POINT OF VIEW

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UNDERSTANDING OVERHEAD: A GOVERNANCE CHALLENGE FOR NONPROFIT TRUSTEES

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OVERHEAD: WHY CARE?

Overhead is a vexing issue for nonprofits and a potential source of financial risk. So trustees serious about risk management must understand the particular risks associated with overhead. They should know what their organization's overhead is comprised of and appreciate the complexity and challenge of defining and calculating it. They should be curious about how they compare to other similar organizations. But they should be wary of peer comparisons because the lack of standard definitions makes it nearly impossible to make apples-to-apples comparisons using publicly available data. They should work collaboratively with management to explore the various strategies available to fund overhead sustainably. And they should be aware of the contentious context in which this critical issue is being addressed by public and private funders.

We hope that this report, intended as a companion piece to our earlier report, "Risk Management for Nonprofits", will help trustees better understand this important issue and thereby be more effective in exercising their oversight and governance duties.

OVERHEAD: WHAT IS IT?

Nonprofit accounting – both audited financial statements and the IRS Form 990 – requires that nonprofits divide their expenses into three categories: program, administrative and fundraising. Administrative includes accounting, human resources, board expenses, management systems, etc. Fundraising includes costs incurred in the process of raising money, materials, or volunteer time. Overhead is somewhat analogous to Selling, General and Administrative ("SG&A") expense in the for-profit context, while program expenses are similar to Cost of Goods Sold ("COGs").[1]

The administrative and fundraising ratios are a nonprofit's administrative and fundraising expenses divided by its total expenses. (The overhead ratio is the sum of the two.) For most nonprofits, the majority of expenses are staff-related so the overhead ratio often reflects an estimate of the portion of total staff time associated with administrative and fundraising activities and the average salary of those staff relative to the workforce of the organization as a whole.[2]

A note on language: The word "overhead" has a slightly pejorative connotation in the nonprofit sector and is rarely a helpful concept since it includes two very different things: administrative expenses (often called "indirect expenses") and fundraising expenses. To the extent possible, we separate these two in this report.

The allocation of expenses into program, administrative, and fundraising is far from clear-cut. Not only are these categories somewhat arbitrary but they are defined in inconsistent ways depending on the contract or grant, and interpreted in different ways by different nonprofits.[3] Discussions of indirect expenses – by far the largest component of overhead – are further complicated since trustees and staff often fail to distinguish between financial accounting (i.e. how indirect expenses are characterized in the audit), management accounting (i.e. what they think are *really* indirect expenses) and contract accounting (i.e. what contracts require be treated as indirect expense).[4]

Even the recently released OMB Uniform Guidance on Indirect Costs does not provide definitive answers regarding what are, or are not, eligible indirect expenses. [5] For example,

[1] This is a stretched analogy though the most nonprofit-like publicly-traded companies appear to use SG&A and COGs in this way. See Maximus' 2015 10K filing: http://investor.maximus.com/sec-filings.

[2] For example, if 10% of staff time is allocated to overhead, and those staff make 1.3x the average salary in the organization, the overhead ratio is likely to be close to 10%x1.3=13%. In small nonprofits, many staff are often involved in both programmatic and overhead functions.

[3] An example of this would be a program run in a sole-purpose facility where the government contract allows rent to be counted as a program expense but characterizes repairs and maintenance as indirect.

[4] Most nonprofits only keep one set of books but they sometimes discuss overhead as if they keep three.

[5] https://www.councilofnonprofits.org/trends-policy-issues/new-omb-guidance-indirect-costs-what-it-does-and-why-it-matters.

dividing rent or facility costs into administrative and program expenses is very difficult from a management and audit perspective, and highly dependent on the idiosyncratic nature of how and where programs are operated.[6] Some nonprofits have taken the position, in their financial reporting and public advocacy, that almost all expenses incurred by an organization are in fact programmatic in nature and should be considered direct program costs. Although far from perfect, the new OMB guidance is an important first step in getting indirect costs consistently defined and appropriately funded. New York City and New York State are also taking steps to address inconsistent definitions and inadequate funding but the timeline on these efforts is unclear.[7]

The bottom line is that trustees should remember that accurate, reliable comparisons of overhead between organizations are difficult and that overhead ratios can be manipulated by organizations keen to present themselves in a favorable light.

WHY DOES OVERHEAD MATTER?

Despite the challenge of defining or measuring it accurately, overhead matters a lot. Many donors favor nonprofits that minimize spending on overhead versus program expenses. Most government contracts and restricted grants explicitly require that indirect expenses be tightly limited and controlled. And while every contract and grant is different, many indirect expense reimbursement rates do not cover the minimum indirect expenses associated with the program being funded. Yet functions such as IT, finance and HR are critical to the long-term health and sustainability of every nonprofit.

The debate about overhead often reflects a more fundamental clash between two very different views of what nonprofits are. For government and some foundations, nonprofits are delivery vehicles for the programs they favor at the moment. Vehicles whose associated organizational costs (i.e. overhead) are at best necessary evils. By contrast, nonprofits see themselves as long-run going concerns with obvious organizational needs (management, technology, research & development, office space, finance and accounting, staff development) and assets (human, financial and reputational) over and above the programs which a particular set of government agencies and restricted donors happen to be funding at any given moment.

The good news is that nonprofit leaders are working hard to educate donors to place less emphasis on overhead, to mandate that government contracts fully fund the associated indirect expenses, and to encourage foundations to be more generous with unrestricted ”general operating” support.[8]

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[6] This “market” variable is rarely part of the calculation made by funders and often creates distortion in the administrative ratio.

[7] http://www1.nyc.gov/office-of-the-mayor/news/779-16/mayor-de-blasio-new-nonprofit-resiliency-committee.

[8] See the www.indirectmyth.com, www.realcostproject.org, http://www.councilofnonprofits.org/trends-policy-issues/new-omb-guidance-indirect-costs-what-it-does-and-why-it-matters, http://www.geofunders.org/smarter-grantmaking/field-study/resilience

The bad news is that these efforts, even if ultimately successful, will take time. So for the foreseeable future, organizations must continue to cobble together a varied portfolio of funding – high-indirect rate contracts, low-indirect rate contracts, restricted grants, and unrestricted general operating funds – to make ends meet. They may also be forced to constrain and reduce spending on indirect expenses even if that means cutting into critical finance, IT, research and development, HR, and other support functions. Many nonprofits also grapple with the difficult "mission" question of whether to reduce program deliverables in order to use funds to meet the indirect costs of keeping the organization afloat. However, the inflexibility of many government contracts makes this very challenging to do even for groups that want to.

But overhead can be too high as well. The overhead ratio *is* perceived by many as a proxy for "goodness".[9] Some donors *are* enticed by low overhead (or overhead that someone else is paying for).[10] In extreme cases, a high indirect ratio *can* indicate inappropriate executive compensation, over-staffing, wasteful spending, fraud, a zombie condition, or financial distress. And the overhead ratio, while imperfect, *does* provide a metric that is simple to measure and is commonly used by outsiders when looking at nonprofits.[11]

So while nonprofit leaders are right to suggest that outsiders focus less on overhead, trustees should not hesitate to give it careful consideration and scrutiny alongside the other important indicators of efficiency and effectiveness.

PATTERNS: ADMINISTRATION AND FUNDRAISING EXPENSES IN THE FORM 990

Tables 1-8 analyze the overhead of all New York City nonprofits based on the information they are required to include on the Form 990 submitted annually to the IRS.[12] Here are the highlights:

- **The median overhead ratio is 16.3% (mean: 12.8%); for one-quarter of nonprofits it's 10% or less; for one-quarter it's 24% or more**. The average

[9] Discussions of overhead are typically influenced by concerns around the appropriate level of fundraising expenses. While this is a legitimate debate, fundraising expenses represent a very small fraction (less than 10%) of total overhead for most nonprofits.

[10] See http://rady.ucsd.edu/docs/Science-2014-Gneezy-632-5.pdf for a discussion around donor preferences. The findings suggest that it may be rational for individual nonprofits to compete on the basis of "low overhead", even if that encourages a "starvation cycle" that is collectively damaging.

[11] By contrast, impact and cost effectiveness, while more important, are hard to measure and very difficult to compare across organizations despite what Social-Return-On-Investment gurus may say.

[12] 10,754 organizations (2014) from the New York MSA were included in this analysis. We removed all organizations reporting no administrative expenses (representing 10% by count, 1% by functional expense). Source: Amazon Web Services, IRS 990 Public Dataset. https://aws.amazon.com/public-data-sets/irs-990/ While Form 990 data is imperfect, it is the only large scale dataset available and we believe it is accurate enough to support our broad observations.

overhead ratio is lower than the median since larger organizations have lower overhead ratios on average.

- **The median administrative ratio is 12.8% (average: 11.4%); for one-quarter of nonprofits it's 8% or less; for one-quarter it's 19% or more.** In aggregate, administrative expenses represent 90% of total overhead expenses.

- **Administrative ratios differ very little by sector but indicate clear economies of scale.** Within every sector, organizations display a wide range of administrative ratios around relatively consistent median values between 10-12%. However, larger organizations show administrative costs that are 15-50% lower than smaller organizations relative to total expenses.

- **In aggregate, fundraising expenses represent 1.4% of total expenses and 10% of total overhead expenses.** Reported fundraising expenses are concentrated in roughly 30% of the organizations; 50% of organizations report no fundraising costs at all!

- **For organizations reporting non-zero fundraising expenses, the median fundraising ratio is 4.7% (average: 2.4%); for one-quarter of these nonprofits it's 2% or less; for one-quarter it's 9% or more.[13]** For these organizations, fundraising expenses represent 17-18% of total overhead expenses. Average fundraising expenses appear to have grown roughly 2-3% per annum for the last four years.

- **Fundraising <u>ratios</u> differ considerably by sector and scale.** Higher spending sectors (6-7% on average) include Arts & Culture, Environment and Animals, Science and Technology. Lower spending sectors (1-4%) include Health and Human Services, Hospitals, and Educational Institutions. Larger organizations also have significantly lower fundraising ratios than smaller ones.

- **Fundraising <u>efficiency</u> (fundraising expenses divided by private funds raised) varies far less by sector and not at all by size.** The median organization spends $0.17 per private dollar raised; one quarter spend $0.09 or less and one quarter spend $0.29 or more. There appears to be little difference in fundraising efficiency based on size with the smallest groups spending $0.15 and the largest spending $0.17.[14]

[13] 5,930 nonprofits reported zero fundraising: 70% of these are very small (i.e. Grassroots), 89% (by dollar value) are in Health and Human Services and Hospitals where private contributions are close to zero for many organizations.

[14] This result is consistent with the fact that amount of private philanthropy is largely fixed so many of the largest organizations are unlikely to see a return on development expenses above a certain amount.

- **In aggregate, 50-60% of overhead is directly related to staff (salary and benefits, occupancy, etc.).** This holds true for program, administrative and fundraising expenses. Most organizations are people intensive and purchase relatively few inputs from other organizations. Important non-staff costs include financial (e.g. depreciation, insurance, interest) and fees which are a surprisingly large expense item and have been growing. While some fees are for third-party services (audit, book keeping, etc.) we suspect that for smaller organizations, fees are spent on services that larger and/or more stable organizations might employ staff to provide.

Trustees must not draw high-stakes conclusions from peer comparisons based on reported overhead. Our analysis does not provide sufficient information for trustees to assess their organization's administrative or fundraising expenses and any comparison with peers based on Form 990 data is fraught with uncertainty. However, organizations that appear to be well outside the normal range – high or low – should try to understand why if only because funders are likely to ask about it. If costs appear low, is this a sign of efficiency, underinvestment or poor reporting? If costs appear high, is this an inherent feature of the program, a function of organizational structure, or something else?

TWO STRATEGIC QUESTIONS

Critics of the "overhead myth" are right to point out that an organization's level of overhead has little, if anything, to do with whether its program is effective. But an analysis of overhead – particularly administrative expenses – *can* suggest whether the program, effective or not, might be deliverable in a more efficient or sustainable way. Programs don't deliver themselves, organizations do. Sustainable, cost-effective impact requires an effective program *and* an efficient, financially stable organization to deliver it.

In developing a long-run strategy for overhead, trustees should work with management to consider two distinct questions:

1. Given our organizational boundaries how can we fund our overhead?

   - **Raise more unrestricted funding:** Dollar for dollar unrestricted funding is by far the most valuable type of funding. It is also the hardest to raise from the government or foundations.[15] To maximize unrestricted support, it's critical for trustees to give meaningfully to organizations they govern and to encourage others to do the same. Despite this, only 60% of nonprofits report 100% giving by trustees

[15] No more than 25% of foundation funding is unrestricted; much more of individual and board giving is likely in this category though data is hard to find. There are some signs that suggest government funders may offer additional flexibility in funding <u>without</u> offering additional funding. This would allow organizations to spend less on program and more on indirect though this will be a difficult choice for many nonprofits to make.

and only 26% of trustees are directly involved in fundraising from others.[16] Trustees should continuously pay attention to the ratio of (i) private, general support relative to (ii) government and other restricted funding. A reduction in this ratio over time can lead to much greater risk.

- **Optimize restricted funding:** Funding streams differ in the amount of indirect expenses that can be recovered.[17] Different organizations can incur very different marginal indirect costs for an identical program depending on how it fits with the rest of their activities. In theory, it should be possible to optimize restricted funding based on a thorough understanding of each contract (or potential contract) and how it fits together with the rest. In practice, things are more difficult. Organizations must resist the temptation to "chase fat contracts" outside their area of expertise. Becoming over-reliant on contracts that have been taken on "because of the margin" may erode the nonprofit's ability to stay on mission, and can be difficult to unwind if circumstances change.[18]

- **Achieve efficiency through organic growth:** Scale *is* associated with greater efficiency *on average*. But many nonprofits (and their trustees) underestimate the risks associated with trying to grow their way out of a funding problem. Increased scale is often accompanied by more managerial complexity. And contracts that don't cover their fully-loaded costs individually are unlikely to do so in aggregate. Furthermore, organizations generally require more private philanthropy (in absolute terms) as they grow even if they become more efficient and therefore require less as a percentage of revenue. Growth may also require increased space to conduct programs. The financial commitments required to secure this space will generally be much longer in duration than the guaranteed program income, creating a significant "mismatch" risk.

- **Achieve efficiency through process redesign:** While scale effects are real, they appear modest compared with the range of performance exhibited by organizations of the same size. So nonprofits concerned about their overhead expenses, but reluctant or unable to grow, may still be able to increase efficiency by redesigning processes, better use of technology, or outsourcing some functions. Nonprofits interested in exploring these strategies should work to recruit trustees with deep operating, technology, or business process experience.

2. Given our overhead how should we move our organizational boundaries?

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[16] See www.LeadingWithIntent.org.

[17] Nonprofits also differ considerably in how well they take advantage of all available recoveries.

[18] The unwind costs are greatest if the resources – usually staff and real estate – have become a Gordian Knot that cannot be undone or redeployed even when a program is discontinued. FEGs appears to have entered a death spiral in part because of this phenomenon.

A second approach to funding overhead more sustainably is to consider moving the organization's boundaries. Sometimes an effective program is embedded within an organization that, for whatever set of reasons, is not well positioned to deliver it efficiently or sustainably.[19] This situation might be improved through divesting/spinning-off programs, joining a management service organization, sharing space, or even entering into merger with a complementary organization.[20] These opportunities too often go underexplored, particularly by organizations that are "doing fine".

Any movement of organizational boundaries raises sensitive issues of mission alignment, organizational culture, ego, job security, the reaction of funders, etc. However, with thoughtful planning these issues can often be worked through and the resulting transaction can offer the benefits that might come from greater scale, redesigned processes, or optimized funding but at lower risk than trying to achieve these things alone. And even if the organization determines not to move its boundaries, the exploration process can leave the organization better aware of its strengths/weaknesses and the environment in which it operates.

FINAL THOUGHTS

Overhead is a dry subject. People don't join nonprofit boards to read spreadsheets or study expense allocations. Compensation and staffing levels are sensitive topics. "Merger" is sometimes a dirty word. Analysis can suppress the warm glow that drives giving and service. There are no outside financial analysts, activist shareholders, or markets for corporate control to impose organizational effectiveness and efficiency from the outside. So the commitment to make analysis part of everyday leadership and governance must come from within. We hope that this addendum will prove useful to trustees who are already committed while encouraging others to take the plunge.

[19] Many nonprofits have a natural lifecycle. Sometimes an organization that was once well positioned no longer remains so because of internal or external changes.

[20] For a good taxonomy of the possible options see: http://lapiana.org/insights-for-the-sector/insights/collaboration-and-strategic-restructuring/collaborative-map.

APPENDIX

Table 1 shows aggregate overhead expenses as a percentage of total expenses (i.e. the Overhead Ratio). In 2014, the median was 16.3%, the weighted average was 12.8%, 20% of organizations had indirect of 7.6% or less, and 20% had ratios of 30.9% or more.

Table 1: Aggregate Overhead Ratios

OVERHEAD RATIO					
Distribution	**2010**	**2011**	**2012**	**2013**	**2014**
10%	4.1%	4.1%	3.8%	3.6%	3.8%
20%	7.7%	7.7%	7.6%	7.3%	7.6%
30%	10.3%	10.5%	10.6%	10.4%	10.5%
40%	13.1%	13.3%	13.4%	13.3%	13.3%
50%	15.7%	16.0%	16.3%	16.2%	16.3%
60%	19.0%	19.3%	19.6%	19.5%	19.7%
70%	23.2%	23.8%	24.0%	23.8%	24.2%
80%	30.0%	30.5%	30.8%	30.6%	30.9%
90%	46.8%	48.2%	47.2%	47.1%	47.7%
Weighted Average	12.8%	12.5%	12.3%	12.5%	12.8%

Table 2 shows the aggregate administrative expenses as a percentage of total expenses as reported on the Form 990. In 2014, the median was 12.8%, the weighted average was 11.4%, 20% of organizations had indirect of 5.8% or less, and 20% had ratios of 25.4% or more.

Table 2: Aggregate Administrative Ratios

ADMINISTRATIVE RATIO					
Distribution	**2010**	**2011**	**2012**	**2013**	**2014**
10%	3.1%	3.1%	3.0%	2.9%	2.9%
20%	6.2%	6.1%	5.9%	5.7%	5.8%
30%	8.5%	8.5%	8.4%	8.2%	8.3%
40%	10.5%	10.6%	10.6%	10.5%	10.5%
50%	12.7%	13.0%	12.9%	12.8%	12.8%
60%	15.1%	15.4%	15.6%	15.4%	15.4%
70%	18.6%	19.0%	19.3%	19.0%	19.2%
80%	24.1%	25.0%	25.0%	24.9%	25.4%
90%	37.7%	40.7%	39.7%	40.3%	40.6%
Weighted Average	11.7%	11.3%	11.1%	11.2%	11.4%

Table 3A shows the aggregate fundraising expenses as a percentage of total expenses as reported on the Form 990. In 2014, the median was 0% as more than 50% of the organizations reported no fundraising expenses, the weighted average was 1.4%, 10% of organizations had fundraising ratios of 10.9% or more.

Table 3B shows the same information for those organizations reporting non-zero fundraising expenses. In 2014, the median was 4.7%, the weighted average was 2.4%, 20% of organizations had fundraising ratios of 1.1% or less, and 20% had ratios of 11.6% or more.

Table 3A: Aggregate Fundraising Ratios

FUNDRAISING RATIO					
Distribution	**2010**	**2011**	**2012**	**2013**	**2014**
10%	0.0%	0.0%	0.0%	0.0%	0.0%
20%	0.0%	0.0%	0.0%	0.0%	0.0%
30%	0.0%	0.0%	0.0%	0.0%	0.0%
40%	0.0%	0.0%	0.0%	0.0%	0.0%
50%	0.0%	0.0%	0.0%	0.0%	0.0%
60%	0.4%	0.3%	0.4%	0.4%	0.5%
70%	2.0%	2.1%	2.3%	2.2%	2.4%
80%	4.9%	4.9%	5.5%	5.5%	5.6%
90%	10.6%	10.5%	10.8%	10.8%	10.9%
Weighted Average	1.2%	1.2%	1.2%	1.2%	1.4%

Table 3B: Aggregate Fundraising Ratios, excluding organizations with zero fundraising expenses.

FUNDRAISING RATIO					
Distribution	**2010**	**2011**	**2012**	**2013**	**2014**
10%	0.3%	0.4%	0.5%	0.5%	0.4%
20%	0.9%	1.0%	1.2%	1.2%	1.1%
30%	1.7%	1.9%	2.1%	2.0%	2.0%
40%	2.7%	2.9%	3.2%	3.2%	3.2%
50%	4.0%	4.2%	4.7%	4.6%	4.7%
60%	6.0%	6.1%	6.4%	6.5%	6.5%
70%	8.2%	8.3%	8.7%	8.9%	8.7%
80%	11.6%	11.3%	11.7%	11.8%	11.6%
90%	19.3%	17.5%	17.9%	17.8%	16.9%
Weighted Average	2.1%	2.2%	2.3%	2.2%	2.4%

Exhibit 4 shows the Administrative Ratio by sector and then by size. For example, table 4A shows that the median Arts and Culture organization has an Administrative Ratio of 13.7% compared with 12.1% for Health and Human Services.

Table 4B shows the Administrative Ratio for organizations of different sizes. For example, the table shows that 20% of Small Safety Net organizations have Administrative Ratios of 20.1% of more; for the largest Economic Engines the corresponding figure is 15.4%

Table 4C shows the same data only for organizations in Health and Human Services.

Table 4A: Administrative Ratio by Sector

ADMINISTRATIVE RATIO									
Distribution (2014)	**10%**	**20%**	**30%**	**40%**	**50%**	**60%**	**70%**	**80%**	**90%**
Religious Institutions	1.0%	3.2%	6.2%	9.3%	12.3%	16.3%	21.3%	31.7%	71.2%
Environment and Animal-Related	3.5%	4.9%	6.6%	8.3%	10.8%	13.5%	16.7%	22.8%	34.2%
Philanthropy	0.8%	2.0%	3.4%	5.7%	8.1%	11.8%	15.5%	24.2%	44.7%
Arts, Culture & Humanities	4.7%	7.6%	9.6%	11.6%	13.7%	16.9%	20.4%	26.6%	41.1%
Science, Technology & Social Sciences	3.6%	6.4%	8.0%	9.9%	12.4%	16.1%	20.4%	26.1%	42.8%
Other	1.7%	4.6%	6.7%	8.5%	10.6%	12.9%	16.6%	22.9%	37.9%
Youth Development	1.7%	3.5%	5.3%	7.4%	9.9%	12.7%	15.7%	21.4%	34.2%
Community Capacity	4.0%	7.1%	9.7%	12.1%	14.9%	17.9%	22.0%	28.9%	49.2%
Educational Institutions	3.9%	6.8%	9.4%	11.3%	13.4%	15.8%	19.2%	23.8%	33.2%
Health & Human Services	3.3%	6.3%	8.5%	10.3%	12.1%	14.2%	17.0%	20.8%	30.3%
Hospitals & Care Organizations	3.7%	6.7%	9.4%	10.8%	13.0%	15.1%	18.1%	21.7%	37.3%

Table 4B: Administrative Ratio by Size[21]									
Distribution (2014)	**10%**	**20%**	**30%**	**40%**	**50%**	**60%**	**70%**	**80%**	**90%**
Grassroots	2.4%	5.1%	8.1%	10.9%	14.0%	17.9%	23.3%	32.7%	55.6%
Small Safety Net	3.4%	6.3%	8.4%	10.4%	12.3%	14.4%	16.8%	20.1%	27.1%
Mid Safety Net	4.7%	7.0%	8.9%	10.5%	11.6%	13.5%	15.6%	18.9%	24.1%
Large Safety Net	4.5%	7.1%	8.7%	10.0%	11.5%	12.9%	14.8%	17.2%	22.3%
Economic Engine	3.5%	6.1%	8.0%	9.6%	10.6%	11.7%	13.4%	15.4%	19.2%

[21] Nonprofit size categories are as follows by revenue: Grassroots (< $1.0 million); Small Safety Net ($1-$5 million); Mid-Safety Net ($5-$10 million); Large Safety Net ($10-$50 million); Economic Engines (>$50 million)

Table 4C: Administrative Ratio for Health & Human Services by Size

Distribution (2014)	10%	20%	30%	40%	50%	60%	70%	80%	90%
Grassroots	3.1%	5.5%	8.9%	11.3%	14.1%	17.2%	20.8%	27.3%	45.3%
Small Safety Net	3.4%	6.6%	8.2%	9.9%	11.4%	13.2%	15.2%	17.9%	22.6%
Mid Safety Net	4.5%	7.7%	9.0%	10.8%	12.0%	13.5%	15.0%	17.0%	20.5%
Large Safety Net	4.7%	6.8%	8.1%	9.3%	10.8%	11.7%	12.9%	14.5%	17.9%
Economic Engine	4.2%	6.4%	7.9%	8.6%	9.4%	10.6%	11.4%	12.8%	14.6%

Exhibit 5 shows the Fundraising Ratio by sector and then by size. For example, table 5A shows that the median Environment and Animal-related organization has a Fundraising Ratio of 6.7% compared with 3.1% for Health and Human Services.

Table 5B shows Fundraising Ratios by size. For example, 10% of the smallest grassroots organizations spend 22% or more on fundraising; the corresponding figure for the largest Economic Engines is 8.8%.

Table 5A: Fundraising ratios, organizations with zero fundraising excluded

FUNDRAISING									
Distribution (2014)	**10%**	**20%**	**30%**	**40%**	**50%**	**60%**	**70%**	**80%**	**90%**
Religious Institutions	0.7%	1.5%	2.4%	3.6%	5.3%	6.5%	8.8%	12.0%	17.8%
Environment and Animal-Related	0.6%	1.6%	3.2%	4.4%	6.7%	9.4%	11.8%	14.2%	19.2%
Philanthropy	0.8%	1.7%	3.6%	5.5%	7.4%	9.8%	12.0%	17.9%	31.9%
Arts, Culture & Humanities	1.1%	2.3%	3.7%	5.1%	6.5%	8.1%	9.3%	11.8%	15.8%
Science, Technology & Social Sciences	1.6%	2.9%	4.7%	5.9%	7.3%	8.2%	11.0%	13.2%	17.5%
Other	0.6%	1.7%	3.1%	4.4%	6.1%	8.0%	10.2%	13.8%	19.3%
Youth Development	0.7%	1.7%	3.1%	4.4%	5.8%	7.6%	10.5%	13.6%	21.2%
Community Capacity	0.7%	1.6%	2.3%	3.7%	5.3%	7.0%	8.8%	11.6%	16.3%
Educational Institutions	0.3%	0.7%	1.2%	2.0%	2.7%	4.0%	5.8%	9.4%	14.9%
Health & Human Services	0.3%	0.7%	1.3%	2.0%	3.1%	4.9%	7.3%	10.2%	15.7%
Hospitals & Care Organizations	0.1%	0.3%	0.9%	1.6%	3.1%	5.1%	7.0%	11.1%	16.2%

Table 5B: Fundraising Ratio by Size									
Distribution (2014)	**10%**	**20%**	**30%**	**40%**	**50%**	**60%**	**70%**	**80%**	**90%**
Grassroots	0.7%	1.6%	2.8%	4.3%	5.8%	7.6%	10.2%	14.0%	22.1%
Small Safety Net	0.5%	1.3%	2.4%	3.7%	5.5%	7.2%	9.0%	11.1%	15.0%
Mid Safety Net	0.3%	0.8%	1.4%	2.1%	3.2%	4.8%	6.5%	8.9%	12.1%
Large Safety Net	0.2%	0.6%	1.0%	1.6%	2.3%	3.1%	4.6%	7.0%	10.8%
Economic Engine	0.1%	0.3%	0.6%	0.9%	1.5%	2.0%	2.9%	4.5%	8.8%
Total	0.4%	1.1%	2.0%	3.2%	4.7%	6.5%	8.7%	11.6%	16.9%

Table 5C: Fundraising Efficiency (Dollars spent per dollar raised) by sector

Distribution (2014)	10%	20%	30%	40%	50%	60%	70%	80%	90%
Religious Institutions	$0.01	$0.03	$0.04	$0.06	$0.08	$0.11	$0.14	$0.19	$0.30
Environment and Animal-Related	$0.01	$0.04	$0.07	$0.10	$0.14	$0.17	$0.21	$0.27	$0.40
Philanthropy	$0.02	$0.05	$0.08	$0.12	$0.16	$0.22	$0.26	$0.38	$0.56
Arts, Culture & Humanities	$0.03	$0.06	$0.09	$0.14	$0.18	$0.22	$0.27	$0.36	$0.52
Science, Technology & Social Sciences	$0.03	$0.05	$0.07	$0.10	$0.13	$0.16	$0.20	$0.26	$0.34
Other	$0.01	$0.03	$0.05	$0.08	$0.10	$0.14	$0.20	$0.29	$0.41
Youth Development	$0.04	$0.08	$0.12	$0.16	$0.21	$0.25	$0.31	$0.41	$0.70
Community Capacity	$0.03	$0.05	$0.08	$0.11	$0.14	$0.18	$0.24	$0.36	$0.63
Educational Institutions	$0.02	$0.07	$0.10	$0.14	$0.19	$0.25	$0.34	$0.45	$0.84
Health & Human Services	$0.03	$0.06	$0.10	$0.14	$0.18	$0.22	$0.29	$0.39	$0.62
Hospitals & Care Organizations	$0.03	$0.06	$0.09	$0.13	$0.18	$0.23	$0.31	$0.39	$0.63

Table 5D: Fundraising Efficiency by Size

Distribution (2014)	10%	20%	30%	40%	50%	60%	70%	80%	90%
Grassroots	$0.02	$0.05	$0.07	$0.11	$0.15	$0.21	$0.28	$0.40	$0.67
Small Safety Net	$0.03	$0.06	$0.09	$0.13	$0.17	$0.21	$0.27	$0.34	$0.52
Mid Safety Net	$0.05	$0.09	$0.12	$0.15	$0.19	$0.24	$0.31	$0.41	$0.69
Large Safety Net	$0.04	$0.08	$0.12	$0.16	$0.21	$0.26	$0.35	$0.43	$0.62
Economic Engine	$0.04	$0.09	$0.12	$0.15	$0.19	$0.23	$0.31	$0.46	$0.72
Total	$0.03	$0.06	$0.09	$0.13	$0.17	$0.22	$0.29	$0.39	$0.62

Exhibit 6 shows the Administrative Ratio by sector and then by size. For example, table 6A shows that the median Environment and Animal-related organization has an Administrative Ratio of 17.3% compared with 14.5% for Health and Human Services.

Table 6B shows Administrative Ratios by size. For example, 20% of the smallest grassroots organizations spend 39.5% or more on administration; the corresponding figure for the largest Economic Engines is 17.4%.

Table 6A: Administrative ratios

ADMINISTRATIVE RATIO

Distribution (2014)	10%	20%	30%	40%	50%	60%	70%	80%	90%
Religious Institutions	1.8%	5.5%	8.9%	12.6%	16.0%	20.2%	27.2%	40.8%	80.5%
Environment and Animal-Related	4.2%	6.8%	10.2%	14.5%	17.3%	20.4%	26.4%	30.7%	44.9%
Philanthropy	1.1%	2.8%	5.4%	9.2%	12.5%	17.8%	25.2%	36.1%	66.2%
Arts, Culture & Humanities	6.3%	10.6%	14.6%	17.6%	20.4%	23.6%	27.0%	33.7%	47.3%
Science, Technology & Social Sciences	7.4%	10.5%	13.1%	16.5%	20.1%	22.9%	26.6%	32.8%	49.8%
Other	3.0%	6.7%	9.4%	12.6%	15.7%	19.3%	23.8%	30.0%	46.5%
Youth Development	2.1%	4.0%	6.9%	10.5%	13.9%	17.3%	21.7%	27.5%	42.1%
Community Capacity	5.2%	9.5%	12.9%	15.8%	19.0%	22.3%	26.9%	33.6%	53.5%
Educational Institutions	4.5%	8.5%	11.1%	13.5%	16.1%	19.2%	23.0%	28.8%	39.2%
Health & Human Services	3.8%	7.5%	10.0%	12.2%	14.5%	17.2%	20.0%	25.3%	37.6%
Hospitals & Care Organizations	4.6%	8.4%	10.1%	12.7%	14.7%	17.5%	20.4%	26.9%	42.7%

Table 6B: Administrative ratio by Size

Distribution (2014)	10%	20%	30%	40%	50%	60%	70%	80%	90%
Grassroots	3.1%	6.6%	10.2%	13.9%	18.1%	22.6%	29.1%	39.5%	65.1%
Small Safety Net	4.6%	8.8%	11.5%	14.0%	16.5%	18.7%	21.8%	26.1%	33.1%
Mid Safety Net	6.4%	9.2%	11.5%	13.0%	15.2%	17.2%	19.4%	22.8%	27.4%
Large Safety Net	6.1%	8.3%	10.2%	12.1%	13.7%	15.4%	17.8%	21.2%	26.7%
Economic Engine	4.7%	7.4%	9.4%	10.5%	11.9%	13.6%	15.5%	17.4%	23.1%

Exhibit 7 shows the breakdown of expenses by sector and then size disaggregated into five broad categories: compensation & benefits, fees, office-related, financial and other. For example, table 7A shows office-related expenses are 12.1% (of the total) for Health & Human Services compared with 5.8% for Religious Institutions.

Table 7B shows the same information by size. For example, the smallest grassroots organizations spend an average of 35.3% on their expenses on compensation and benefits; the corresponding figure for the largest economic engines is 49.5%.

Table 7A: Aggregate expense structure

EXPENSE STRUCTURES	Compensation and Benefits	Fees	Office-related	Financial Expense	Other Costs
Arts, Culture & Humanities	47.3%	8.3%	9.6%	10.3%	24.6%
Community Capacity	53.7%	7.4%	10.8%	5.2%	22.9%
Educational Institutions	63.2%	5.4%	9.7%	8.3%	13.4%
Environment and Animal-Related	48.1%	13.8%	10.3%	6.3%	21.5%
Health & Human Services	60.1%	6.0%	12.1%	5.5%	16.3%
Hospitals & Care Organizations	46.8%	12.2%	7.6%	5.7%	27.7%
Other	29.7%	6.1%	6.7%	2.8%	54.8%
Philanthropy	49.2%	7.0%	7.2%	2.6%	34.2%
Religious Institutions	26.8%	52.5%	5.8%	2.4%	12.5%
Science, Technology & Social Sciences	47.4%	7.5%	15.1%	7.1%	22.9%
Youth Development	43.1%	8.6%	11.8%	8.8%	27.8%

Table 7B: Weighted average expense structure by Size

	Compensation and Benefits	Fees	Office-related	Financial Expense	Other Costs
Grassroots	35.3%	10.2%	10.1%	7.7%	36.6%
Small Safety Net	50.8%	8.0%	9.6%	6.7%	24.9%
Mid Safety Net	57.1%	8.2%	9.8%	5.6%	19.3%
Large Safety Net	59.8%	7.6%	10.3%	6.1%	16.2%
Economic Engine	49.5%	10.5%	8.3%	6.2%	25.5%

Exhibit 8 shows fundraising, management & general (i.e. administrative) and program expenses disaggregated into five broad categories: compensation & benefits, fees, office-related, financial and other. For example, 8.1% of program expenses are office related compared with 13.3% of fundraising expenses.

Table 8: Aggregate expense structure

EXPENSE OVERVIEW			
	Fundraising	**Management and General**	**Program**
Compensation and Benefits	52.8%	51.0%	50.7%
Fees	10.9%	14.0%	9.4%
Office-related	13.3%	11.8%	8.1%
Financial Expense	2.5%	8.1%	6.0%
Other Costs	20.6%	15.1%	25.8%

ABOUT THE AUTHORS

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This report is an addendum to ***Risk Management for Nonprofits*** by the same authors (to download a copy visit: http://owy.mn/1Z21jeV). A number of leading organizations have been working actively on the overhead issue. We encourage interested trustees to learn more at www.overheadmyth.com, www.realcostproject.org, www.councilofnonprofits.org and www.geofunders.org.

Overhead is a sensitive topic on which a lot has been written. So we wish to thank reviewed earlier drafts of this report and helped us “get it right”. Our 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 – and that their health is vital to New York. All New Yorkers are indebted to those nonprofit trustees 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.

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