE OF REVENUE BY SIZE AND SECTOR									
Distribution (2014)	**10%**	**20%**	**30%**	**40%**	**50%**	**60%**	**70%**	**80%**	**90%**
Philanthropy	0.0%	0.0%	6.5%	32.9%	58.7%	87.0%	96.7%	99.7%	100.0%
Environment and Animal-Related	2.7%	19.3%	30.0%	39.0%	49.7%	60.5%	79.7%	93.9%	99.9%
Religious Institutions	0.1%	6.5%	22.0%	48.9%	69.6%	95.0%	99.0%	100.0%	100.0
Science, Technology and Social Sciences	0.0%	0.4%	4.2%	10.0%	31.1%	45.6%	52.6%	74.2%	97.7%
Other	0.0%	0.0%	0.5%	6.7%	16.3%	44.8%	79.5%	98.4%	100.0%
Community Capacity	0.0%	0.0%	2.8%	8.9%	16.9%	28.5%	42.2%	67.0%	94.9%
Youth Development	0.0%	0.8%	4.6%	11.6%	19.9%	35.3%	61.3%	84.1%	99.0%
Arts, Culture and Humanities	4.4%	14.0%	27.6%	38.5%	50.6%	60.3%	69.1%	77.9%	93.0%
Health and Human Services	0.0%	0.0%	0.0%	1.1%	4.7%	14.2%	30.0%	60.2%	96.2%
Total	**0.0%**	**0.0%**	**1.3%**	**7.3%**	**18.1%**	**33.9%**	**56.3%**	**80.8%**	**99.3%**
Distribution (2014)									
Very Small (<$1MM)	0.0%	0.0%	2.8%	12.0%	24.4%	44.6%	68.0%	89.7%	99.9%
Small ($1-5MM)	0.0%	0.0%	2.8%	8.4%	18.9%	30.1%	44.2%	62.6%	93.6%
Medium ($5-10MM)	0.0%	0.0%	0.1%	0.8%	3.8%	9.1%	17.7%	40.2%	53.4%
Large ($10-50MM)	0.0%	0.0%	0.1%	0.5%	1.2%	2.4%	5.4%	10.7%	36.6%
Very Large ($50MM+)	0.0%	0.0%	0.3%	0.5%	0.8%	1.3%	2.4%	7.2%	50.6%
Total	**0.0%**	**0.0%**	**1.3%**	**7.3%**	**18.1%**	**33.9%**	**56.3%**	**80.8%**	**99.3%**
Health and Human Services Distribution (2014)									
Very Small (<$1MM)	0.0%	0.0%	0.0%	2.3%	13.9%	29.9%	57.8%	81.8%	99.9%
Small ($1–5MM)	0.0%	0.0%	0.2%	2.3%	7.2%	17.9%	22.4%	36.4%	68.8%
Medium ($5–10MM)	0.0%	0.0%	0.1%	0.5%	1.8%	4.4%	8.5%	13.8%	23.7%
Large ($10-50MM)	0.0%	0.0%	0.1%	0.3%	0.9%	1.6%	2.2%	4.0%	8.1%
Very Large ($50MM+)	0.0%	0.3%	0.5%	0.7%	0.8%	1.2%	1.7%	2.3%	5.2%
Total	**0.0%**	**0.0%**	**0.0%**	**1.1%**	**4.7%**	**14.2%**	**30.0%**	**60.2%**	**96.2%**

Exhibit 8: Philanthropy as a percentage of total nonprofit spend by size and sector

DISTRIBUTION OF PHILANTHROPY AS A PERCENTAGE OF TOTAL NONPROFIT SPEND BY SIZE AND SECTOR									
Distribution (2014)	**10%**	**20%**	**30%**	**40%**	**50%**	**60%**	**70%**	**80%**	**90%**
Philanthropy	0.0%	0.0%	5.5%	49.9%	89.5%	100.1%	109.0%	134.6%	218.6%
Environment and Animal-Related	6.7%	22.1%	35.5%	49.7%	67.3%	75.7%	88.7%	102.3%	142.2%
Religious Institutions	0.3%	16.7%	25.3%	58.4%	83.3%	96.0%	103.1%	113.5%	136.5%
Science, Technology and Social Sciences	0.0%	0.6%	4.7%	11.8%	33.1%	47.3%	73.5%	85.5%	106.1%
Other	0.0%	0.0%	0.9%	7.8%	21.9%	57.1%	85.6%	103.9%	130.3%
Community Capacity	0.0%	0.0%	3.5%	10.4%	20.3%	33.2%	53.9%	83.7%	107.9%
Youth Development	0.0%	0.9%	4.9%	12.9%	23.0%	47.8%	75.8%	95.0%	117.9%
Arts, Culture and Humanities	5.5%	17.6%	29.5%	42.4%	52.7%	68.5%	79.3%	93.3%	125.0%
Health and Human Services	0.0%	0.0%	0.0%	1.1%	5.6%	15.8%	32.5%	67.5%	103.6%
Total	**0.0%**	**0.0%**	**1.6%**	**8.6%**	**21.9%**	**41.3%**	**67.1%**	**92.8%**	**115.7%**
Distribution (2014)	**10%**	**20%**	**30%**	**40%**	**50%**	**60%**	**70%**	**80%**	**90%**
Very Small	0.0%	0.0%	3.5%	15.0%	28.9%	52.8%	79.0%	99.0%	126.9%
Small	0.0%	0.0%	3.0%	8.8%	21.5%	36.3%	54.7%	77.6%	102.9%
Medium	0.0%	0.0%	0.1%	1.0%	4.2%	11.1%	19.0%	44.2%	83.2%
Large	0.0%	0.0%	0.1%	0.5%	1.5%	2.9%	5.8%	13.0%	53.2%
Very Large	0.0%	0.0%	0.3%	0.6%	0.8%	1.4%	2.7%	11.3%	92.3%
Total	**0.0%**	**0.0%**	**1.6%**	**8.6%**	**21.9%**	**41.3%**	**67.1%**	**92.8%**	**115.7%**
Health and Human Services Distribution (2014)	**10%**	**20%**	**30%**	**40%**	**50%**	**60%**	**70%**	**80%**	**90%**
Very Small (<$1 MM)	0.0%	0.0%	0.0%	3.2%	16.2%	31.9%	62.7%	95.9%	118.9%
Small ($1–5MM)	0.0%	0.0%	0.3%	2.8%	7.7%	17.0%	27.6%	49.3%	92.9%
Medium ($5–10 MM)	0.0%	0.0%	0.1%	0.6%	2.0%	5.3%	9.0%	13.1%	23.2%
Large ($10-50 MM)	0.0%	0.0%	0.1%	0.4%	1.0%	1.6%	2.6%	4.9%	9.8%
Very Large ($50 MM+)	0.0%	0.3%	0.5%	0.7%	1.0%	1.2%	1.6%	2.6%	5.5%
Total	**0.0%**	**0.0%**	**0.0%**	**1.1%**	**5.6%**	**15.8%**	**32.5%**	**67.5%**	**103.6%**

Exhibit 9: Overhead (administrative expenses as percentage of total functional expense)

ADMINISTRATIVE EXPENSE AS A PERCENT OF TOTAL FUNCTIONAL EXPENSE									
Distribution (2014)	**10%**	**20%**	**30%**	**40%**	**50%**	**60%**	**70%**	**80%**	**90%**
Religious Institutions	0.0%	2.9%	6.5%	10.2%	13.4%	17.6%	23.0%	30.4%	51.3%
Environment and Animal-Related	1.6%	5.6%	8.4%	11.2%	14.0%	15.9%	18.3%	22.7%	30.1%
Philanthropy	0.0%	1.7%	3.7%	5.8%	8.0%	9.6%	12.1%	17.5%	27.6%
Arts, Culture and Humanities	3.3%	7.5%	10.1%	13.0%	15.2%	18.8%	22.6%	27.0%	37.9%
Science, Technology and Social Sciences	3.2%	6.6%	9.8%	13.5%	18.4%	21.8%	27.1%	32.9%	43.6%
Other	0.0%	1.9%	4.2%	7.2%	10.9%	14.0%	18.9%	25.3%	63.9%
Youth Development	0.0%	1.6%	3.9%	6.2%	8.7%	11.0%	14.9%	19.3%	30.4%
Community Capacity	0.0%	2.2%	4.7%	6.8%	9.4%	12.8%	16.4%	22.5%	39.6%
Health and Human Services	1.1%	4.6%	7.0%	9.3%	11.4%	13.7%	16.4%	20.5%	27.9%
Total	**0.0%**	**3.0%**	**5.9%**	**8.5%**	**11.1%**	**14.1%**	**17.6%**	**23.4%**	**35.6%**
Distribution (2014)	**10.0%**	**20.0%**	**30.0%**	**40.0%**	**50.0%**	**60.0%**	**70.0%**	**80.0%**	**90.0%**
Very Small (<$1 MM)	0.0%	2.2%	5.0%	7.8%	11.0%	14.8	19.3%	25.8%	41.1%
Small ($1–5MM)	1.9%	5.2%	7.3%	9.5%	11.6%	13.5%	16.1%	19.6%	26.3%
Medium ($5–10 MM)	1.2%	5.0%	7.5%	9.9%	11.1%	13.2%	15.9%	19.4%	27.7%
Large ($10-50 MM)	5.2%	7.0%	9.1%	10.3%	11.6%	13.5%	15.7%	18.6%	24.4%
Very Large ($50 MM+)	0.0%	2.7%	4.5%	6.0%	7.7%	8.8%	10.5%	13.3%	15.8%
Total	**0.0%**	**3.0%**	**5.9%**	**8.5%**	**11.1%**	**14.1%**	**17.6%**	**23.4%**	**35.6%**
Distribution (2014)	**10.0%**	**20.0%**	**30.0%**	**40.0%**	**50.0%**	**60.0%**	**70.0%**	**80.0%**	**90.0%**
2010	1.0%	4.3%	6.8%	9.2%	11.4%	14.1%	16.9%	22.2%	31.0%
2011	0.0%	2.9%	5.6%	8.5%	11.1%	13.8%	17.6%	23.2%	34.8%
2012	0.0%	2.8%	5.8%	8.4%	10.9%	13.8%	17.9%	23.2%	36.1%
2013	0.0%	3.0%	6.1%	8.8%	11.1%	13.8%	17.5%	23.0%	36.3%
2014	0.0%	3.0%	5.9%	8.5%	11.1%	14.1%	17.6%	23.4%	35.6%

ABOUT THE AUTHORS

Oliver Wyman is a global management consulting firm, and part of the Marsh & McLennan Companies (MMC), a global professional services network with brands and affiliates in more than 100 countries. Oliver Wyman's management consulting business has more than 4,000 consultants working out of offices in over 50 cities, spread across some 26 countries. Oliver Wyman Group also includes NERA Economic Consulting and the brand and identity consultancy Lippincott.

GuideStar is the world's leading provider of information about the nonprofit sector. GuideStar is a 501(c)(3) public charity that collects, organizes, and presents nonprofit data, including 990 tax filing data as well as additional information directly sourced from nonprofits, in an easy-to-understand, searchable, and analyzable format. The organization seeks to disseminate nonprofit information to a broad audience at no costs, as a public service.

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ABOUT THIS REPORT

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The report draws on SeaChange's experience and Oliver Wyman's 30+ years of experience advising the largest global financial institutions and regulators with respect to risk management; a 2016 rigorous analysis of the most comprehensive data set on the financial performance of New York's and Philadelphia nonprofits provided by GuideStar, the largest source of information on nonprofit organizations; in-depth interviews with more than 20 executive directors, board members, and funders involved with nonprofits in distress; and discussions with the Human Services Council and the Center for an Urban Future, both of which have undertaken related projects to understand and improve the financial health of the nonprofit community

We wish to thank everyone who participated in these interviews and discussions, as well as those people who provided feedback on earlier drafts of the report. This work is motivated by our recognition that nonprofits play a critical social role improving education, alleviating poverty, providing economic opportunity, supporting our healthcare system, sustaining the arts -- their health is vital to us all. We hope to have contributed to the important discussion about how to mitigate the likelihood of acute financial distress for nonprofits of any size or sector. All are indebted to nonprofit board members who take seriously their duties of care, obedience, and loyalty to govern their organizations well, striving to maximize the good they do while managing the risks they face. We hope that this report will prove useful to at least a few of them.

Oliver Wyman is a global leader in management consulting that combines deep industry knowledge with specialized expertise in strategy, operations, risk management, and organization transformation.

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