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The Pressure to 'Do More with Less': Exploring Donor Misconceptions about Nonprofit Financial Health and Performance

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Abstract

As the nonprofit sector has grown in size and importance over the years, so has competition for donations and attention to the financial behaviors of organizations. Donors and information intermediaries have long expected nonprofits to remain financially lean - there is an expectation for organizations to direct all revenues directly to program areas, and any other spending is viewed as a misappropriation of funds. Nonprofit organizations attempt to satisfy this widely held donor expectation at the expense of organizational infrastructure and growth potential. I reviewed the Economic Research Institute's Form 990 data and NCCS CORE data for 2013/2014 and 2018/2019 to analyze how donors respond to nonprofit financial measures through their donative behaviors. I analyze the two periods to determine if donative behaviors, and thus donor expectations, have shifted with increased research and discourse on the negative implications of NPO financial leanness. This study looks at the root of the discussion about misguided donor expectations, the need for greater impact disclosure, and the need for more discussion with donors about the importance of organizational growth and capacity building to further program impact. Donor aversion to administrative spending and emphasis on financial leanness is evident in the findings. This reaffirms the need for more discussion about the importance of overhead spending and capacity building in the nonprofit sector and for more transparent and uniform means of reporting organizational impact.

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Introduction

The Growing Role of Nonprofit Organizations

Over the past decade, we have seen the nonprofit sector grow significantly – more specifically, at a rate of 20% compared to the for-profit sector's growth of 2-3%. This can be attributed to the fact that there are constantly new societal needs to be met and problems to address. Nonprofit organizations are an essential means of solving these problems and tending to the specific needs of communities. Each community must confront issues such as growing housing insecurity, food insecurity, environmental degradation, and a wide array of others that hinder societal progression and negatively impact human lives. The nonprofit sector has become a means for communities to bypass an often slow and inadequate policy implementation process. While the government is generally tasked with promoting social welfare, the responsibility tends to fall into the hands of nonprofit organizations. This occurs because governments attempt to minimize interference and control. While there are benefits to nonprofit organizations taking on some of this responsibility, there are also complications that result. It is important to note that nonprofit organizations function within our market system and must maintain their financial health to thrive and attract capital. They must earn revenues and incur expenses to fund their programs, face economic hardship, and attain their organizational goals. There are many widely held misconceptions about how nonprofit organizations function financially and operationally that hinder nonprofit success and growth.

Donor Expectations

Nonprofit organizations (NPOs) are a necessary force in the progression of our society, but they cannot operate without consistently attracting funding. Nonprofit organizations depend heavily upon individual and organizational donors for the funding necessary to accomplish their mission and make a meaningful difference. This is especially the case for activism NPOs that often do not rely heavily on selling products as a source of revenue, such as many environmental advocacy groups, human rights groups, and housing and food insecurity organizations. Their reliance on donations for revenue means these organizations face greater pressure from donors regarding their decisions. How organizations report financially and present their work can make a significant difference in the number of donors drawn to support the organization, how much funders will be willing to donate, and if they will offer continued support to the organization. As an example, Hahn (2013) finds that among a small sample of nonprofits, an increase in administrative and fundraising expenses was found to lead to a decrease in donations. This study found that donors are sensitive to accounting measures and deem increases in these expense categories as indicative of inefficiency. Therefore, donor biases and beliefs about nonprofit finances are of significant importance to organizations. Donor misconceptions and expectations about financial behaviors can have a notable impact on the donations they receive. They must satisfy potential donors' expectations if they intend to secure funding to sustain the organization, achieve their program goals, and continue serving their communities.

Nonprofits continue to face increasing pressure to conform to a wide variety of donor expectations and sector norms. As financial disclosure requirements have increased, so have donor and charity watchdog attention to financial behaviors. Parsons (2007) found that donors are more likely to make a charitable contribution to an organization if they receive financial

information along with their fundraising request. Information intermediaries, such as Charity Navigator and CharityWatch, assign a grade or rating to organizations based on a variety of performance indicators. In order to receive their highest ratings, organizations must exhibit leanness in their financial behaviors. Charity Navigator requires a maximum administrative expense ratio of 15.5% and a maximum fundraising ratio of 20% to earn their highest rating. CharityWatch penalizes organizations with 3 or more years of available assets. This pressure on leanness is also prevalent in funding criteria among foundations, government agencies, and other institutions. Organizations face pressure from all directions to minimize all non-program expenditures. While these expectations are held in attempt to curb mismanagement of funds and poor governance and instead reward the most efficient and impactful organizations, nonprofit leadership and recent empirical research by nonprofit experts has addressed the harm that is resulting from these misconceptions.

Financial Measures and Organizational Sustainability

While financial measures should not be used as a means of quantifying an NPO’s impact on their communities, financial data can give us an idea of how an organization might fare in hardship over time and what their capacity for growth and service expansion might look like. Despite the widely held emphasis on leanness, actions such as having cash on hand and building capacity are essential to organizational sustainability and growth. A nonprofit can further its impact and longer-term reach if they focus on strengthening the organization financially. Research has indicated that attention to the use of financial resources affects program performance. This indicates that it is important to converge donor opinions with recent findings on the importance of strengthening NPOs’ financial capacity. Donors are sensitive to the financial behaviors of an organization because they wish to donate to those who will be most

productive and impactful with their funds, which typically means donors expect all, or most, funds to flow directly to program areas. This is not a reasonable expectation because nonprofit organizations must invest in many different aspects of the organization beyond programs alone in order to thrive. Contrary to popular belief, organizations with solid financials are more likely to continue operations, grow, and expand their services within communities, thus having a more sustainable and lasting impact.

Measures of Nonprofit Financial Health

The health of an organization is indicated by its general vulnerability, capacity, and sustainability. Some important accounting measures commonly used in recent research to gauge NPO financial health are solvency, profitability, and margin. Solvency is a measure of a nonprofit's ability to pay off long-term debts. This means there are more total assets than total liabilities, which is necessary for measuring vulnerability and borrowing capacity. Solvency captures how an organization will fare if faced with a financial shock or unexpected threat (Bowman, 2011). I used total net assets/total assets to measure solvency. The profitability indicator I reviewed is the return on assets, calculated as the net income divided by total assets. This indicates how much the organization nets after accounting for expenses and is an indicator of long-term sustainability. Margin is a significant determinant of short-term sustainability (Prentice, 2016). This is a measure of the efficiency of earnings and will be measured as net income divided by total revenue (Greenlee & Tuckman, 2007). Below I concisely summarize the formulas I used in my analysis.

Table 1: Summary of Formulas

Solvency:

$$\frac{\text{Total Assets} - \text{Total Liabilities}}{\text{Total Assets}}$$

Profitability:

$$\frac{\text{Total Revenues} - \text{Total Expense}}{\text{Total Assets}}$$

Margin:

$$\frac{\text{Total Revenues} - \text{Total Expenses}}{\text{Total Revenues}}$$

Components of Overhead Expense:

$$\frac{\text{Management \& General Expense}}{\text{Total Expense}}$$

$$\frac{\text{Fundraising Expense}}{\text{Total Expense}}$$

The Overhead Ratio

The IRS requires financial statement disclosures via the Form 990 from all 501 (c) (3) nonprofits annually in order for organizations to maintain their tax-exempt status. Nonprofits depend heavily on in-kind donations to carry out organizational goals, and donors pay significant attention to the financial behaviors of an organization when deciding if they want to donate. A specific financial indicator that donors and charity reporting sites analyze to gauge nonprofit performance is the overhead expense ratio. There is a widely held misconception that a higher

overhead expense ratio has a negative relationship with program effectiveness and organizational performance. Overhead costs consist of expenditures such as fundraising, salaries, rent, legal services, and accounting. 'Overhead' is more generally defined as activities that are not identifiable with a single program, fundraising, or membership development activity, but are indispensable to the content of these activities and to the organization's existence. All overhead expenses fall within one of the two other groups – management & general expense or fundraising expense. These costs are essential to organizational infrastructure and lend directly to the successful implementation of programs. Many donors hold the misconception that these administrative costs are a diversion of funds away from program areas, and this 'misappropriation of funds' lessens the potential impact of an organization (Ashley and Faulk, 2010). There is much discourse today on the fact that the overhead ratio is an inaccurate measure of organizational success and efficiency and should not be analyzed as such. Overhead is a measure of inputs, which cannot paint a picture for donors about the lives changed by the programs, or outputs. It can be analyzed as a measure of organizational health, though, and aids in determining whether the organization has the capacity to continue serving communities over time.

Purpose of Study

The way donors perceive nonprofit financial behaviors has a significant impact on the decisions nonprofit organizations make. This has significant implications for the sector as a whole, and can either help or hinder their performance and progress towards addressing pressing societal causes. Program areas suffer when organizations sacrifice supporting infrastructure-building for the sake of satisfying donor expectations. This not only hurts the organization and its programs, but it hurts the communities that nonprofit organizations serve. The needs of our

communities cannot be fully met by starved nonprofit organizations. My goal of carrying out this research is to understand how donations are impacted by the financial behavior of nonprofit organizations. This is important to understand the significance of these financial measures to donors and how they affect their donation behavior. If higher overhead ratios and measures of invulnerability, capacity, and sustainability have a negative relationship with donations, organizations must attempt to communicate the necessity of these financial health indicators to donors. This would signal that donors perceive stronger financial health and infrastructural investment as indicative of poor program performance, which could harm nonprofit organizations in the long-term. On the other hand, if evidence of overhead aversion and preference towards leanness has diminished over time, this could lessen organizational pressure to lower overhead for the sake of donations. Since nonprofit financial professionals make decisions depending on what would satisfy potential donors, it is important to empirically study what donors' contributive behaviors suggest. I also intend to analyze if that landscape has changed over a 5-year time period due to increased research and calls for change by nonprofit leadership and journals in recent years. This study contributes to the existing research by analyzing the current landscape of nonprofit financial analysis and donor behaviors, and then comparing that more recent model to the same sample from 5 years prior to analyze shifts in donor responses to financial behaviors.

Literature Review

When deciding which financial health measures to focus on in this analysis, I built off findings from previous nonprofit research. Recent literature has dominantly utilized some generally accepted accounting constructs, three of which I used in this analysis: solvency,

margin, and profitability (Prentice, 2016). I reviewed the specific formulas outlined earlier in the paper, as discussed by previous researchers (Park, 2021, Prentice, 2016). I also analyzed the role of overhead expense measures in determining charitable contributions due to their prevalence in recent research and the extensive discussion in the sector about overhead aversion and the infrastructural consequences that result from it.

Progression of Nonprofit Financial Research

Financial management practices are very important to successful operations and mission attainment (Park, 2021), so it is important to study empirically the impacts of financial performance on varying aspects of the organization. The discussion about nonprofit financial performance began in the early 1990s when researchers sought to analyze the financial predictors of organizational demise, or dissolution (Tuckman & Chang, 1991). This initial study found that inadequate equity balances, revenue concentration, low administrative costs, and low or negative operation margins were all associated with NPO demise. Literature has since built off Tuckman & Chang's findings to further explore what financial performance indicators predict dissolution. Studies have extended beyond a focus on dissolution in recent years to even investigate what financial performance measures correspond with organizational impact, outcomes, ability to face economic hardship, and much more. While the breadth of existing research has overwhelmingly indicated that capacity building is core to sustainability and growth, many organizations still fear how donors will respond to seemingly 'frivolous', or non-program-specific, spending and decisions.

Responding to Economic Hardship

There have been many studies in recent years about the negative consequences of normative managerial practices that emphasize minimized overhead and financial leanness. One such study looks at the impact of financial leanness on the ability of nonprofits to respond to changes in the economic environment (Mitchell, 2015). To do this, the study specifically looked at years of net assets as a measure of how long the organization could sustain its current program expenses by liquidating net assets. The research found that lean nonprofits are significantly less capable of responding to changes in the economic environment compared with less lean organizations. They specifically cite the inefficiency that results from nonprofit leanness. They call for foundations and donors to reconsider mandatory financial ratio thresholds since leanness restricts organizations' ability to grow and respond to a changing economic environment. Donor emphasis on leanness puts organizations at risk of dissolution in unsure economic times. Nonprofit organizations, like for-profit organizations, must maintain the capacity necessary to face turmoil if they wish to survive and continue to grow. This specific study indicates the importance of maintaining an optimal level of assets for the sake of an organization's success.

Inadequacy of Overhead as a Performance Measure

The emphasis placed on lower proportions of nonprofit overhead has been heavily perpetuated by charity watchdogs, who grade and report nonprofit performance and financial behaviors. They post these grades on their site for donors to utilize in making funding decisions. Overhead expenses being framed as 'frivolous spending' has created an environment where nonprofits are pressured to neglect financial systems, employee training, information technology systems, employee compensation, fundraising processes, and many more essential areas of an

organization. Many organizations have come together and released publications urging donors and the public to dispel myths regarding overhead. Large and significant organizations in the sector, such as Bridgespan, Guidstar, and CharityWatch, have made statements on the inadequacy of overhead as a productivity measure. Nonprofit Quarterly ended an article by saying, “So when you are making your charitable giving decisions, please consider the whole picture. The people and communities served by charities don’t need low overhead, they need high performance” (Berger, Harold, Taylor 2013). The pressure to maintain low management & general and fundraising spending limits nonprofit organizations’ capacity for growth. Focus on meeting lean expectations limits their ability to have a positive impact on their communities through successful programs. The lack of uniform and meaningful methods of reporting impact have led funders to rely on financial ratios as a measure of impact and effectiveness, but this is not an effective or sustainable method. Every nonprofit organization has unique needs and goals that require different financial strategies. Neglecting areas of overhead expense puts the organization at risk and stifles its potential.

The pressure among nonprofit organizations to maintain low levels of fundraising and administrative expenses is a direct result of studies that indicate donors respond negatively to lower program spending. Qu and Daniel (2020) surveyed individuals to gauge their ‘overhead aversion’, which refers to donors’ reluctance to donate to organizations with higher overhead ratios. Participants in the study indicated that their primary reason for choosing an organization was their higher program spending compared to overhead spending. Qu and Daniel additionally found that disclosing the purpose of overhead expense alleviated overhead aversion to some degree. There was even a beneficial result when the word ‘overhead’ was simply omitted. He interestingly also found that many participants couldn’t produce an accurate definition of what

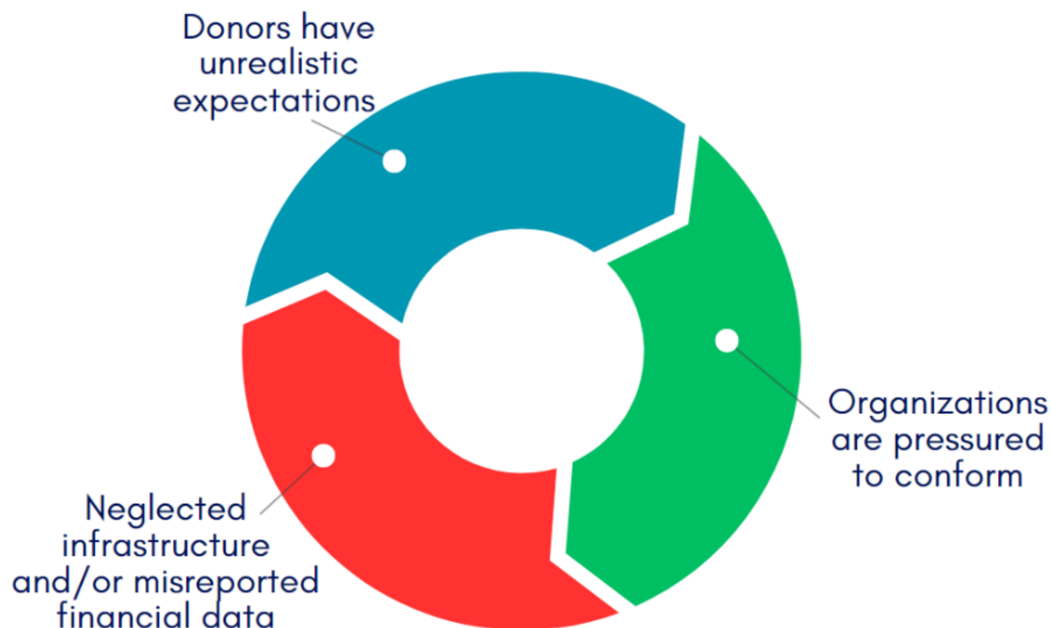
overhead expense is. This leads to the conclusion that much overhead aversion is simply based on preexisting misconceptions about what overhead expenses consist of. A generalization exists that non-program spending is a sign of poor governance – that this money simply goes to executive salaries and takes from the actual programs and communities in need. This is simply not the case across the sector and overhead expenses encapsulate a wide array of essential expense areas that benefit high performance organizations. This study verifies that overhead aversion is a result of donor and public misconceptions and that by framing overhead differently and/or providing more information around the specific components of overhead spending and why they are essential to performance, organizations could lessen overhead aversion. There is a generally held perception of overhead spending as 'bad' and a misuse of donors' funds, while program spending becomes synonymous with performance. Donors' attitude towards even the phrase 'overhead expense' alone has majorly shaped the way organizations behave and report their financial information.

The Nonprofit Starvation Cycle

Organizations' dependence on donations to achieve program goals and the concept of donor overhead aversion often leads nonprofits to lower their overhead ratios and sacrifice sound infrastructure as a result. Competition for donations forces nonprofits to cut their overhead spending lower and lower. Lecy and Searing (2014) studied falling overhead ratios over the years to discover if this is truly a phenomenon occurring as a result of overhead aversion. They found empirically that a steady decline has been reported for overhead expenditure within the sector. Overhead ratios have declined by 2.6% since 1985. This seems to verify the existence of the nonprofit starvation cycle as a result of donors' aversion to higher overhead spending. Nonprofits respond to donor overhead aversion by conforming to their expectations. There is

high demand and much competition for donations in the sector, which forces organizations to maintain a competitive edge by lowering overhead with the belief that donors will fund organizations that remain lean and direct all funds to program areas. This pressure to do more with less hurts organizational efficiency and increases financial vulnerability.

The nonprofit starvation cycle is a significant issue in the sector. In 2009, Gregory and Howard studied the factors that contribute to the continuation of this cycle. They took a deeper look into the cycle itself and outlined the steps that result from myths about overhead. It begins with unrealistic expectations held by funders surrounding financial ratios. In the second step, nonprofits feel the pressure to conform to these expectations in order to secure funding and compete with other nonprofit organizations. Next, organizations will choose one of two alternatives to confront these expectations: they will either underreport their overhead expenditures or neglect overhead expenses outright. These behaviors further perpetuate funders' unrealistic expectations. In the last step of the cycle, donors continuously expect organizations to do more with less and this cycle continues. Neglecting infrastructure – letting systems become obsolete, not adequately funding often overworked employees, inadequate training programs, etc. – hurts the organization's program areas and mission achievement in the long run. Organizations that can't offer competitive salaries for qualified candidates, train employees in a meaningful way, or provide technology that allows for growth and improvement cannot adequately thrive and sustain themselves. Studies indicate that donors are off-put by higher overhead ratios, and this results in organizations lowering their reported spending on fundraising and administrative costs – either through truly spending less or simply reporting less. This leads us to look more specifically at the significance of overhead and the part it plays in organizational performance.



Overhead Ratio and Program Performance

In 2021, Altamimi and Liu looked at how overhead ratios affect program outcomes specifically in the arts nonprofit sector. The research found that there is a curvilinear relationship between overhead ratios and nonprofit outcomes. As one would expect, productivity increases alongside increasing overhead ratios up to an optimal point. Beyond this optimal point, program outcomes begin to suffer as a result of poor governance. This implies an optimal level of overhead expense. Further study seems to disprove the general belief that the optimal overhead ratio does not exceed 25%. In their research, Altamimi and Liu (2021) found optimal levels were around 40% for this specific sample. They end by encouraging exploring the prioritization of other measures of efficiency and performance apart from overhead ratios. A similar study was carried out to explore the linkage between overhead expense and nonprofit effectiveness

specifically looking at Habitat for Humanity (Berrett, 2021). The study measures the dependent variable of effectiveness as houses built by the organization. The findings suggest that an increase in overhead ratios leads to greater effectiveness in terms of houses built and revenues raised to an optimal point, which lingers around 15% for this specific organization. Optimal overhead ratios are not so easily defined and organizational needs change across nonprofit categories – even across different organizations – as shown by these two studies. This further demonstrates that charity watchdog organizations' ratings of financial measures are inadequate. There is a necessary level of overhead needed for an organization to function efficiently and while exorbitant overhead spending can indicate poor governance and mismanagement of funds, there is no uniform way of measuring what this optimal level is and trying to do so is unfair.

Financial Behaviors and Growth

Building off of the existing research on nonprofit overhead and performance, another study looks at how both revenue concentration and overhead costs lend to financial capacity growth (Chikoto and Neely, 2013). Revenue diversification helps an organization maximize resource independence as donor preferences change and government support fluctuates. This prevents a nonprofit from being dependent on any one source of income. Their findings suggest that revenue diversification is necessary to protect organizations from financial vulnerability. The next key finding in the study is that there is a significant positive relationship between financial capacity growth (whether measured as total revenue or restricted or unrestricted fund balances) and administrative support and fundraising expense. "Spending more on administrative support is associated with an expected 13% growth in total revenue over a 5-year period (15% when we exclude hospitals) and an expected 7% growth in both restricted and unrestricted net assets over the 5-year period" (Chikoto and Neely, 2013, p. 578). Therefore, empirical evidence

indicates that the overhead ratio and strategic revenue management allow an organization to grow and expand, which then allows them to have a greater impact on communities and a greater long-term impact. Therefore, by investing in overhead, a nonprofit organization increases its longevity and stability compared to its counterparts who neglect administrative expenditures.

Financial Behaviors and Dissolution

The topic of longevity is also addressed in an article by Lu and Shon (2019). Their study looks at the rate of dissolution among nonprofit organizations in relation to a nonprofit's overhead costs and revenue mix. They find that there is a curvilinear relationship between overhead and risk of dissolution. Also, nonprofit organizations with more diversified revenue portfolios experience a lower risk of dissolution. This reaffirms the initially positive relationship between overhead ratios and performance, which then diminishes and declines after an optimal level is exceeded. As expected, diversifying revenues makes organizations less susceptible to financial instability and decreases their risk of dissolution. Revenue diversification can also be related to overhead expense because it takes fundraising and administrative dollars to attract a variety of revenue sources.

In recent years, there has been a call by information intermediaries, nonprofit journals, researchers, and nonprofit organizations themselves to lessen reliance on the overhead ratio as a measure of performance. In 2013, GuideStar, the BBB Wise Giving Alliance, and Charity Navigator launched The Overhead Myth campaign in order to address the misconception that financial ratios are the sole indicator of nonprofit performance. In 2019, five nonprofit CEOs announced that they would begin doing more to help organizations fund overhead, noting the importance of decent wages, technology, and other areas of overhead to an organization. There

has been extensive research on the necessity of overhead to organizational growth, longevity, and performance to an optimal point. Much discourse has occurred about the consequences of the nonprofit starvation cycle and the ways neglected infrastructure manifests as poor-performing organizations – even leading to dissolution. Nonprofit scholars are working to increase impact disclosure in order to give funders and communities a better understanding of the specific work nonprofits do. This is being done in an attempt to lessen the focus on the overhead expense ratio and other measures of financial performance.

With all of this, I think it is important to gauge the current landscape of overhead aversion – do higher overhead ratios lead to lower levels of contribution revenues? Do donors' reliance on financial measures to determine if an organization is making a meaningful difference reflect in their donative behaviors? Has the landscape changed in recent years with all of the research being done and calls for change? By empirically analyzing the relationship between the financial performance of nonprofit organizations and their contribution revenues, we can attempt to answer these questions and deliberation can take place on the next steps for the sector. I propose that there is still an inverse relationship between overhead spending and donations. There are still many sites that focus on overhead as a measure of efficiency in grading criteria and many organizations understandably struggle to quantify their impact. There are also still widely held expectations for nonprofit organizations to remain lean and focus directly on program areas – it is not considered acceptable for NPOS to accumulate assets or cash for the sake of organizational growth and expansion. The public has more access to nonprofit financial information than ever, and a consequence of nonprofit financial leanness is a continued struggle to access the resources and employees necessary to quantify and report program outcomes.

Data & Methodology

In my study, I am going to be focusing on public charities relying dominantly on donations for funding (50% or more of revenues are from contributions). I reviewed IRS Statistics of Income, Economic Research Institute's Form 990 Finder, and NCCS (National Center of Charitable Statistics) CORE data from 2013 to 2014 to measure how donors respond to overhead, solvency, profitability, and margin measures through their donative behaviors. I reviewed the same sample for the years 2018 and 2019 to determine if donor expectations have shifted with increased research and discourse on the negative implications of NPO financial leanness and donor focus on organizations' financial performance.

My dependent variable is the natural log of contribution revenue in the year following the release of the Form 990 containing the financial health measures used as independent variables (2014 in the first model, 2019 in the second). This will determine how financial performance reported for the previous year impacted donor perceptions and behavior in the year following. This follows the method used in previous studies, such as Tinkelman (1999) and Trussel and Parsons (2007). This digitized data set differentiates government grants from private contributions, which allows this study to more accurately analyze the impact our financial health measures have on individual donations. I take the natural log of contribution revenues because, following previous research, I expect that revenues will have diminishing returns as our independent variables increase. I also divided the overhead ratio into its two components in order to determine the relation donors have with the fundraising expense ratio and the management and general expense ratio separately.

I included variables in my model for organizational size (measured in total assets), industry type as outlined in the National Taxonomy of Exempt Entities (NTEE), and age. I chose

to create a variable that distinguishes organizations with less than $100,000 in assets and another variable that distinguishes organizations with more than $500,000 in assets. I chose to do this due to the findings of Lecy and Searing (2015), which conclude that smaller nonprofits have notably different financial behaviors and responding donative patterns than those with mid-sized and larger nonprofit organizations. The age variable is important because organizations with a stronger foothold in the sector, and a stronger reputation, will likely have less difficulty soliciting donations. This study looks at the root of the discussion about misguided donor expectations, the need for greater impact disclosure, and the necessity of more discussion with donors about the importance of organizational growth and capacity building in order to further impact. I did this by empirically examining the impact on contribution revenues of nonprofits' financial behaviors.

Using the NCCS CORE files for 2013, 2014, 2018, and 2019, I narrowed down organizations that met the following criteria across all four years: organization classified as a public charity and 50% or more of revenues are contribution revenues. I then filtered out organizations with negative assets, revenues, or expenses and those organizations with zero expenses. After narrowing the sample of NCCS data to fit these criteria, I ensured that there was Form 990 data on the Economic Research Institute's website for all of the four years I analyzed (2013, 2014, 2018, and 2019). I then selected a random sample of 200 organizations from this large, refined set of data.

Based on the literature, in the initial model for 2013/2014, I hypothesize that donor behavior will be impacted inversely by both the management & general and fundraising expense ratios. This is due to the prior discussion of overhead aversion, and the tendency for donors and information intermediaries to lump the overhead expense areas together as generally bad and a misuse of funds. I expect that our solvency measure will have a positive relationship with

contribution revenue. Margin would similarly have a positive relationship with contribution revenue because they must earn revenues adequate to cover program and overhead expenses. Parsons and Trussel (2008) found that nonprofit organizations with a higher operating margin were able to raise more donations than those with lower operating margins. Profitability would be expected to have a negative relationship with contribution revenues since donors would perceive profitability as wasted donations.

When considering the signs for the variables in the 2018/2019 model, I conclude that increased research and discussion about the importance of capacity building and infrastructure spending for organizational growth and sustainability would slightly shift the relationships earlier expected. With that being said, I still believe management & general expense (MGR) will have a negative relationship with contribution revenues. Since there are not many resources for impact measurement, I expect donor reliance on overhead as a means of measuring performance to still exist heavily. I expect that this relationship will be positive – more fundraising expense will allow organizations to solicit more donations. I expect that organizations will be slightly less averse to overhead spending and for increased social media use for fundraising and marketing to result in a positive relationship between the variables. NPOs have more means of reaching donors through social media advertisement, and increased spending in that area will increase donor awareness about programs, their impact, and the organization's mission. I expect the other relationships to remain the same.

Below are each of my variables and their expected signs:

Table 2: Variables & Expected Signs

Variable	Description	Expected Sign when t = 2014	Expected Sign when t = 2019	Explanation
CONTR	ln of Contribution Revenue in year *t*			Dependent Variable
MGR	Management & General Expense Ratio at year *(t-1)*	-	-	Overhead aversion – donors will reward lower levels of management & general expense as a ratio to total expense.
FUNDR	Fundraising Expense Ratio at year *(t-1)*	-	+	Overhead aversion – similar to MGR, donors will expect a low fundraising expense ratio. With increased digital marketing and social media to solicit donations, a higher fundraising expense ratio will lead to greater contribution revenues.
SOLV	Solvency at year *(t-1)*	+	+	Stability measure – this indicates the ability of an organization to cover liabilities. This measure would be expected to be positive.
PROF	Profitability at year *(t-1)*	-	-	Underutilized donor funds. If revenues are extremely high while expenses are extremely low, organizations are not fully funding programs or infrastructure, meaning donors' funds are being wasted.
MARG	Margin at year *(t-1)*	+	+	Stability measure – indicates if an organization can fund its expenses adequately (Greenlee and Trussel, 2000)
AGE	Years since receiving tax-exempt status at year *(t-1)*	+	+	Older organizations will be more established and stable. Will have more name recognition (Bennett and DiLorenzo, 1994)

I analyzed the following equation:

$$\ln(CONTR)_t = \beta_o + \beta_1(MGR)_{t-1} + \beta_2(FUNDR)_{t-1} + \beta_3(MARG)_{t-1} + \beta_4(PROF)_{t-1} + \beta_5(SOLV)_{t-1} + \beta_6(ASSET100)_{t-1} + \beta_7(ASSET500)_{t-1} + \beta_8(ARTS)_{t-1} + \beta_9(EDU)_{t-1} + \beta_{10}(HEALTH)_{t-1} + \beta_{11}(HUMANSVS)_{t-1} + \beta_{12}(AGE)_{t-1} + \varepsilon_i$$

Results

Testing for superfluous variables indicates that profitability should be removed from the model. The p-value is statistically insignificant, and when the profitability variable is removed from the model, each of the models overall improved. This is also theoretically reasonable since donors likely do not use profitability (net income divided by total assets) as a measure of nonprofit performance as commonly as they do other financial health measures. Profitability is not significant in the nonprofit sector since the goal of an NPO is not to accumulate profit but to utilize revenues to fund programs and the overall organization. Measuring net income against assets, or return on assets, does not paint a meaningful picture for donors of nonprofit performance. It does not factor in expense areas or use of funds. I thus omitted profitability from the models.

Below is the new model after omitting the superfluous variable:

$$\ln(CONTR)_t = \beta_o + \beta_1(MGR)_{t-1} + \beta_2(FUNDR)_{t-1} + \beta_3(MARG)_{t-1} + \beta_4(SOLV)_{t-1} + \beta_5(ASSET100)_{t-1} + \beta_6(ASSET500)_{t-1} + \beta_7(ARTS)_{t-1} + \beta_8(EDU)_{t-1} + \beta_9(HEALTH)_{t-1} + \beta_{10}(HUMANSVS)_{t-1} + \beta_{11}(AGE)_{t-1} + \varepsilon_i$$

Below are tables containing the descriptive statistics for all variables for the two time periods analyzed.

Table 4: 2013/2014 Descriptive Statistics

Variable	Obs.	Mean	Std. Dev	Min.	Max.
ln(14CONTR)	*200*	*13.3445*	*1.5882*	*7.3045*	*21.3531*
MGR	*200*	*0.1611*	*0.1614*	*0*	*1.0000*
FUNDR	*200*	*0.0435*	*0.0712*	*0*	*0.4071*
SOLV	*200*	*0.7502*	*0.8269*	*-9.5294*	*1*
MARG	*200*	*0.0614*	*0.2865*	*-1.2763*	*0.9450*
ASSET100	*200*	*0.12*	*0.3258*	*0*	*1*
ASSET500	*200*	*0.6*	*0.4911*	*0*	*1*
ARTS	*200*	*0.055*	*0.2286*	*0*	*1*
EDU	*200*	*0.13*	*0.3371*	*0*	*1*
HEALTH	*200*	*0.125*	*0.3315*	*0*	*1*
HUMANSVS	*200*	*0.375*	*0.4853*	*0*	*1*
AGE	*200*	*18.5*	*16.1167*	*0*	*73*

Table 5: 2018/2019 Descriptive Statistics

Variable	Obs.	Mean	Std. Dev	Min.	Max.
ln(19CONTR)	*200*	*13.3173*	*1.7101*	*7.7075*	*20.9164*
MGR	*200*	*0.1485*	*0.1459*	*0*	*0.9970*
FUNDR	*200*	*0.0475*	*0.0869*	*0*	*0.8077*
SOLV	*200*	*0.7975*	*0.3532*	*-0.9778*	*1*
MARG	*200*	*0.0282*	*0.4281*	*-3.9759*	*2.1786*
ASSET100	*200*	*0.1*	*0.3008*	*0*	*1*
ASSET500	*200*	*0.665*	*0.4732*	*0*	*1*
ARTS	*200*	*0.055*	*0.2286*	*0*	*1*
EDU	*200*	*0.13*	*0.3371*	*0*	*1*
HEALTH	*200*	*0.125*	*0.3315*	*0*	*1*
HUMANSVS	*200*	*0.375*	*0.4853*	*0*	*1*
AGE	*200*	*27.095*	*16.0788*	*5*	*78*

The following section will discuss the findings from regression analysis for the two periods of time analyzed.

Table 6: 2013/2014 Output

Regression Statistics	
Multiple R	0.6053
R Square	0.3664
Adj R Square	0.3293
Standard Error	1.3006
Observations	200

Y = ln(contrev)

ANOVA

	df	*SS*	*MS*	*F*	*Signif F*
Regression	11	183.9218	16.7202	9.8841	4.57217E-14
Residual	188	318.0237	1.6916		
Total	199	501.9455			

	Coefficients	*Std Error*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*	*Lower 95.0%*	*Upper 95.0%*
Intercept	12.9013	0.3271	39.4420	7.28E-93	12.2561	13.5465	12.2561	13.5465
MGR	-2.2622	0.6196	-3.6508	3.39E-04	-3.4845	-1.0398	-3.4845	-1.0398
FUNDR	-0.1999	1.3492	-0.1482	0.8824	-2.8615	2.4616	-2.8615	2.4616
SOLV	-0.3404	0.1147	-2.9675	0.0034	-0.5666	-0.1141	-0.5666	-0.1141
MARG	0.5724	0.3474	1.6476	0.1011	-0.1129	1.2576	-0.1129	1.2576
ASSET100	-0.8482	0.3381	-2.5085	0.0130	-1.5153	-0.1812	-1.5153	-0.1812
ASSET500	0.9817	0.2247	4.3687	2.06E-05	0.5384	1.4249	0.5384	1.4249
ARTS	-1.2669	0.4375	-2.8958	0.0042	-2.1300	-0.4039	-2.1300	-0.4039
EDU	0.2359	0.3122	0.7556	0.4508	-0.3799	0.8516	-0.3799	0.8516
HEALTH	-0.0207	0.3136	-0.0660	0.9474	-0.6394	0.5980	-0.6394	0.5980
HUMANSVS	0.2141	0.2264	0.9459	0.3454	-0.2325	0.6607	-0.2325	0.6607
AGE	0.0155	0.0062	2.5174	0.0127	0.0034	0.0277	0.0034	0.0277

Looking at our initial model for 2013 & 2014, we find through regression analysis that our F-statistic is 4.5721E-14. This indicates that the independent variables, our financial health measures during 2013, are jointly significant in determining contribution revenues (the dependent variable) in 2014. Management & general expense ratio (MGR) and solvency (SOLV)

both are significant at a level less than 1%, which indicates that these two measures have a strong relationship with contribution revenues (2014). Both SOLV and MGR have negative coefficients. This means that a negative relationship exists between each of these variables and donations. Based on the output results, a 1% increase in the management & general ratio in 2013 would result in a 2.26% decrease in contribution revenues for 2014. Margin (MARG) has a p-value of 0.1011. The coefficient of MARG is positive, indicating that the variable has a positive relationship with donations. This means that 0.57% increase in contribution revenues will result from a 1% increase in the margin ratio. The fundraising expense ratio (FUNDR) has a surprisingly high (insignificant) p-value. This leads us to conclude that the fundraising expense ratio is not significant to donors and their donative decisions, which is a surprising result. We can conclude from this analysis, as well as from theory and prior research, that much donor overhead aversion is likely specific to the administrative expense component – salaries, technology, and other infrastructure-focused expenditures. This aligns with the public fear of poor governance and mismanagement of funds that motivates donor attention to financial behaviors.

The coefficients for each independent variable were as predicted, besides SOLV. The solvency measure has a negative sign, indicating that higher levels of solvency actually have a negative relationship with contribution revenues. While this contradicts my earlier expectations, it does parallel the discussion earlier presented regarding profitability. It also aligns with general literature and research suggesting that donors expect unrealistic leanness in nonprofit financial behaviors. Donors do not reward asset accumulation with higher donations because they expect financial leanness from organizations. A high level of assets significantly exceeding liabilities could signal 'frivolous' asset accumulation to donors. As discussed earlier, years of net assets are necessary for an organization's longevity and its ability to face changes in the economic

environment (Mitchell, 2015). Despite this, donor misconceptions lead to a negative relationship between our measure of solvency and contribution revenues. Lean nonprofits are less capable of adjusting to changes in the economic environment than less lean organizations, but more lean organizations receive greater donations from funders. This is supported by the data analysis for our 2013/2014 model.

The asset size dummy variables are both significant in this model. The dummy variable for smaller organizations (organizations with assets less than $100,000) is significant at the 5% level with a p-value of 0.013. The larger organizations dummy variable (distinguishing organizations with assets greater than $500,000) is even more significant. It is significant at less than the 1% level with a p-value of 2.063E-05. The negative coefficient for the smaller asset size organizations dummy variable indicates that when these smaller organizations are included in the model, contribution revenues decrease by 0.85%. This indicates that smaller organizations, those with smaller total assets, face the brunt of the impact of donor expectations for financially lean behaviors. This intensifies their struggle to obtain contributions and grow. While donors hold these financial behavior expectations in hopes of curbing mismanagement of funds and preventing organizations from growing too large internally, they are actually hurting smaller organizations that need the resources and capacity-building to better serve their communities and develop a foothold in the sector.

Similarly, the 2013/2014 model shows that the dummy variable for organizations that fall under the NTEE category of ‘arts’ is significant at less than 1%. The coefficient is negative, meaning when these arts organizations are factored into the model, contribution revenues fall. This implies that arts organizations face more financial pressure and have a harder time soliciting donations than organizations in other subsectors.

Age is significant in the model at less than the 1% level with a p-value of 0.0127. The positive coefficient means that age and donations have a positive relationship, although small. This makes theoretical sense, since older organizations will have more loyal donors, more stability, and stronger infrastructure. Older nonprofits with more experience and longer history of impact will not face as much pressure from donors regarding financial behaviors.

Table 7: 2018/2019 Output

Regression Statistics	
Multiple R	0.5883
R Square	0.3461
Adj R Square	0.3078
Std. Error	1.4228
Observations	200

Y = ln(contrev)

ANOVA

	df	*SS*	*MS*	*F*	*Signif F*
Regression	11	201.3836	18.3076	9.0442	6.97E-13
Residual	188	380.5575	2.0242		
Total	199	581.9411			

	Coefficients	*Std Error*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*	*Lower 95.0%*	*Upper 95.0%*
Intercept	13.6945	0.4251	32.2178	1.791E-78	12.8560	14.5330	12.8560	14.5330
MGR	-3.2285	0.7151	-4.5146	1.117E-05	-4.6392	-1.8178	-4.6392	-1.8178
FUNDR	0.8470	1.1997	0.7060	0.4811	-1.5196	3.2136	-1.5196	3.2136
SOLV	-0.7316	0.2972	-2.4615	0.0147	-1.3179	-0.1453	-1.3179	-0.1453
MARG	0.4800	0.2457	1.9537	0.0522	-0.0047	0.9646	-0.0047	0.9646
ASSET100	-1.4606	0.3935	-3.7117	0.0003	-2.2368	-0.6843	-2.2368	-0.6843
ASSET500	0.7036	0.2489	2.8267	0.0052	0.2126	1.1946	0.2126	1.1946
ARTS	-1.0874	0.4767	-2.2812	0.0237	-2.0277	-0.1471	-2.0277	-0.1471
EDU	0.4144	0.3370	1.2297	0.2204	-0.2504	1.0792	-0.2504	1.0792
HEALTH	0.1222	0.3391	0.3603	0.7190	-0.5467	0.7911	-0.5467	0.7911
HUMANSVS	0.3697	0.2469	1.4972	0.1360	-0.1174	0.8568	-0.1174	0.8568
AGE	0.0051	0.0066	0.7647	0.4454	-0.0080	0.0181	-0.0080	0.0181

I then looked at the regression analysis results for the 2018/2019 data. Again, there is a very low significance-F of 6.97E-13, indicating a high level of joint significance among the variables. This means that the independent variables included in the model are highly significant in determining our dependent variable, contribution revenues. The management & general expense ratio (MGR) is highly significant at a level of less than 1%. This variable has a p-value of 1.1E-05. It is an even more significant variable than in the prior analysis for the same sample of organizations in 2013/2014. The coefficient is also more negative than in the prior model at negative 3.2285. This means that a 1% increase in the management & general expense ratio in 2018 will result in a 3.23% decrease in contribution revenues for 2019. Solvency (SOLV) is significant at a level of less than 5% with a p-value of 0.0147. The coefficient is -0.7316, meaning a 1% increase in SOLV will result in a 0.73% decrease in contribution revenues. Margin (MARG) is significant at a level of less than 10%. The p-value for MARG is 0.0522 and the coefficient is again positive, signifying a positive relationship between our margin ratio and contribution revenues. We again see that the fundraising expense ratio (FUNDR) is statistically insignificant with a p-value of 0.4811. This is shocking, especially because it would be expected that in recent years, higher levels of fundraising expense would be beneficial in soliciting more donations and for the variables to thus have a significant positive relationship. This could be contributed to, at least in part, the fact that recent research has discovered that many organizations inaccurately report zero fundraising expenses on their Form 990 (Krishnan et al., 2006). Donor expectations have pressured many organizations to misrepresent their overhead expenses to make program spending look more attractive. This reinforces the nonprofit starvation cycle, and donors will continue to expect organizations to be able to ‘do more with less’. This research indicates that organizations face overhead pressure primarily on the

administrative component of overhead expense. Donors respond negatively to an organization spending a higher fraction of their total expenditures on staffing, salaries, rent, technology, and other capacity-focused expenses. The negative coefficients for MGR and SOLV in this model reinforce our expectation that donors reward financial leanness and view overhead and infrastructure-focused spending as frivolous.

Asset size is significant in this model as well in the determination of contribution revenues. Both smaller organizations (ASSET100) and larger organizations (ASSET500) have p-values that are statistically significant at less than the 1% level. ASSET100 has a p-value of 0.0003, and a negative coefficient. When nonprofit organizations with less than $100,000 are included in the model, donations decrease by 1.4606%. Larger nonprofits with assets greater than $500,000 in the model result in an increase in contribution revenues of 0.7036%. In both models, smaller organizations face a decrease in contributions as a result of donor misconceptions, whereas larger organizations don't seem to face as much negative impact.

There is also a p-value of 0.0237 for organizations that fall into the arts subsector (ARTS), indicating that this distinction is significant in determining contribution revenues at a level less than 5%. The coefficient is negative, which indicates that when arts nonprofits are included in the model, contribution revenues decrease. Again, arts organizations face notable pressure for leanness from donors.

In this model, age of the organization (AGE) is not a statistically significant determinant of contribution revenues. Donors do not seem to care as much in the 2018/2019 model about age and the reputation that comes with more time and experience as an organization.

Table 8: Change in Output 2013/2014 – 2018/2019

Change	*Coefficients*	*P-value*
Intercept	0.7932	1.79E-78
MGR	-0.9664	-3.28E-04
FUNDR	1.0469	-0.4013
SOLV	-0.3912	0.0113
MARG	-0.0924	-0.0489
ASSET100	-0.6123	-0.0127
ASSET500	-0.2781	0.0052
ARTS	0.1796	0.0194
EDU	0.1786	-0.2305
HEALTH	0.1429	-0.2284
HUMANSVS	0.1555	-0.2094
AGE	-0.0105	0.4328

By comparing the two models, we can examine the shift in donor behavior and expectations over the five-year period. Looking at the change in output for MGR, we see that the relationship with our dependent variable, contribution revenues, has grown stronger over time. The coefficient is more negative now than it was in the 2013/14 output and the p-value decreased significantly. This signifies that donors are notably *more* averse to management & general spending than they were in the past – overhead aversion, and more specifically an aversion to administrative spending, has grown more severe over the five-year period for this sample of 200 nonprofit organizations. The significance of solvency (SOLV) has decreased very slightly over the time period, indicated by the slight p-value increase. It is still highly statistically significant and has a lower coefficient, indicating a greater impact on contribution revenues resulting from a 1% change in this independent variable, SOLV. Margins (MARG) became more significant in determining donations, having a p-value of 0.522 by 2018/2019. This leads us to conclude that donors, in general, are paying greater attention to organizations' spending decisions. This data

suggests that overhead aversion and donor emphasis on financial leanness is still prevalent in the sector.

Discussion and Conclusion

Donors and the general public have more access to nonprofit organizations' financial information than ever before. Charity watchdog sites are easy to access and navigate, and Form 990s are public for anyone to view. As the nonprofit sector has grown in size and scope, so has pressure for more accessible and transparent financial reporting. This has also been encouraged due to nonprofit scandals and accountability issues over the years. Examples include the lack of outcome transparency demonstrated on the behalf of the Red Cross following the 2010 earthquake in Haiti and Wounded Warrior Project executives taking expensive trips and living extravagant lifestyles while neglecting program areas in 2016. These instances, and other similar ones, have led to skepticism on the part of donors and the public and overall compromised public trust in nonprofit organizations. There are now more extensive expectations for transparency regarding how donations are being used by organizations. Demanding more transparency and detailed reporting is an understandable result of nonprofit scandals and misuse of contribution revenues, but as this analysis has indicated, this has also had negative implications for the sector. It starves organizations that are behaving ethically and want to serve communities while also building a durable organization. Expecting extreme leanness in nonprofit organizations' financial behaviors has led to many organizations that lack a solid foundation. These NPOs struggle to meet unreasonable donor expectations while still positively impacting their communities. This leads to high rates of dissolution in the sector and makes it difficult for organizations to grow and expand their services. Financial disclosure is necessary for donors and the general public to

check poor governance and extreme mismanagement of funds, but it is now often being used as a way for donors and charity watchdog sites to overanalyze financial measures and draw conclusions about nonprofit outcomes, impact, and the overall performance using input measures. The extreme is now optimal in the eyes of donors – the less funds that organizations allocate to non-program areas, the better. Despite widespread efforts to lessen donor reliance on financial measures when making donative decisions, this analysis indicates that donors are paying closer attention to the financial decisions of organizations and are more averse to administrative expenses than they were five years earlier. This study contributes to the existing body of research by making clear that action is necessary – both on the part of donors and on the part of nonprofit leadership.

By examining the results of this research, we can expect that in the future, organizations will continue to strive to meet donor expectations of financial leanness in order to maximize donation revenues. In order to satisfy donors, organizations will opt to neglect infrastructure and/or underreport their financial data on Form 990s. As discussed in the introduction, this behavior perpetuates the nonprofit starvation cycle. Lower levels of overhead and more lean financial behaviors will further enforce donors' unrealistic expectations. Donors will continue expecting organizations to do more with less, and the cycle will continue on. By heeding unrealistic donor expectations and neglecting necessary administrative and organizational spending, nonprofits become more susceptible to dissolution during times of economic hardship. This also limits organizations' access to the technology, staffing, and other resources necessary to have a greater reach in program areas. If donors maintain these misconceptions about nonprofit financial health and behavior, organizations will continue struggling to face financial shocks and will not be able to grow in the ways necessary to address today's societal needs.

Xintong (2022) found that financial distress from disasters increases the likelihood that a nonprofit organization will dissolve or have to restrict program areas. This research found that this is especially the case for smaller nonprofit organizations, and those organizations that do not rely on commercial revenues. This aligns with the findings from this study – smaller organizations face the brunt of the impact of donor overhead aversion and push for financially lean behavior.

As indicated by the analysis above and also discussed by Behn (2010), financial disclosure and meeting donor expectations is significantly easier for larger organizations. Larger organizations are more likely to have the resources and expertise necessary to provide voluntary financial disclosure for donors and the public. For smaller organizations, meeting donor expectations and also providing the desired financial information can be difficult. Smaller organizations must invest in infrastructure and build their capacity to be able to weather financial hardship and economic downturns. This means their financial ratios and spending behaviors can face more scrutiny from donors, as their ratios may be less attractive to donors. The empirical analysis above indicates that smaller organizations face a greater degree of 'punishment' through decreased donations than larger organizations for not meeting donor financial expectations. Their inclusion in the model results in a more negative relationship between the independent variables, our measures of financial health, and the dependent variable, contribution revenues. While donors have good intentions with their financial expectations and simply hope their contributions can go as directly to serving communities as possible, their expectations are having a heavier impact on smaller organizations than on larger ones. Smaller nonprofit organizations need access to the resources necessary to build themselves up and provide more services, foster a more

qualified team, and create a lasting and sustainable organization. This is necessary for our underserved communities and the small nonprofit organizations that seek to serve them.

It is important that donors, information intermediaries, and the general public can access detailed financial statements of nonprofits to ensure that organizations are not spending exorbitant amounts on salary, non-program areas, and infrastructure while neglecting programs and not meaningfully impacting their communities. With that being said, there must also be reasonable, informed expectation levels for nonprofit financial health. All organizations have different missions, growth paths, and needs. Different resources are necessary depending on the organization's goals and the nonprofit's category. For instance, an organization focused on food security will have different administrative and fundraising needs than an environmental advocacy NPO. Nonprofit organizations should be more transparent in communicating their specific needs to donors, and donors should not expect organizations across the spectrum of missions and categories to follow the same rules regarding administrative and fundraising expenses, asset accumulation, revenue diversification, and in other financial behaviors.

Nonprofit organizations are accountable to both donors and their communities. With time and research, it is becoming increasingly evident that successful and impactful organizations must invest in administrative and fundraising costs. Donors should evaluate the way investment in overhead benefits the organization and allows for greater mission attainment rather than judging the performance of an organization by how little it can spend on administrative and fundraising expenses. Funding overhead areas will benefit the organization and its communities in the long run by creating a stronger organizational foundation. Hung et al. (2022) found that overhead aversion is greater with amateur donors than with professional donors. This is owed partially to the fact that professional donors are likely to have more resources and time to

evaluate the financial behaviors and performance of nonprofit organizations. They also likely have a greater understanding of how essential capacity spending is to the success and survival of an organization. These findings suggest that the sector as a whole could benefit from more educated donors. Research such as this is important for this reason – while there has been much research and discussion on the necessity of capacity spending, continuing the discussion will eventually lead to more informed and understanding donors. The public as a whole would benefit from better understanding the way nonprofit organizations function both operationally and financially.

The Importance of Reporting Program Performance

Outcomes, outputs, and impact are key metrics for determining nonprofit performance. This leads to a fundamental issue in the discussion of nonprofit performance – the difficulty of quantifying and reporting nonprofit performance metrics, which is in part a result of neglected overhead. Nonprofits not having clearly outlined performance metrics perpetuates donor dependence on financial measures as a way to gauge impact and performance. The two problems outlined are intrinsically interconnected and result in a vicious cycle – neglected infrastructure (minimized administrative spending) means fewer skilled employees on the team that can focus on measuring and reporting program impact. Lack of impact reporting leads donors and watchdog organizations to rely on financial measures. Studies have empirically proven that the most significant obstacle to reporting program outcomes for nonprofit organizations is a lack of funds and time, indicating staffing and compensation negligence (Mitchell & Berlan, 2016). When donors don't have access to impact measures, they resort to financial (input) indicators of performance. Research by Bodem-Schrötgens & Becker (2020) evaluated the impact of outcome and impact indicators on donative behaviors. The researchers discovered from surveying students

that individuals pay significant attention to information on intermediate and long-term impacts when choosing to donate to an organization. Presenting information on the far-reaching impact of donations increases donative behavior. This allows potential donors to see how their contribution will make a greater impact and allows them to compare these metrics to the work of other similar organizations. If more nonprofits had the capacity and the means to openly disclose performance measures, this would lessen dependence on financial measures as a means of attempting to gauge organizational success and impact. Organizations should focus on demonstrating program outputs and metrics in a meaningful way so that donors are not looking at input measures to interpret efficiency and overall impact. By making it clear to donors that the organization is taking specific action and creating quantifiable outputs with donor dollars, donors will not look to program expenses as a way of interpreting impact. The obvious obstacle of limited funding and staffing makes the shift towards greater impact reporting difficult.

Beyond the difficulty of reporting impact metrics due to limited internal resources, it is also difficult to express in numbers the work carried out by nonprofit organizations. There is also difficulty in quantifying the work that a nonprofit organization does – how do you place a dollar value or really express the impact of providing housing in the community or providing fresh, healthy meals to people who don't have adequate access and resources? An organization could state how many meals or houses were provided, or place a dollar value on the resources utilized, but this is still not a full picture. A healthy meal with fresh, local ingredients is significantly different than a canned meal from a food pantry. Both are hugely beneficial to those in need, but one would require more overhead – a well-equipped kitchen, a team of volunteers, skilled culinary staff. While one minimized overhead and is likely able to funnel a great deal of revenues directly to the purchase of food items, the organization providing balanced and

wholesome meals provides a depth of service that is difficult to quantify. This is the case for many nonprofit organizations across many categories. For instance, the above analysis proves that organizations within the arts subsector face more donor pressure – when included in the model, there is a stronger negative relationship between donations and the measures of financial health used. This is especially interesting given the discussion of the findings by Altamimi and Liu (2021) earlier in the paper. This research found that while donors usually expect a general overhead ratio not exceeding 25%, the average optimal overhead ratio for the arts organizations sampled was 40%. At this point, organizations had the greatest outcomes. This goes to show that financial needs vary across subsectors, and setting specific expectations for financial behavior will not allow donors or the public to accurately gauge the impact of an organization has. The work done by nonprofits meets human needs and improves lives in a complex way. A good starting point in the shift away from analyzing financial behaviors to gauge performance is continuously communicating with donors. By providing a vibrant picture of the work done, donors aren't relying on quantified spending metrics to determine the quality of a nonprofit organization.

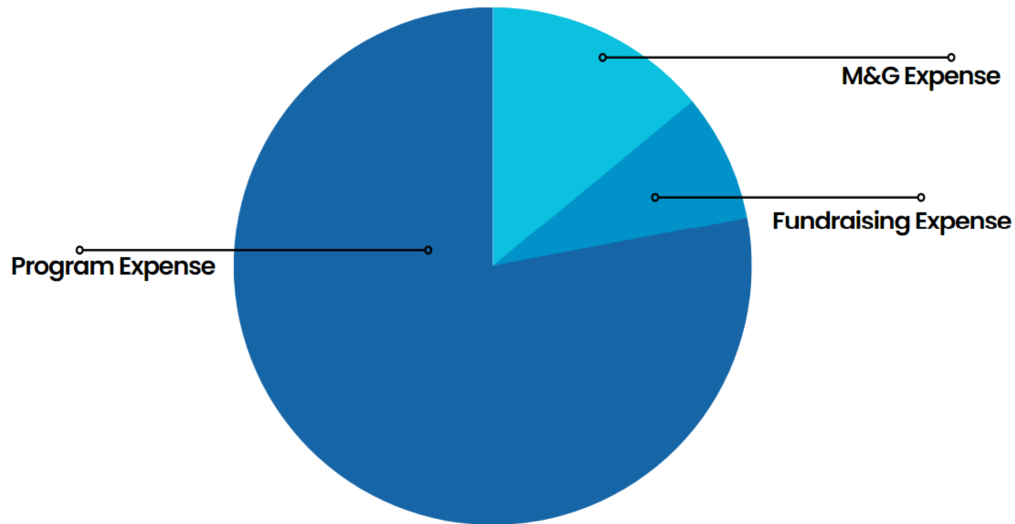
Not only is it difficult to quantify and report performance within a category of nonprofits doing similar work, but it is also not feasible to evaluate and compare nonprofit performance across the board. Eckert & Moulton (2010) addresses the substantial heterogeneity within the sector that makes performance evaluation tools difficult. Organizational impact is "contextual to the influence of specific organizations of community-wide indicators, and are more difficult (if not impossible) to quantify" (p. 100). Reporting program outcomes would be counterproductive if funders evaluated organizations across subsectors based on their performance evaluations. The nonprofit sector is valued for its heterogeneity and wide breadth of service offerings that seek to

address the wide array of society needs that currently exist. For this reason, donors and the public should take caution when comparing performance metrics across organizations and subsectors. There is no ‘one size fits all’ method of evaluating impact or comparing the performance and financial behaviors of nonprofit organizations.

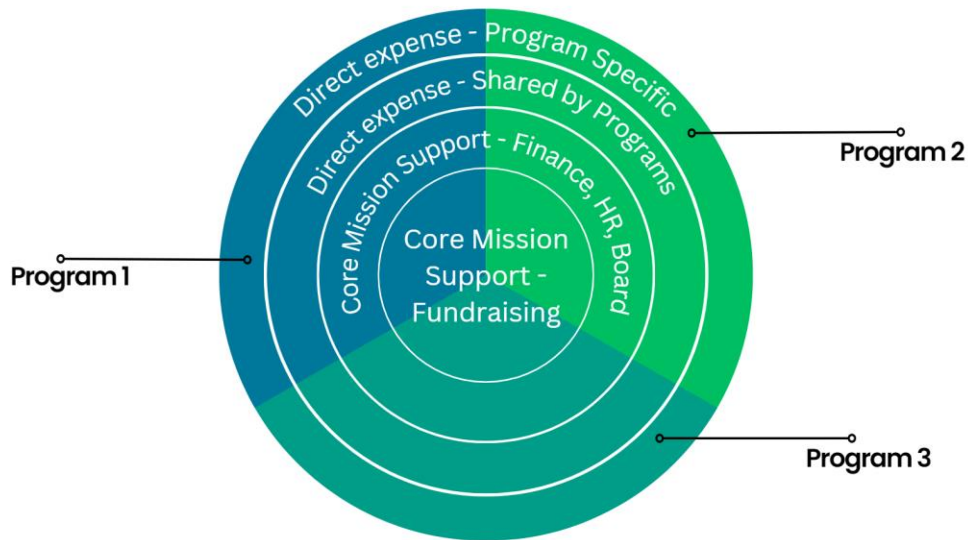
Framing and Discussing Financial Decisions

A way that leadership in nonprofit organizations can level with donors and a meaningful shift in expectations can occur is through more transparent and clear discussion and framing. As indicated by the study carried out by Qu and Daniel (2020), word choice and framing are extremely important in donor decisions. Much of the donor aversion to overhead spending and other infrastructure-focused financial behaviors is due simply to misconceptions and lack of understanding. Many nonprofits are ‘graphically revisioning’ these poorly perceived financial measures by framing them in a way that makes clear to donors and the public why they’re essential to the organization’s success and lend directly to program performance. For instance, nonprofits are using a different graph structure to communicate the role of the different expense categories to donors. During my time interning with a nonprofit environmental advocacy organization in the summer of 2022, the finance team created a chart that depicted how overhead spending was essential to program expense areas – not a separate and unrelated piece of the expense pie.

Traditional Depiction of Nonprofit Expense Areas:



More Accurate Revisioning of Nonprofit Expense Areas:



By reframing overhead expenses – management & general expenses and fundraising expenses – as core mission support, donors are provided a fuller picture of the importance of this kind of spending. Overhead expenses are essential to the foundation of an organization, and program expense build on top of this solid organizational foundation. Overhead expenses are quite literally core to the organization's overall mission. Through this depiction, donors can visualize how line-item funding creates a gap at the core of the organization. When donors contribute specifically to program areas while overhead expenses, or 'core mission support', is neglected, the organization as a whole can crumble. The traditional depiction of organizational expenses makes it appear as if overhead expenses take away from programs, which is simply not a full and accurate picture of how nonprofit organizations' expense areas function. It is understandable why this traditional image led donors to perceive overhead expenses as a waste of funding that could go to programs. Overhead expense is not a piece of the pie that misdirects funding from serving communities and furthering programs, though. This graphic revisioning has been encouraged by Nonprofit Quarterly and other nonprofit management blogs. In order to express the consequences of financial leanness and starved infrastructure to donors, nonprofit organizations need to reconsider the way they present their financial data and communicate their financial decisions with donors. As the donations landscape changes, donor resources must evolve as well. Organizations must reframe the importance of overhead and infrastructure-building financial behaviors in a way that donors will understand. This is essential for the growth of the sector. If nonprofit organizations hope to further their reach within underserved communities and withstand economic shocks through time, they must begin with strengthening the core of the organization and receiving donor support in doing so.

Limitations

There are a few notable limitations of this research, which means that the findings should be interpreted cautiously. As previously mentioned in the paper, a huge and problematic result of lean donor expectations and overhead aversion is nonprofit financial misreporting. Many organizations face pressure to underreport their expenses and non-program spending areas to compete with other nonprofits in the donations market. Qu et al. (2019) found that over 1/3 of nonprofit organizations in the U.S. have financials that deviate from Benford's law, indicating potential fraud. This was found most commonly in organizations reporting very small fundraising and administration expenses and that face stronger funder oversight. Krishnan et al. (2006) found through empirical evidence that the large number of nonprofit organizations reporting zero fundraising expenses is due at least partly to inaccurate reporting. The very high number of organizations with zero fundraising expenses was something I noticed and questioned during my data collection as well. Nonprofits attempt to conform to donors' unrealistic expectations by misreporting on Form 990s. This leads to some financial data that is not reliable. I attempted to mitigate this issue by removing organizations from the sample with negative values, zero values, and expense areas that did not sum to total expenses, but this does not fully control for misreported overhead expense areas, underreported assets, and other modifications. According to Gordon (2007), there are some discrepancies between Form 990 data and the information provided on tax forms. Despite this, 990 data has been generally accepted as the best source of nonprofit financial data available.

Another limitation of this research exists in the scarcity of nonprofit financial datasets. There is no public, easily accessible dataset containing overhead data for nonprofit organizations. This meant I had to manually input fundraising expense and management & general expense

values for all 200 organizations over the two periods. Additionally, NCCS Core data has been said to not be a perfect method for sampling the sector. Mitchell (2017) notes the existence of data extraction errors in the sets, leading to missing observations and some repeated values over multiple year files. I attempted to mitigate the issue of entry mistakes through data cleaning. While the overall accuracy of NCCS data has been called into question, it is the most cohesive and accurate set of nonprofit financial data provided freely and accessibly.

Appendix A: Organizations Included in Sample

EIN	Organization Name
954539145	AMERICAN GOLF FOUNDATION
561134052	VOLUNTEER CENTER OF GREENSBORO INC
520591577	HEARING AND SPEECH AGENCY OF METROPOLITAN BALTIMORE INC
621706248	BOYS & GIRLS CLUB OF GREENEVILLE GREENE COUNTY
592968614	FLORIDA COUNCIL ON COMPULSIVE GAMBLING INC
132941841	WEST BRONX HOUSING AND NEIGHBORHOOD RESOURCE CENTER INC
541635649	FAIRVOTE
731081013	BLUESTEM REGIONAL MEDICAL DEVELOPMENT FOUNDATION
10532230	SCHOODIC ARTS FOR ALL
521603246	NEIGHBORHOOD HOUSING SERVICES OF CAMDEN INC
341831168	WOODLAWN CEMETERY HISTORICAL ASSOCIATION INC
113513108	NYS ASSOC OF TRAFFIC SAFETY BOARDS PROGRAMS INC
562641064	BUILDING A GLOBAL COMMUNITY
112977789	LONG BEACH MIKVEH SOCIETY INC
431943334	GREAT RIVERS ENVIRONMENTAL LAW CENTER
521362103	CHRIST HOUSE
931154632	ELIM OUTREACH MINISTRY
742354492	WESTSIDE CARES INC
131997636	UNITED WAY OF WESTCHESTER AND PUTNAM INC
221726712	VANTAGE HEALTH SYSTEM INC
330962765	IL SHIM SENIOR ASSOCIATION
870509354	FOREVER YOUNG FOUNDATION
841417153	CHURCH PARTNERSHIP EVANGELISM
300455050	PROJECT KNAPSACK INC
202997260	MUSIC FOR EVERYONE
741914638	ROY MAAS YOUTH ALTERNATIVES INC
770051124	MONO LAKE FOUNDATION
330843213	DEVELOPMENTS IN LITERACY INC
346562552	ECONOMIC OPPORTUNITY PLANNING ASSN OF GREATER TOLEDO INC
911744281	TRI-CITIES SUNRISE ROTARY CHARITY
581480175	CHATTAHOOCHEE VALLEY EPISCOPAL MINISTRY INC
20432242	COURT APPOINTED SPECIAL ADVOCATES OF NEW HAMPSHIRE INC
931078791	HABITAT FOR HUMANITY INTERNATIONAL INC
20732028	PHOENIX ACADEMY DAY SCHOOL
370865085	JOSEPH & LOUISE TITUS MEMORIAL PRESBYTERIAN HOME INC
522121856	AMERICAN CIVIL RIGHTS UNION
260734351	NOT FORGOTTEN INC
42774252	MASSACHUSETTS ASSOCIATION OF HEALTH BOARDS INC
46149986	CONSERVATION LAW FOUNDATION INC
310936007	HANCOCK COUNTY SENIOR SERVICES INC

742446158	DOWNING STREET FOUNDATION
742233861	HIGHLAND LAKES FAMILY CRISIS CENTER INC
10857784	KEROSENE LAMP FOUNDATION
205876631	SEA TOW FOUNDATION INC
581762069	GEORGIA CENTER FOR CHILD ADVOCACY INC
411404769	NEW HORIZONS CRISIS CENTER
900149470	ELKTON VOLUNTEER FIRE CO INC
262559147	MAXIMILIAN MONTESSORI FOUNDATION INC
391960514	BEREAN BIBLE INSTITUTE INC
382597776	TENTMAKERS BIBLE MISSION
141867532	CENTER FOR SPIRITUAL RENEWAL
390828504	LABOR AND EMPLOYMENT RELATIONS ASSOCIATION
931266991	WILDLAND FIREFIGHTER FOUNDATION
208461747	SANKATMOCHAN TEMPLE INC
150574854	MINOA FREE LIBRARY
930756960	ROTARY CLUB OF MILWAUKEE COMMUNITY TR
421563295	BAY STATE EQUINE RESCUE INC
382689979	THE MICHIGAN WOMENS FOUNDATION
61662346	LECHAIM CHARITIES INC
990350425	HULA PRESERVATION SOCIETY
61780902	ARTS EVERY DAY INC
10712431	HILLSIDE FOOD OUTREACH INC
541860804	PATHFINDERS FOR GREENWAYS
912160009	LAGUNA BEACH LIVE
10357213	FREEPORT CONSERVATION TRUST
10592853	COLLABORATIVE EFFORT TO REINFORCE TRANSITION SUCCESS INC
431768625	ST LOUIS CARDINALS COMMUNITY FUND
650832961	CAFE OF LIFE INC
710918711	SHUMEI INTERNATIONAL INSTITUTE INC
621608572	OUR DAILY BREAD OF TENNESSEE INC
582045173	BUCKHEAD ROTARY FOUNDATION INC
363492306	WILL-GRUNDY MEDICAL CLINIC INC
630506191	INTERNATIONAL SERVICES COUNCIL OF HUNTSVILLE-MADISON COUNTY INC
383501697	RUTH ELLIS CENTER INC
742523086	BROWNSVILLE ADULT LITERACY COUNCIL INC
56009376	RHODE ISLAND BAR FOUNDATION
310908695	OWSLEY COUNTY HOUSING ASSN
520883435	CHINA OUTREACH MINISTRIES INC
141783039	NEW YORK STATE INDEPENDENT LIVING COUNCIL INC
752571525	HEALTH EDUCATION LEARNING PROJECT H E L P
222088378	PUERTO RICAN ORG FOR COMMUNITY EDUCATIONAL & ECONOMIC DEVELOPMENT
640790065	PRINCE STREET NEIGHBORHOOD PROJECT INC
581197537	FEDERAL DEFENDER PROGRAM INC

541993339	SHENANDOAH VALLEY WORKFORCE INVESTMENT BOARD INC
362936845	ARCS FOUNDATION INC ILLINOIS CHAPTER
202797093	RUBENS CUNHA EVANGELISTIC MINISTRIES
311657019	CASA OF ADAMS & BROOMFIELD COUNTIES INC
263786470	MERCY HEART INC
951042503	MANTECA HISTORICAL SOCIETY
742603325	FISHER HOUSE INC
731125382	HELP IN CRISIS
261425925	GATEWAY SCIENCE ACADEMY OF ST LOUIS
731651475	HIGH COUNTRY BEHAVIORAL HEALTH
942576612	CATHOLIC CHARITIES OF SACRAMENTO INC
262741240	GOODWILL WORKS FOUNDATION INC
956123757	CALIFORNIA STATE UNIVERSITY FOUNDATION
840617651	TLC MEALS ON WHEELS
752687636	ST PAUL CHILDRENS FOUNDATION INC
20669356	VOYAGEURS EXPEDITIONARY SCHOOL
951652919	YOUNG WOMENS CHRISTIAN ASSOCIATION OF GREATER LOS ANGELES CALIFORNIA
20506104	VISION INTERNATIONAL MISSION
223072580	PALS PLUS INC
720954229	VOLUNTEER INSTRUCTORS TEACHING ADULTS INC
586008133	UNITED WAY OF NORTHEAST GEORGIA INC
592713072	OSCEOLA COUNTY HISTORICAL SOCIETY INC
232915763	SALT N LIGHT YOUTH MINISTRY
43454124	LEAP SELF-DEFENSE INC
411290349	CENTRO CULTURAL CHICANO
911586491	PRESBYTERIAN RETIREMENT COMMUNITIES NORTHWEST FOUNDATION
570604034	CLARENDON COUNTY COUNCIL ON AGING INC
630821997	BAY AREA FOOD BANK
352399355	COLINS KIDS INC
222511450	KINGSTON HOSPITAL FOUNDATION
352203762	INSPIRE WOMEN
941728064	COMMUNITY ENVIRONMENTAL COUNCIL INC
593237140	CORNERSTONE BROADCASTING CORPORATION
366101090	CHRISTIAN LEGAL SOCIETY
461472724	HEREFORD SPORTSPLEX INC
275192761	GLOBAL VILLAGE ACADEMY INC
50395601	RHODE ISLAND COMMUNITY FOOD BANK ASSOCIATION
341467793	HUMANE SOCIETY FOUNDATION OF HANCOCK COUNTY
593009352	PUTNAM RADIO MINISTRIES
421490010	ANITA FOUNDATION INC
720883574	WILL WOODS FOUNDATION
204970676	WHEATSTONE ACADEMY INCORPORATED
237101643	THE OHIO ART LEAGUE INC

460366277	CHILDRENS HOME FOUNDATION
222318286	MAIMONIDES HEBREW DAY SCHOOL
800742504	PATHWAY TO FREEDOM INC
330836931	CENTER FOR FAITHWALK LEADERSHIP
364148832	SUPPORTIVE HOUSING PROVIDERS ASSOCIATION
942280033	JOVENES DE ANTANO DEL CONDADO DE
133176952	NAZARETH HOUSING INC
742876270	SAN ANTONIO FOR GROWTH ON THE EASTSIDE INC
953864190	PIONEER MANOR OF GENEVA INC
261572599	NO GREATER SACRIFICE FOUNDATION
133620767	JOHN A REISENBACH FOUNDATION INC
262957409	GROWING SPINE FOUNDATION
202278505	SALVUS CLINIC INC
526054493	LUTHERVILLE VOLUNTEER FIRE COMPANY
232615160	NORTHUMBERLAND FIREMANS RELIEF ASSOCIATION
386090334	MICHIGAN ACCOUNTANCY FOUNDATION
611253192	KENTUCKY HIGHLANDS COMMUNITY DEVELOPMENT CORPORATION
391889252	COMMUNITY LIVING ALLIANCE INC
300732290	ARTISTS AGAINST OPPRESSION INC
830449496	NORTHWEST AGRICULTURE BUSINESS CENTER
251550113	WASHINGTON CHRISTIAN OUTREACH INC
810488863	BLACKFOOT CHALLENGE INC
650611917	SHAKE-A-LEG MIAMI INC
541244769	RONALD MCDONALD HOUSE CHARITIES OF SOUTHWEST VIRGINIA INC
430653270	CATHOLIC CHARITIES OF ST LOUIS
223490986	NEW JERSEY CHAMBER OF COMMERCE FOUNDATION
953253234	COLONIA BARRIOS SENIORS INC
541641580	HERITAGE HUMANE SOCIETY
363385583	STERLING TRACK CLUB INC
710653912	MCGEHEE DESHA COUNTY HOSPITAL FOUNDATIONS INC
10925282	HERO HOUSE
316068733	HILLEL THE FOUNDATION FOR JEWISH CAMPUS LIFE
201434680	WILDLIFE FOR EVERYONE ENDOWMENT FOUNDATION
231653135	COMMUNITY PROGRESS COUNCIL INC
592956529	POLK EDUCATION FOUNDATION AND BUSINESS PARTNERSHIP INC
237054735	FRIENDS OF HISTORIC KINGSTON
137120573	IN HIS IMAGE
770695791	SOMANG SOCIETY
611559832	MEADOWS ARTS AND TECHNOLOGY ELEMENTARY SCHOOL
742135991	COMMUNITY ACTION COMMITTEE OF VICTORIA TEXAS
522173971	PROGRESSIVE TECHNOLOGY PROJECT
56015936	ALUMNI ASSOCIATION OF THE UNIVERSITY OF RHODE ISLAND
260844268	CHESS CLUB AND SCHOLASTIC CENTER OF SAINT LOUIS

392014547	HOPE CHRISTIAN SCHOOLS INC
742783731	CHILDRENS ADVOCACY CENTER OF LAREDO WEBB COUNTY
205205488	SILICON VALLEY COMMUNITY FOUNDATION
200184774	CATHOLIC FOUNDATION OF SOUTH GEORGIA INC
770283072	STORYTELLER CHILDRENS CENTER INC
391779099	VILLAGE OF WAUWATOSA-B I D INC
263521232	LANIER MIDDLE SCHOOL DANCE BOOSTER CLUB
421379026	P E O SCHOLAR AWARDS
236289914	LIBERTY BELL SHRINE OF ALLENTOWN
952145967	CENTURY CLUB OF SAN DIEGO
840679976	LAS ANIMAS HOUSING DEVELOPMENT CO
911931487	CHICAGO FIRE FOUNDATION
411763181	WORLD RELIEF MINNESOTA
223710219	SERVICIOS LATINOS DE BURLINGTON COUNTY INC
841631034	REGIONAL CULTURAL ALLIANCE OF GREATER BIRMINGHAM INC
943361252	GIRLS 2000
352245430	NEW GATEWAYS
946129010	PACIFIC COAST REPRODUCTION SOCIETY
470547017	SANTA MONICA INC
232741739	FOOD MARKETING EDUCATIONAL FOUNDATION
841069605	COLORADO RIVERFRONT FOUNDATION INC
560894222	MDC INC
931159778	DOUGLAS COUNTY CHILDRENS CENTER INC
680257528	CONSORTIUM FOR ENERGY EFFICIENCY INC
742657972	LITTLETON SOCCER CLUB
596002104	CLARA WHITE MISSION
451539816	ALIVEANDKICKN A NEW JERSEY NON PROFIT CORPORATION
136163539	AMERICAN MEDICAL WOMENS ASSOCIATION INC
581480173	MINISTRY SEVEN
592082218	MEMORIAL FOUNDATION INC
30355283	VITAL COMMUNITIES INC

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