CONNECTING DOLLARS TO OUTCOMES

How to Measure Outcomes That Deliver Mission Impact in Nonprofits

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Introduction

When a 7.0 earthquake flattened Haiti in 2010, millions of donors rushed to an iconic humanitarian nonprofit to help. Contributions climbed to half a billion dollars in one of the most successful online fundraising campaigns ever. But five years later, only six homes had been rebuilt.

Although the organization continued to defend its disaster relief efforts, it couldn't provide a public summary of how its donations had been spent. Nor could it ever. Investigative reports showed that this international nonprofit had outsourced Haitian projects to local affiliates and lacked the accounting mechanisms to connect the dollars it raised to outcomes achieved regionally. While it's possible that the charity had indeed rebuilt entire Haitian villages, it couldn't prove it, leaving its public reputation in shambles while it revised its accounting and reporting structures to ensure that future projects were transparent and accountable.

Stories like these make donors distrust nonprofits and nonprofit executives squirm. Charity leaders know how hard it is to convey a mission's impact to supporters. Doing so is made more difficult by confusing nonprofit accounting regulations and a philanthropic culture that hamstrings them from fully delivering, much less evaluating their programs.

Peter Orza, the former director of the federal Office of Management and Budget, echoes this common funder sentiment perfectly: "Public funders—and eventually private funders as well—will migrate away from organizations with stirring stories alone toward well-managed organizations that can also demonstrate meaningful, lasting impact."

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Chapter **1**

HOW DO WE MEASURE IMPACT?

"I have heard people say nonprofits should be run 'more like businesses' and be accountable in the same way for-profits are. But for-profits report income, not outcomes. Every nonprofit leader knows exactly how much money he or she raised and spent. That's easy. Which companies report outcomes? Does Microsoft report how productivity increased with its software? Does 24 Hour Fitness report on how much healthier its customers are? McKinsey on how much better its clients perform?...But nonprofits have two customers: recipients and funders. Our recipients don't pay for their services, so demand alone doesn't prove value creation."[1] **Peter Fortenbaugh,** ED Boys and Girls Club of Peninsula

Yet how do nonprofits adequately measure impact when they're attempting to help solve complicated issues—like global climate change—that are influenced by civic, individual and corporate behavior well beyond the control of just one organization? And who determines the criteria of a well-managed nonprofit?

In the last decade, watchdog agencies like Charity Navigator have introduced various metrics of nonprofit effectiveness, including the overhead ratio, which uses low overhead as a benchmark for mission effectiveness. And yet, even Charity Navigator has begun questioning this metric—the agency partnered with BB Giving Alliance and Candid in 2013 to publish The Overhead Myth*, a public mea culpa to sector pushback popularized by charity leader Dan Palatto in his seminal TED talk The Way we Think About Charity is Dead Wrong.

As early as 2009, Stanford University researchers Anne Groggins Gregory and Don Howard published "The Nonprofit Starvation Cycle"*, espousing their findings that organizations that build robust infrastructure are more likely to succeed than those that don't. While the notion of overhead investment may run counter to traditional philanthropic opinions, a growing number of capacity building organizations like the Nonprofit Finance Fund are embracing full-cost funding and partnering with grantmakers to demonstrate that philanthropic support for

[1] https://ssir.org/articles/entry/chasing_the_holy_grail_of_outcomes
* New term to you? Check our 'Terms to Know' on page 15 & 16

“Funders need to acknowledge outcomes that may be attributable to more than one organization as in most instances no single organization can address the needs of any sector. This will foster collaboration over competition.” **Nonprofit Survey Participant**

overhead spending is not only plausible it’s urgently needed.

To kick off our educational series “Mastering and Measuring Mission Impact,” NetSuite approached 353 nonprofit executives to ask whether and how they evaluate mission effectiveness. We asked if they were familiar with logic models and whether they’re using outcomes measurements to determine the impact of their programs? We wanted to know if they were aware of Charity Navigator metrics and whether they used them? And we wanted to determine whether they correlate programs to financial metrics to create dollars-to-outcome transparency?

To frame our survey participant responses, I we must first explore the following topics:

Outcomes Measurement
Outcomes measurement is an approach to assess the social impact a nonprofit creates. Nonprofit researcher Robert M. Penna says that the charity sector for most of its history has not had to prove its impact on the issue area for which the organization was created. Most nonprofits have focused on *what they are doing, not how they have impacted change.*

In his book “Braided Threads,” Penna states that nonprofits are unable to measure impact for two primary reasons:

- Lack of definition. The target problems, actual programmatic interventions, expected outcomes and desired impacts have not been sufficiently defined to be *measurable*.
- Lack of clear program results tied to resource expenditure. Expenditure of resources such as time, people and money have not been linked to outcomes.

Logic Models to Build and Measure Change
Program delivery for nonprofit organizations is the heart of the sector: Foodbanks deliver canned goods to food-insecure communities; domestic violence shelters provide beds to battered women; environmental organizations advocate for green energy. Without programs, the nonprofit sector has no meaning.

Formal evaluation of program delivery has actually been integral to demonstrating outcomes since the mid-70s when the Kellogg Foundation began to develop methodologies with the United Way to fund, monitor and evaluate its programs. Logic Models and Theories of Change describe two common

* New term to you? Check our ‘Terms to Know’ on page 15 & 16

methodologies used to create programs and measure their impact. Program evaluation staff uses Logic Models, but financial evaluation sits with the finance office. Meanwhile, watchdog agencies have created an entirely different set of criteria for success.

What Does that Cost You? The Accounting Rules that Govern and Constrain Nonprofits

Nonprofits are bound by Financial Accounting Standards Board (FASB) regulations to categorize each donation based on donor intent (restriction) and allocate each expense as either an administrative, fundraising or program cost (functional expense). These two simple accounting rules have a fundamental, far-reaching and cascading impact on the nonprofit sector. The inability of the humanitarian organization to articulate its Haitian disaster relief effort boils down to an inadequate accounting of source and use of funds—in other words, restriction and expense allocation.

Compliance as Controversy: Restrictions* and Functional Expense* Allocations

Fundraising operation and accounting staff must ensure that they solicit and earmark each contribution as either for general operating costs (without donor restrictions) or with donor restrictions. For example, if a fundraiser creates a giving campaign for Haitian relief,

* New term to you? Check our 'Terms to Know' on page 15 & 16

“Effective outcomes measurement can help us push back against institutional funders who want to restrict funding to direct program expenses as a way to ensure their dollars are being spent effectively. By better communicating our impact, we create trust and are better positioned to request general operating support.” **Nonprofit Survey Participant**

each dollar contributed must be tagged as such and cannot be comingled with general operating funds.

Conversely, every expense must be allocated into fundraising, programmatic and operating buckets. Because many expenses span all three categories (indirect costs), finance staff creates allocation schedules that divide office supplies, human resources and other expenses across functional expense categories—a laborious, time-consuming and inexact process. Data from these expense allocations are reported on nonprofit 990s and used by charity watchdog agencies to calculate program, administrative and fundraising efficiency. Increasingly, finance leaders are critical of the time spent on functional expense allocation and the harsh judgement heaped on nonprofits when money is spent on general operations or infrastructure.

Nonprofit Finance Fund Director, Claire Knowlton, states: “The reporting of functional expenses exacerbates the myth that, somehow, nonprofits should be able to operate programs without an administrative structure to manage, measure and execute. It implies that, by some as-yet-unknown magic, nonprofits should be able to achieve their mission without dedicated and systematic fundraising efforts to pay for it. The attempt to segregate interwoven and complementary expenses according to the function they serve is an exercise in futility. The truth is, all resources spent by a nonprofit are spent in order to successfully deliver on programs (with obvious exceptions made in cases of fraud). Certainly, not all spending in a nonprofit is efficient; but functional expenses tell us nothing about efficiency.”

What’s often missing in headlines about nonprofit spending is the complex accounting regulations that constrain nonprofits from spending money where it’s most needed; the reality that functional expense allocations, even when prudently applied, are unavoidably subjective; and the negative public opinion of overhead that makes nonprofits hesitate to report on full costs, thus creating a cycle of underfunded and destabilized programs.

Chapter **2**

SURVEY DEMOGRAPHICS

What does it mean to measure change?

NetSuite approached 353 nonprofit executives to ask if and how they evaluate mission impact. Are they using outcomes measurements to determine program effectiveness? Do they use Charity Navigator metrics? What works and doesn't when evaluating impact?

TOP 4 CONCERNS

What keeps the CFO up at night?

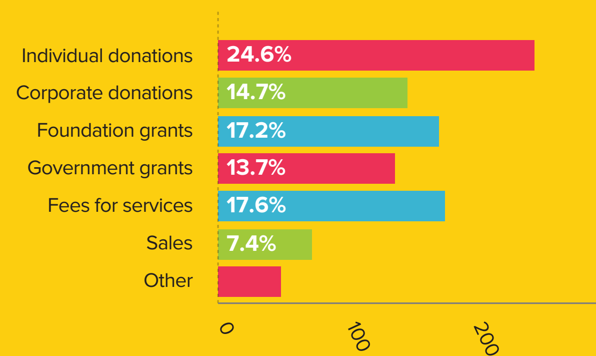
Having enough money to keep the lights on is the overarching concern for nonprofit leaders which impacts all downstream operations.

- **31%** Financial Stability
- **29%** Staff Turnover
- **27%** Donor Retention
- **27%** Programs Outpace Financial Support

FUNDING SOURCES

One person makes a difference

Individual contributions still make up the lionshare of funding for nonprofits, followed by fees for services, then foundation giving.

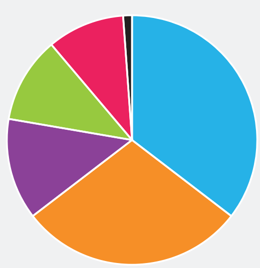


BUDGET SIZE

Stewardship from $1 Million to $5 Billion

Roughly 60% of nonprofit executives led organizations of $5 million and below. Roughly 40% led larger organizations of $10 million to $5.1 billion dollars.

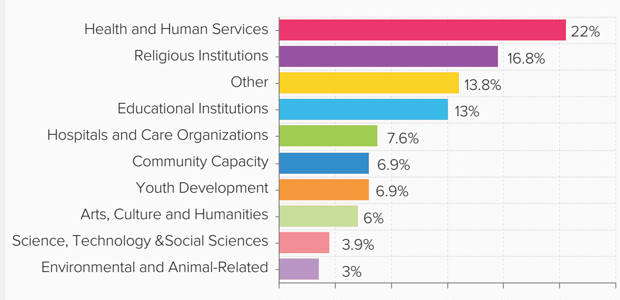
- $1 million **35.4%**
- $1 million - $5 million **29.1%**
- $5.1 million - $10 million **13.1%**
- $10.1 million- $50 million **11.1%**
- $50.1 million- $5 billion **10.0%**
- $5.1 billion **1.1%**



MISSION

Who do you serve?

Health and Human Services leading the pack, followed by religious and educational institutions.



Chapter **3**

SOLUTIONS

"It is the difficulty in measuring outcomes that makes it imperative to do so and to work on better and more nuanced metrics of the efficacy and outreach of programs." **Nonprofit Survey Participant**

Movers. Shakers. Policy Makers.
A growing number of grant makers, nonprofit executives, watchdog agencies and technology companies are working together to create new technology, measurement tools and funding models to address understanding the infrastructure needs of nonprofits.

The following technology trends will be the hallmark of the next generation of technology.

1. Dollars to Outcomes
   Finance, program and fundraising teams are unique functions within a nonprofit with specialized business processes and separate databases. When a funder is approached for a grant, however, all three functions must provide data that the funder uses to assess risk and worthiness. For mission delivery metrics, technology must be able connect the dots between fundraising, finance and program metrics, which means integration points between the data. Technology companies are responding by collaborating with nonprofits and grant makers to build unified datasets and data models to trace dollars to program results.

2. Real Needs, Real Impact
   Our survey revealed that the three primary pain points for nonprofit decision makers are financial stability, staff attrition and donor retention. Technology companies and funders can assist by collaborating to donate technology to nonprofits and build mission impact with pro bono services and capacity building resources, such as technology workforce development for underserved communities.

3. Encourage Transparency for Full Cost for Nonprofits and Funders
   One leading lender and capacity builder, the Nonprofit Finance Fund, is on a mission to partner with grant makers, lenders and funders to build transparency and systems to report full costs. By reinventing the way philanthropic organizations measure the true cost of infrastructure, donors will have full cost accounting and nonprofits will have the general operating support they need to deliver their missions.

"Nonprofits have a responsibility to their boards, founders, community, etc. to measure and communicate outcomes. How do you know you are making a difference if there is no outcome measurement?" **Nonprofit Survey Participant**

4. Build a Technology, Funder, Nonprofit, Program Beneficiary Ecosystem
   Smart phones, cloud platforms, digital payment tools, social media and video streaming have upended business-as-usual, and the nonprofit sector is no exception. Together, an ecosystem of funders, program beneficiaries, nonprofits and technology companies can usher in a new era of unprecedented, positive social change.

Hundreds of governments, disaster relief nonprofits and individuals went to Haiti in humanitarian response to the 2010 earthquake, and an iconic charity was singled out for its tepid response to catastrophic destruction. In the nine years since that disaster, it has changed its accounting methods and is using its very public challenges to drive sector awareness of the importance of transparent financial operations to demonstrate programmatic impact.

The voices of nonprofit executives we surveyed reflect important viewpoints that can shape how technology can be used to build products and services to help nonprofits master and measure mission impact. As we move toward a world of social collaboration, these survey results show us how to shift the conversation from judging nonprofits for their perceived inadequacies to transforming their operations to achieve results.

Our Recommendations

Becoming an outcomes measurement champion within your nonprofit is dependent on your role. Let's explore that briefly.

Program Managers: Educate Your Organization on Program Evaluation Principles

Because finance staff are generally focused on numbers only, they are likely to be unfamiliar with program logic models—the graphic representations of the linkages between program activities and the changes those activities will produce. Logic models, or "theories of change," help stakeholders such as funders, boards, program staff and executive directors understand whether there is any "logic" to your programs—whether the connections between what you do and what you hope to achieve make sense. Such models provide greater clarity about your mission and tell the story of your program.

To educate nonprofit teams on current outcomes measurement approaches, consider registering for the online and in-person trainings at Candid-GuideStar and the Nonprofit Quarterly. These teach nonprofit staff how to identify target problems, propose programmatic interventions, and define the overarching outcomes and desired impacts of their organizations.

Your organization may also want to explore the documentaries produced by nonprofit outcomes expert Kate Robinson: "Failing Forward – On the Road to Social Impact" and "Saving Philanthropy – Resources to Results". She has led a national advisory board of high-performing, nonprofit organizations and conducted extensive research on evaluation strategies.

Last, if you need cost-effective consulting expertise, consider Capacity Catalyst, an organization that provides Ph.D candidate program evaluators to nonprofits that need assistance in developing program logic models.

Finance Managers: Review and Revise Your Financial Transaction Data Structures

To correlate program activities with revenue and expenses, the appropriate data structure needs to be in place. Your accounting system must be set up to tag expense and revenue transactions with the appropriate dimensions at the line level: revenue type (donation, pledge, fee for service), restriction status (with or without donor restrictions) and fund/program.

Nonprofit outcomes KPIs are based on aggregate transactions using the source (revenue type, restriction) and use of funds (fund/program). These dimensions (also called segments or tags) form the basis of modern accounting structure, replacing the long accounting code strings that were used in the past. For nonprofits, this is a critical feature in outcomes measurement because the aggregation of revenue and expense transaction dimensions are what allows visibility into program sustainability and financial transparency reports.

Executives: What's on the Horizon

As nonprofits get better at identifying their programmatic and financial outcomes, the next stage is to correlate program service delivery to financial data. Our survey results show that many nonprofits aspire to do this, but don't yet have the infrastructure in place to implement it. NTEN, the nonprofit technology membership hub, is a great resource for assistance because it has resources to help nonprofit IT staff understand the basics of nonprofit data architecture, the key to envisioning a program and financial technology solution.

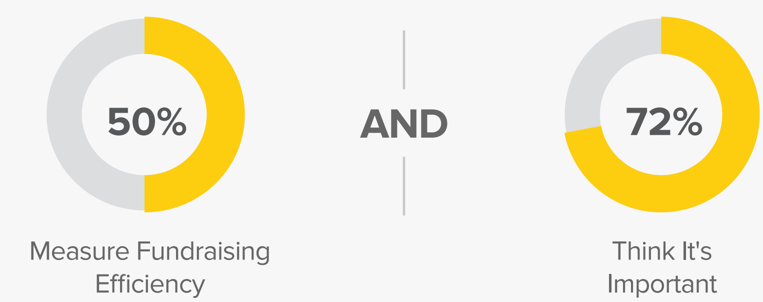
FINANCIAL EFFICIENCY METRICS

YES, WE MEASURE VS. YES, IT'S IMPORTANT

ADMINISTRATIVE EFFICIENCY

PROGRAM EFFICIENCY

FUNDRAISING EFFICIENCY



YES, WE MEASURE VS. YES, IT'S IMPORTANT

REVENUE GROWTH YEAR-TO-YEAR

Measure Revenue Growth Year-to-Year

Think It's Important

PROGRAM EXPENSE GROWTH YEAR-TO-YEAR

Measure Program Expense Growth Year-to-Year

Think It's Important

WORKING CAPITAL - DAYS CASH ON HAND

Measure Days Cash on Hand

Think It's Important

Chapter **5**

WHAT WE'RE HEARING

WE WANT TO MEASURE BETTER VALUES AND CHALLENGES

OUT OF 353 EXECUTIVES:

Obstacles to Measurement

95 Data Silos

130 No Human Resources

105 No Tracking System

33% Use a Logic Model

71% Consider Outcomes Measurement Important

20% Believe they are Very Effective at Demonstrating Outcomes

76% Say that Measuring Outcomes is a Priority for 2019

WHAT EXECUTIVES SAY ABOUT OUTCOMES MEASUREMENT

69% Rewards Large, Well Resourced Nonprofits

60% Minimizes Complexity of Social Issues

45% Focuses on the Short Term

55% Measure beyond Charity Navigator Metrics

WE WANT TO MEASURE BETTER ABOVE AND BEYOND

WHAT GETS MEASURED BEYOND FINANCES

Beyond Financial Metrics, Programs Matter

55%

CFOs track program activities and outcomes

- 75% Outcomes of Programs
- 64% Number of Programs
- 47% Dollar Value of Services
- 46% Number of Volunteer Hours

HOW PROGRAM VALUE IS COMMUNICATED

- 65% Annual Reports
- 54% Email Communication
- 34% One-on-One Meetings
- 32% Grant Reports

LIMITATIONS OF ONLY MEASURING CHARITY NAVIGATOR METRICS

62%

Do not fully communicate the impact of programs

33%

Do not reflect investments made in growing the organization

AT A GLANCE: TERMS TO KNOW

TERM	DEFINITION
Allocation	The process by which contributions and expenses are divvied up between program, fundraising or administrative categories.
Financial Accounting Standards Board (FASB)	Established in 1973, the Financial Accounting Standards Board (FASB) is the independent, private-sector, not-for-profit organization based in Norwalk, Connecticut, that establishes financial accounting and reporting standards for public and private companies and not-for-profit organizations that follow Generally Accepted Accounting Principles (GAAP).
Full Operational Costs	The Nonprofit Finance Fund offers the guiding equation of full costs as the sum of: • Day-to-day operating expenses • Unfunded expenses (e.g., underpaid staff) • Working capital (cash for day-to-day needs) • Reserves (e.g., savings, rainy day fund) • Fixed asset/technology additions (money to purchase a building or new computers) • Debt • Change capital (e.g., resources to adapt, grow and/or expand)
Functional Expense	All nonprofit expenses must be tagged by function—administrative, fundraising or program.
Indirect Costs	Indirect costs are expenses used for a common or joint purpose benefitting more than a single cost objective, for example when an employee's time is spent on multiple projects or when an office supply is used for multiple programs.
Logic Model	A method by which a nonprofit can determine the effectiveness of its programs tracking inputs, activities, outputs, outcomes and impact. Logic models vary for nonprofits depending on their issue area.
Outcomes Measurement	Outcomes measurement is an approach to nonprofit activity that looks to create, measure and assess the social impact created by a nonprofit. Measuring outcomes is a shift from measuring nonprofit program activity toward the results produced by program activity.
Overhead	Expenses such as rent, employee salaries and utilities, commonly presented as management and general and fundraising functions on Form 990s. Also known as general operating or operating costs.

TERM	DEFINITION
Overhead Myth	Assumption that low nonprofit overhead determines the effectiveness of a nonprofit.
Overhead Ratio	Amount of money a nonprofit spends on its programs versus money spent on overhead costs – a hotly contested ratio. Refers to Administrative Efficiency (lower the better) and Program Efficiency (higher the better).
Restriction	Refers to restriction on a donation as stipulated by the donor (such as giving to a specific program). Also called a "use" restriction, or a "time" restriction such as a grant or a pledge which will be promised in its entirety but received on a set schedule.
Starvation Cycle	A term coined by researchers Ann Goggins Gregory and Don Howard to describe the vicious cycle created when nonprofits underreport administrative costs to secure funding and then run into deficits, creating the need for more funding.
The Overhead Myth Campaign	Open letter from GuideStar, Charity Navigator and the Better Business Bureau Wise Giving denouncing the 'overhead ratio' as a valid indicator of nonprofit performance.
Watchdog Agency	An agency that rates nonprofit effectiveness such as Guidestar (now Candid), Charity Navigator and the Better Business Bureau Wise Giving Alliance.

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