

# **The Benefactor: Assessing the Financial Performance of Charitable Organizations**

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## **Abstract**

This project provides students with a simulation of the process used by many private foundations in distributing grants to charities. In particular, the project is based on a fictitious benefactor of a large private foundation who has decided to appoint accounting students to grant-making committees. The committees are responsible for using not-for-profit specific financial performance measures to evaluate local charities and determine which charities should be awarded grants. The charities determined to have the strongest financial performance are awarded operating grants from the private foundation. The project complements traditional lecturing methods by providing a realistic context for introducing students to the importance of the not-for-profit sector and the accounting and financial performance issues faced by charitable organizations.

## **Introduction**

Private foundations are tax exempt entities organized primarily to distribute grants to charitable not-for-profit organizations. Wealthy benefactors interested in philanthropy typically endow private foundations. Examples of some well-known private foundations include the Rockefeller Foundation ([www.rockfound.org](http://www.rockfound.org)), the Carnegie Corporation ([www.carnegie.org](http://www.carnegie.org)) and the Bill and Melinda Gates Foundation ([www.gatesfoundation.org](http://www.gatesfoundation.org)).

After recently winning the lottery your Instructor, the benefactor, endows a hypothetical \$60 million private foundation. The foundation will award grants of \$250,000 each to local charitable organizations. The grants will be used to assist the chosen charitable organizations with day-to-day operations. The benefactor wants to select the grant recipients rather than have individual entities apply for the grants. He/she intends to award a grant to one local 501 (c)(3) entity in each of the following areas of interest:

- Arts, Culture, and Humanities
- Environment/Animal Welfare
- Education
- Health Care/Mental Health and Crisis Intervention
- Food, Agriculture and Nutrition/Housing and Shelter
- Recreation and Sports/Youth Development
- Human Services

The benefactor, who is extremely busy with his/her teaching job, decides to form a Grant Committee in each area of interest. Each committee will determine the grant recipient for that area.

## Requirements

### *Committee responsibilities*

Each committee will:

1. Select two charitable organizations from the local community within a specified area of interest.
2. Evaluate two or more performance dimensions using specific not-for-profit financial performance measures for each of the selected charitable organizations.
3. Recommend which charitable organization should receive the \$250,000 operating grant by identifying the one with the best performance based on the evaluation.

### *Reporting requirements*

Each committee must adequately demonstrate that it has fulfilled each of its responsibilities by completing the following reporting requirements:

1. A comprehensive performance evaluation of the two charitable organizations selected for possible grant distribution must be documented in a professionally written report. The written report should include background information about the two charities selected for evaluation as well as clear identification and evaluation of their performance. Calculations of specific financial performance measures should be presented in an organized fashion.
2. A final recommendation should be clearly stated at the end of the written report. Each Grant Committee should document their justification for selecting the most deserving charity.

## Implementation

Although a lecture-based approach is likely to be the primary method used for teaching not-for-profit subjects, Bonner (1999) concludes that a single method (e.g., lecture only) typically cannot comprehensively achieve all the learning objectives for a given accounting topic. This project complements a lecture-based approach by exposing students to a real-world use of not-for-profit financial information.

The project provides a realistic context for introducing students to the importance of the not-for-profit sector and accounting issues regarding charitable not-for-profit organizations. Students role-play as members of a grant distribution committee of a private foundation responsible for evaluating charitable organizations based on financial performance indicators. The project is appropriate for an upper-division or graduate-level governmental and not-for-profit course or as a component of an advanced accounting course. Within an advanced accounting course, the format of the project is likely to be condensed.

Most accounting students are familiar with financial performance measures used to assess for-profit entities (e.g., income from operations and return on equity as financial performance measures of firm profitability). However, accounting students have not been exposed to the types of performance measures applicable to not-for-profit organizations. One beneficial aspect of this project is that it allows students to use performance measures unique to not-for-profit organizations. These measures are beyond net income and the common ratios typically taught in a financial statement analysis or intermediate accounting course.

Students are required to identify and select charitable organizations from the local community as candidates for a grant distribution from a hypothetical private foundation. This process exposes students to the different types of not-for-profit organizations in existence and their specific areas of interest. Selecting local charities introduces students to charity-specific programs and operations that provide benefits to the local community. Students have an opportunity to learn about the types of financial information created by these charities and how this information may benefit not-for-profit stakeholders, including private foundations. Furthermore, students gain an appreciation for the

importance of charitable organizations, which has the potential to stimulate student learning about not-for-profit accounting topics.

### ***Learning Objectives***

Project-based assignments provide an opportunity for accounting students to learn-by-doing and a means for making accounting education more applicable to the business world. Barron, et al. (1998) argue that it is important to craft a project based on a single driving question in order to make the connections between the activities required within the project-based assignment and the underlying learning objectives. The underlying learning objectives for this project are to provide students with an:

1. Introduction to the role of not-for-profit accounting and financial information in charitable organizations.
2. Opportunity to use analytical skills in calculating and evaluating the financial performance of charitable organizations.

### **Learning objective one: The role of not-for-profit accounting**

The role of not-for-profit accounting is generally a primary learning objective within all not-for-profit accounting courses. This project achieves this first learning objective by providing a realistic context for why not-for-profit accounting is especially important to a primary stakeholder in the nonprofit sector: private foundations.

Private foundations are one of the primary users of financial information created and reported by charities. Foundations are specifically formed to distribute grants to charities rather than provide charity directly. They often use financial performance measures to determine whether a charitable organization is capable of effectively and efficiently using a grant distribution toward its charitable objectives.

Not-for-profit financial performance measures require analysis of accounting information specifically found in the financial statements of charitable organizations. Unlike publicly-traded companies, charities are not required to make their financial statements available to the general public. However, charities are required to file an annual tax return (i.e., IRS Form 990) with the Internal Revenue Service. The IRS Form 990 includes financial information about a charity's activities (i.e., income and expenses) and financial position (i.e., assets and liabilities) as well as non-financial disclosures about program service accomplishments, officer compensation, and the general activities of the organization.<sup>1,2</sup> Financial information may also be available from an organization's website and from interviews with the organization's managers and staff.

### **Learning objective two: Calculate/evaluate financial performance measures**

The main purpose of this project is to calculate and evaluate financial performance measures specific to charitable organizations. Financial performance measures relate to specific dimensions of performance. Students should be familiar with the three common dimensions of liquidity, profitability, and solvency and the financial performance measures associated with each of these dimensions as they are used to evaluate for-profit corporations. For example, for-profit organizations measure profitability using return on assets. These financial performance measures are commonly found in financial accounting and financial statement analysis courses and textbooks.

Charitable organizations do not have owners and therefore do not distribute their profits. Therefore, profitability measures are not always appropriate for charities. However, liquidity and solvency measures are important in a not-for-profit setting. A charitable organization should have adequate liquidity and solvency for operating and sustaining its charitable programs. Charitable organizations also have other types of financial performance measures specific to their organizational form, including financial viability and efficiency (Granof and Khumawala 2011, Wilson et al. 2010, Keating and Frumkin 2001).

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<sup>1</sup> Form 990 was redesigned by the IRS starting in tax year 2008. The current form requires disclosure of financial and non-financial information. More information about Form 990 is available at <http://www.irs.gov/charities/article/0,,id=181089,00.html>.

<sup>2</sup> Guidestar ([www.guidestar.org](http://www.guidestar.org)) provides free access to downloadable IRS Form 990 annual tax returns for most charitable organizations located in the United States.

Although similar in form to for-profit financial measures, students are probably unfamiliar with financial performance measures specific to charitable organizations. These measures are often used by charity oversight agencies<sup>3</sup> and are often included in governmental and not-for-profit accounting textbooks. Table 1 provides a list of not-for-profit financial performance measures commonly found in textbooks and related resources (Panel A) and used by charity oversight agencies (Panel B).

Students are introduced to the primary elements presented in not-for-profit financial statements. In particular, students may learn how revenue recognition issues (i.e., donated goods and services, donor-imposed restrictions, and pledges receivable) and functional expense classifications (i.e., program, fundraising, and administrative expense classifications) specific to charities affect performance measures related to efficiency and financial vulnerability. For example, a charity with a preponderance of donor-restricted contributions may appear financially stable because large amounts of contribution revenues and/or total net assets are reported. However, if these contributions and net assets are restricted for specific purposes, a charity may not have adequate resources to cover operating expenses. Contrary to the initial evaluation, the charity may actually be financially vulnerable.<sup>4</sup>

Finally, instructors may want to include discussions concerning the difficulties of measuring charity performance. In particular, the financial performance measures common to charities provide little or no information about the effectiveness of their charitable programs. For example, a charity may appear to have strong financial performance because it is run in an efficient manner (i.e., total expenses consist primarily of program-related expenses), but may be failing at providing effective services to its beneficiaries. Because profits are less important for charities, other non-financial performance measures may also need to be developed to validly assess the broad objectives of charitable organizations. However, non-financial performance may be difficult or impossible to reliably measure.

#### ***Other Implementation Considerations***

The project is designed as a team project. This allows students to practice team-building, communication, and conflict-resolution skills. Teams of two or three students each are assigned to a grant distribution committee based upon areas of interest. Committees may either select their specific area of interest or the instructor can appoint teams to a specific area of interest. The National Taxonomy of Exempt Entities (NTEE) provides a classification system for charitable organizations that may be used for identifying areas of interest.<sup>5</sup>

If necessary, the project may be abridged and used as an individual student project. As an individual project, students are still introduced to the two learning objectives. However, this approach does not provide the contextual richness available in the team project. With an individual approach, students do not have the opportunity to practice their team-building, communication, and conflict-resolution skills as members of a grant distribution committee organized to make a final grant-making decision. In addition, time constraints are likely to eliminate the opportunity for students to present their final decisions to the class as a whole. As a result, students are less exposed to discourse and constructive criticism from their fellow students (i.e., team-mates and/or student board members) and lose out on some of the benefits gained from the team project approach.

Instructors are encouraged to limit the selection of charitable organizations to the state or local community levels. This familiarizes students to local charities and possibly motivates students to become more interested in their operations. Local charities are often open and candid about describing what their programs are and why these programs are important to their communities. Students should be strongly encouraged to directly contact the local charities they select for initial evaluation to 1) find out more about the organization directly from charity managers

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<sup>3</sup> Charity oversight agencies such as the Better Business Bureau Wise Giving Alliance (<http://www.bbb.org/us/charity/>) and Charity Navigator (<http://www.charitynavigator.org/>) provide specific standards and criteria for evaluating and rating not-for-profit organizations.

<sup>4</sup> This example is provided to demonstrate how the unique methods for recording revenues and expenses affect financial performance evaluation for charitable organizations.

<sup>5</sup> See <http://nccs.urban.org/classification/NTEE.cfm>.

and employees, and 2) promote contact and interest with business leaders and charity providers in the local community.

Students are likely to struggle at the onset of the project and will therefore need some instructor guidance and feedback related to developing an understanding of the performance dimensions and specific measures. The instructor may want to preview the concepts of dimensions and specific financial performance measures before allowing teams to select charitable organizations for evaluation. This preview allows students to think about not-for-profit performance issues while they are selecting charities for evaluation.

The performance evaluation and final recommendation should be formally documented in a professionally written report that includes background information and comparative evaluation of the two charitable organizations selected as operating grant finalists. The comparative evaluation should be based on the dimensions and specific performance measures identified.

As time allows, the initial evaluation and final recommendation for resource allocation may be presented orally at the end of the semester. We suggest the instructor appoint non-presenting committees to act in the role of the foundation board of trustees responsible for asking presenting committee members questions about their presentations and voting for-or-against distribution of the fictitious \$250,000 operating grant. Both the oral presentation and trustee role-playing allow students the opportunity to practice verbal communication skills and to formally advocate and argue a specific position.

Finally, in order to limit the length and time spent on the project and to provide additional structure, instructors may want to place varying restrictions on how the dimensions and specific financial performance measures are selected by students. For example, instructors may limit the performance dimensions to certain types (e.g., efficiency, financial viability) and/or restrict the number of specific performance measures evaluated. Instructors can further compress the time spent on the project by formally providing the dimensions and specific performance measures to be used in completing the project.

### ***Student Reaction to the Project***

We have implemented the project using both the team and individual approaches. Overall, we found a favorable student response to the project using both approaches. Several students documented in their final course evaluations that the project was a positive learning experience. Student comments included the following: “the project was a good experience,” “the project was fun and enlightening,” and “the project was very helpful in applying concepts from class.”

We also received positive anecdotal feedback about the project. For example, one student was formally asked to volunteer as a board of director member for one of the charitable organizations his committee chose for evaluation. One committee was extremely creative during their final oral presentation by using a videotaped “newscast” format. Finally, students were generally surprised how open charitable organizations were in discussing their operations and appreciated the opportunity to directly interact with the local charitable organizations.

To assess the two learning objectives, we also evaluated students’ basic understanding of the charity selected and their use of financial information to evaluate the performance of the charity. Students were required to gain a basic understanding of the charity by collecting information about the charity’s primary exempt purpose, program service revenues, and leadership. Next students were required to compile information from the charity’s IRS Form 990 and calculate and evaluate performance measures related to liquidity (current ratio), financial viability (total liabilities to total assets, unrestricted net asset to expenses), and efficiency (program efficiency, fundraising efficiency). Our assessments indicate that 97% of students met or exceeded our expectations with regard to understanding of the charity selected and 85% met or exceeded our expectations related to compiling financial information and evaluating the performance of a charity. Our assessments provide evidence on student achievement of the two learning objectives.

Overall, both the individual and team approaches are effective at meeting the project's learning objectives. However, the team approach creates a richer context and exposes students not only to accounting-related experiences, but also to "soft" skills such as team building, communication, and conflict-resolution. We proffer that providing accounting students with the opportunity to use these soft-skills within an accounting context is unique and worthwhile. However, we found that the team approach is more difficult to implement and takes more class-time to complete than the individual approach. We recognize that the individual approach may be easier for instructors to implement and for students to complete and we believe that the stand-alone project is a worthwhile compromise for instructors who have limited time.

### Teaching Notes

This project provides students with a simulation of the grant-making process used by private foundations when making charitable distributions. The project requires student teams to complete the two student requirements in order to award a fictitious \$250,000 operating grant to a charitable organization. Here is one suggested approach to completing the student requirements based on analysis of two real not-for-profit organizations.

#### *Student Requirements*

The first responsibility for student teams is the selection of two charitable organizations to evaluate using the applicable financial performance dimensions and measures. In our example, we choose two charities in the Human Service area of interest: Human Services Organization 1 (HSO 1) and Human Services Organization 2 (HSO 2).<sup>6</sup> The two not-for-profit organizations are based on actual charities found in a mid-sized U.S. city.

We suggest the instructor limit the choice of the two charities to a specific area of interest in order to highlight the presence of not-for-profit "industries." Two examples of not-for-profit industry types are not-for-profit hospitals within the Health area of interest and not-for-profit colleges and universities within the Education area of interest. While both types of organizations are considered not-for-profit in nature, they have very different strategic and operating objectives. While most students are cognizant of the heterogeneity associated with financial analysis between for-profit companies in different industries (e.g., the auto industry versus the computer industry), students are probably unaware of industry-specific differences within the not-for-profit sector.

The second responsibility is the identification of performance-related measures used for evaluating charitable organizations. The two sample financial-based performance dimensions are efficiency and financial viability. Efficiency measures are commonly used to assess not-for-profit performance and help determine how well an entity is controlling costs (Granof and Khumawala 2011, Wilson et al. 2010, Keating and Frumkin 2001). Financial viability is defined as the ability of an organization to continue in the future and includes measures related to an organization's long-term debt burden and capacity to support its' charitable programs.

Two specific performance measures have been selected for each of the performance dimensions. Program efficiency and fundraising efficiency measure the efficiency of a charity. Program efficiency is calculated as the percentage of total expenses that are specifically used by an organization in achieving its charitable (i.e., programmatic) goals. Fundraising efficiency captures the efficiency of fundraising efforts by calculating fundraising expenses as a percentage of contribution revenue.

Leverage and adequacy of available resources combined measure the financial viability of a charity. Leverage is computed as total liabilities divided by total assets. Not-for-profit organizations with low leverage are interpreted as more financially viable than organizations with a high leverage. Adequacy of available resources captures the percentage of net assets that are available to a not-for-profit organization for current operating needs and is calculated as unrestricted net assets divided by total expenses. This measure computes the percentage of unrestricted

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<sup>6</sup> The National Center for Charitable Statistics (NCCS) describes the Human Service area of interest as including organizations that raise, distribute, and provide a broad range of social services for individuals or families.

net assets<sup>7</sup> available to pay for current program, fundraising, and administrative expenses. The higher the measure, the more financially stable the organization. Table 2, panel A summarizes the performance dimensions and specific performance measures used in the sample analyses.

An interpretation of the specific performance measures as shown in Table 2, panel A at the beginning of the project is important for at least two reasons. First, the interpretation provides student teams with the methodology for ranking the charities to be evaluated. For example, an interpretation of the program efficiency measure (Table 2 panel A, I) is as follows: an organization with higher program efficiency is more efficient in delivering its programs than an organization with lower program efficiency. Therefore, when student teams actually calculate the program efficiency measure for two charities, teams will have already documented *how* it will determine which charity is performing better on each specific performance measure. Second, the interpretation of each performance measure provides the instructor evidence on whether or not student teams understand the performance measures identified as well as the relation between the specific performance dimensions and specific performance measures. The interpretation provides the linkage between the financial performance dimensions and measures used in evaluating the charitable organizations.

We collected the information used in the sample analysis and needed to calculate and to assess the financial performance measures from two publicly available sources: IRS Form 990 and organizational websites. The specific location of information items used in the sample analysis and found within IRS Form 990 is provided in Table 2, panel B.

Table 2, panel C provides the evaluation results for the financial performance measures pertaining to the two sample Human Service charities. In the sample analysis shown in Table 2, panel C, HSO 2 has higher program efficiency in comparison to HSO 1 (85.5 percent versus 81.1 percent). This means HSO 2 is using a higher percentage of its annual total expenses toward its primary mission. However, HSO 1 has lower fundraising efficiency compared to HSO 2 (13.5 percent versus 33.1 percent), which indicates that HSO 1 is more efficient as a fundraiser.<sup>8</sup> The results for the efficiency performance dimension are mixed based on the two financial performance measures.

In our sample analysis, HSO 2 has much lower leverage than HSO 1 (6.9 percent versus 64.3 percent). In the sample analysis, HSO 2 has higher adequacy of available resources than HSO 1 (73.3 percent versus 19.0 percent). Based on the joint assessment of the leverage and adequacy of available resources measures, HSO 2 has a greater level of financial viability in comparison to HSO 1.

The third (final) responsibility is to recommend which charitable organization should receive the \$250,000 operating grant by identifying the one with the best performance based on the evaluation. HSO 2 has stronger performance measures for three out of the four total financial performance measures assessed in this sample analysis. HSO 2 reports stronger efficiency based on use of the program efficiency measure and is more financially viable in terms of the leverage and adequacy of available resources measures. The \$250,000 operating grant should be awarded to HSO 2 based on the overall evaluation of the financial performance measures.

Although the financial performance measures indicate that HSO 2 is financial stronger, HSO 2 may not be the “best” choice for receiving the grant. For example, although HSO 2 is more efficient at delivering its programs (i.e. program efficiency is better), the organization is less efficient in its fundraising efforts (i.e. fundraising efficiency is worse). This may lead to the following questions. Which function is more important for a not-for-profit organization, the program function or the fundraising function? Even though HSO 2 is more efficient based on the program efficiency measure, is HSO 1 providing more services per dollar raised through fundraising efforts?

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<sup>7</sup> FASB Codification #958-205-05 requires classification of a not-for-profit organization’s net assets into three classes: permanently restricted, temporarily restricted, and unrestricted. This classification is based on the existence (i.e. permanent or temporary) or absence (i.e. unrestricted) of donor-imposed restrictions.

<sup>8</sup> Both organizations have program efficiency and fundraising efficiency measures that exceed the minimum standards established by the Better Business Bureau Wise Giving Alliance (the Alliance). The Alliance recommends a charitable organization spend at least 65% of its total expenses on program activities and spend no more than 35% of related contributions on fundraising.

The comparison between HSO 1 and HSO 2 becomes even more interesting when the respective missions of the two organizations are considered. HSO 1 is a “United Fund” organization with a primary mission of raising funds in the local community to distribute to other human service organizations, while HSO 2 provides social services directly to individuals and families in the local community. These differences highlight the variability of mission-types even within an area of interest, which means any interpretation of the financial performance measures is best driven by the specific mission and operating context present for each organization. These “beyond the numbers” issues may hopefully lead to questions and active discussion when the teams present the final recommendations to the board of trustees.

### ***Conclusion***

As a final point, an instructor may determine that it is important to discuss limitations associated with financial based analysis of charitable organizations. While financial performance measures are relatively reliable and objective, they can also be incomplete. In addition, the use of financial performance measures in a not-for-profit setting suffers because these measures are only indirect measures of social benefit. For example, the conclusion that lower fundraising costs are always better in terms of efficiency is dependent on *the interpretation* of each of the specific performance measures. Some charities have to resort to high-cost fundraising activities in order to receive sufficient public support. For example, a soup kitchen for homeless adults may have greater difficulty in raising funds than a child advocacy program simply because of the types of beneficiaries served. As a result, a soup kitchen might incur much higher fundraising costs to achieve a sufficient level of support.

The operations of not-for-profit organizations are driven by philanthropic and social objectives that are extremely difficult to measure and costly to ascertain. Given this caveat, the evaluation of financial performance for charitable organizations is limited by the effectiveness and reliability of using financial based specific performance measures. The types of questions posed above demonstrate both the strengths and weaknesses associated with both not-for-profit financial performance measures.

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**Table 1**  
**Not-For-Profit Financial Performance Dimensions and Measures**

**Panel A: Dimensions and Measures Identified in Commonly-Used Textbooks and Other Resources**

- Liquidity
  - Current ratio (Current Assets / Current Liabilities)<sup>1,2</sup>
  - Quick ratio (Quick Assets / Current Liabilities)<sup>1,2</sup>
- Efficiency
  - Program efficiency
    - Program Expenses / Total Expenses<sup>1,2,3</sup>
    - Program Expenses / Number of Clients Served<sup>1</sup>
    - Program Expenses / (Fundraising Expenses + Administrative Expenses)<sup>2</sup>
  - Fundraising efficiency
    - Public Support / Fundraising Expenses<sup>1</sup>
    - Fundraising Expenses / (Contributions + Special Event Revenue)<sup>2,3</sup>
- Financial viability
  - Leverage
    - Total Liabilities / Total Assets<sup>1,2,3</sup>
    - Total Liabilities / Net Assets<sup>1</sup>
  - Adequacy of available resources
    - Unrestricted Net Assets / Operating (Total) Expenses<sup>1,2</sup>
    - Revenue, Support, Gains + Interest / Annual Debt Service Expense<sup>1</sup>
  - Others
    - Revenues / Expenses<sup>1,2</sup>
    - Administrative Expenses / Total Expenses<sup>3</sup>
    - Comparison of Budgeted and Actual Revenues and Expenses<sup>2</sup>
- Other financial performance dimensions and measures
  - Investment performance
    - Budgeted Total Return on Investments / Actual Total Return on Investments<sup>1</sup>
  - Revenue concentration:
    - Percentage of revenues from contributions and grants<sup>2,3</sup>
    - Percentage of revenues from program service revenue<sup>2,3</sup>
    - Percentage of revenues from investment income<sup>3</sup>

<sup>1</sup> See Wilson, Kattelous, and Reck (2010)

<sup>2</sup> See Granof and Khumawala (2011)

<sup>3</sup> See Keating and Frumkin (2001)

**Table 1**  
**Not-For-Profit Financial Performance Dimensions and Measures (continued)**

**Panel B: Dimensions and Measures Used by Charity Oversight Agencies**

Charity Navigator<sup>1</sup>

- Organizational efficiency
  1. Program efficiency: Program Expenses / Total Expenses
  2. Administrative efficiency: Administrative Expenses / Total Expenses
  3. Fundraising efficiency: Fundraising Expenses / Total Expenses
  4. Cost of fundraising: Fundraising Expenses / Total Direct Public Support
- Organizational capacity
  1. Primary revenue growth:  $[(Y_{t=1}/Y_{t=3})^{(1/n)} - 1]$ , where  $PR_{t=1}$  is primary revenue (all non-investment revenues) measured in the first year of the interval analyzed,  $Y_{t=3}$  is the primary revenue (all non-investment revenues) measured at the end of the interval analyzed, and n is the length of the interval in years
  2. Program expense growth:  $[(Y_{t=1}/Y_{t=3})^{(1/n)} - 1]$ , where  $Y_{t=1}$  is program expenses measured in the first year of the interval analyzed,  $Y_{t=3}$  is program expenses measured at the end of the interval analyzed, and n is the length of the interval in years
  3. Working capital ratio: (Current Assets – Current Liabilities) / Total Expenses

BBB Wise Giving Alliance<sup>2</sup>

3. Financial performance (generic)
  - a. Spend at least 65% of its total expenses on program activities: Total Program Services Expenses / Total Expenses [Administrative Efficiency]
  - b. Spend no more than 35% of related contributions on fundraising: Total Fundraising Expenses / Total Related Contributions [Fundraising Efficiency]
  - c. Unrestricted net assets should be no more than 3 times the size of the past year's expenses or 3 times the size of the current year's budget, whichever is higher [Financial Need]

<sup>1</sup> See <http://www.charitynavigator.org/>

<sup>2</sup> See <http://www.bbb.org/us/charity/>

**Table 2**  
**Sample Analysis**

**Panel A: Financial Performance Dimensions and Measures Used in the Sample Analysis**

<b>Performance Dimension</b>	<b>Specific Performance Measures</b>	<b>Calculation of Specific Performance Measure</b>	<b>Interpretation of Specific Performance Measures</b>
I. Efficiency	1. Program efficiency	Program Expenses / Total Expenses	Higher program efficiency indicates the organization is more efficient in delivering its programs
	2. Fundraising efficiency	Fundraising Expenses / (Contribution Revenue + Special Event Revenue)	Lower fundraising efficiency indicates the organization is more efficient in its fundraising endeavors
II. Financial viability	1. Leverage	Total Liabilities / Total Assets	Lower leverage indicates the organization has less debt burden
	2. Adequacy of available resources	Unrestricted Net Assets / Total Expenses	Higher adequacy of available resources indicates the organization has adequate unrestricted reserves

**Panel B: Location of IRS Form 990 (Redesigned) Information Used in the Sample Analysis**

<b>Line Item Name</b>	<b>Specific Location on IRS Form 990</b>
<ul style="list-style-type: none"> <li>• Revenues and Expenses               <ul style="list-style-type: none"> <li>Contribution revenue (direct public support)</li> <li>Special event revenue</li> <li>Program expenses</li> <li>Fundraising expenses</li> <li>Total expenses</li> </ul> </li> <li>• Assets, Liabilities, and Net Assets               <ul style="list-style-type: none"> <li>Total assets</li> <li>Total liabilities</li> <li>Unrestricted net assets</li> </ul> </li> </ul>	<p>Part I, line 8; Part VII line 1h. Part VIII, line 7a. Part IX, line 25 (column B). Part I, line 16; Part IX, line 25 (column D). Part I, line 18; Part IX, line 25 (column A).</p> <p>Part I, line 20; Part X, line 16. Part I, line 21; Part X, line 26. Part X, line 27</p>

**Table 2**  
**Sample Analysis (continued)**

**Panel C: Final Evaluation of Financial Dimensions and Measures Used in the Sample Analysis**

Performance Dimensions and Specific Performance Measures	Human Service Organization 1 (HSO1)	Human Service Organization 2 (HSO2)	Conclusion
I. <u>Efficiency</u> Program efficiency Fundraising efficiency	81.1% 13.5%	85.5% 33.1%	HSO2 > HSO1 HSO1 > HSO2
II. <u>Financial Viability</u> Leverage Adequacy of available resources	64.3% 19.0%	6.9% 73.3%	HSO2 > HSO1 HSO2 > HSO1