NONPROFIT OVERHEAD COST PROJECT

FACTS AND PERSPECTIVES BRIEF NO. 1

CENTER ON NONPROFITS AND PHILANTHROPY, URBAN INSTITUTE
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What We Know About Overhead Costs in the Nonprofit Sector

Let's begin with several surprising facts: 37 percent of nonprofit organizations with private contributions of $50,000 or more reported no fundraising or special-event costs on their 2000 Internal Revenue Service (IRS) Form 990, the publicly available return most nonprofits are required to file annually. Nearly 13 percent of operating public charities reported spending nothing for management and general expenses, implying that they spent all of their funds on program or fundraising activities. Finally, for those organizations reporting fundraising or special-event costs on their 990, more than one-quarter received more than $15 for every dollar spent on fundraising while another quarter of the organizations obtained less than $2 for each fundraising dollar. (The median level was $5.40.)

What is going on here? The Nonprofit Fundraising and Administrative Cost Project, a joint initiative of the Center on Nonprofits and Philanthropy at the Urban Institute and the Center on Philanthropy at Indiana University, is finding out. The goal of the project is to untangle some of the mysteries behind these numbers and to improve the quality of reporting where problems are found. This brief reports on these and other findings from the project's analyses of Form 990 data and more than 1,500 responses to a 2002 survey of randomly selected nonprofits.

Why Zero Costs?

There are some plausible reasons why an organization might have zero fundraising costs. These include:

- reliance on volunteer or board fundraising, or a handful of large contributions or private grants;
- use of special events (these expenses are reported on the 990 but are not generally counted as fundraising expenses since they do not appear in its fundraising section); and
- dependence on related organizations, such as a United Way or "Friends of" group.

The failure of many organizations to track or effectively allocate staff time to different functions may contribute to the low reporting of fundraising costs. For example, only half of the

Reported Fundraising Expenses for Organizations Receiving Direct Private Contributions

Level of private contributions	Number of organizations	% reporting fundraising expenses	% reporting special-event expenses	% reporting no fundraising or special-event expenses
Less than $50,000	52,596	23.8	28.4	55.5
$50,000 or more	74,360	54.1	26.5	37.0
$50,000–99,999	18,088	40.3	27.1	45.6
$100,000–249,999	23,883	48.6	24.5	41.8
$250,000–1 mil.	20,659	61.5	27.2	32.1
$1 mil.–5 mil.	8,986	71.8	28.9	24.4
$5 mil. or more	2,744	80.0	26.4	18.2
Total	**126,956**	**41.6**	**27.3**	**44.7**

Source: Urban Institute analysis of fiscal year 2000 IRS Form 990 data.
Note: Only organizations filing an IRS Form 990 (not the 990-EZ) for FY 2000 and reporting direct private contributions ("direct public support" on the 990) greater than zero are included in this table. Row percentages will not add to 100% because many organizations report both fundraising expenses and special-event expenses.

organizations reporting costs for key employees on the 990 distributed these costs among various activities, as IRS instructions specify. Anecdotal evidence suggests, however, that most executive directors are involved in more than one functional area, and the survey results confirm this. Only 24 percent of survey respondents reported that the executive director spent all of his or her time in only one functional area.

How Is Money Raised?

Nearly three-quarters of the organizations used volunteers (including board members) to help with fundraising, according to the survey. However, the overall share of funds raised by volunteers was only 11 percent. A surprisingly small proportion of organizations had full-time fundraising staff. Of those organizations receiving $50,000 to $250,000 in grants and contributions, only 28 percent had full-time staff. Even for those receiving $250,000 to $1 million, only 45 percent had full-time staff.

Did nonprofits rely instead on consultants for fundraising? Apparently not. Only 15 percent reported using consultants, ranging from 7 percent of organizations raising less than $50,000 to 25 percent of those raising more than $1 million.

Many donors think that direct mail and telephone solicitation are preferred fundraising techniques. The survey shows this is only partially true. It asked about 14 different types of tactics, ranging from e-mail and web-based solicitation to planned giving and federated fundraising. Slightly more than half of the organizations said they solicited grants from foundations, held special events, or used direct mail. Telephone solicitation was near the bottom of the list with less than 12 percent of the nonprofits using this technique. The only more unpopular tactics were e-mail and door-to-door solicitations.

One might think that most organizations, especially those using a variety of fundraising tactics, would keep careful track of their fundraising revenue and expenses for each tactic in order to identify emerging trends, fine-tune their efforts, and plan for the future. Wrong! While nearly 90 percent of those surveyed used more than one tactic, only two-thirds used computer software to track fundraising revenue. Of those, more than 40 percent used only a spreadsheet. Only 56 percent tracked revenue by each fundraising method.

Reporting on expenses by fundraising method fell short for the majority of organizations, with many appearing to exclude staff time or to provide otherwise implausible numbers. This finding is consistent with the weak state of expense tracking. The survey found that slightly less than half reported tracking invoices or bills by fundraising tactic, and a mere 6 percent did the same for staff time—a major cost for many fundraising methods.

Policy Implications

Underreporting of fundraising expenses is a major concern in the nonprofit sector. While there are plausible reasons why some organizations are reporting no fundraising costs—all fundraising is done by volunteers, for example—the magnitude of the contributions and the large percentage of organizations reporting no expenses suggest such explanations are inadequate.

What can policymakers do to address the underreporting problem? First, foundations, management support organizations, and nonprofit associations can encourage nonprofits to accurately report their expenses and can help make resources available to do so, such as time-tracking software or job cost modules for accounting systems.

Second, state societies of certified public accountants can encourage their members to more carefully scrutinize the allocation and assignment of costs among different programs and functions. Greater attention from the American Institute of Certified Public Accountants and the Financial Accounting Standards Board would also help.

Finally, the IRS and state charity offices can increase their monitoring of these items. On the front end, these agencies may be able to strengthen their warnings about the importance of accurately reporting these expenses; on the back end, they could request further information or send warnings to organizations reporting no fundraising expenses but substantial direct contributions.

The cost of implementing these measures is unclear, but some aspects can be mitigated with expanded use of electronic filing. The payback in increased public confidence in the nonprofit sector, however, would be immeasurable.

Further Details

The project's lead researchers are Mark A. Hager and Thomas Pollak (Center on Nonprofits and Philanthropy, Urban Institute) and Patrick H. Rooney (Center on Philanthropy, Indiana University). For more on the project, visit www.coststudy.org or call (202) 261-5709 (Urban Institute) or (317) 236-4912 (Indiana University).

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