VenturaCountyStar

Nonprofits facing high demand, tough choices

Thursday, June 11, 2009

- The number of nonprofits serving Ventura County residents has almost tripled over the last three years. We all can see that as a net positive for our communities, with a cumulative impact of $1.5 billion annually.

These organizations sprang up during times when charitable dollars were more plentiful. Now, we have to ask the question: How many of these newly minted nonprofits, and even their established counterparts, can transition to less-forgiving times?

The recent market declines have real and painful consequences for operating budgets of nonprofits and their ability to attract the funds needed to do important work. And it isn't just fundraising that gets tough in this challenging economy. Nonprofits often rely on charitable endowments to cover some of the cost of their programs and even operating expenses. With endowments invested in the markets, the amount the charities can draw from these funds will drop markedly in light of the massive market declines in recent months.

Long seen as anchors to windward, endowment funds are the cushion against fluctuations in donations by providing annual contributions to operating budgets that sustain a charity's mission.

Now, in an ironic twist, that cushion is much thinner at a time when donors are feeling cautious about giving money to a charity when their own families' financial security has them concerned.

And our sector has been dealt another blow. For some nonprofits, the delays in the state budget in Sacramento have had a catastrophic effect. The delay meant charities that contract with the state government suffered major disruptions of their cash flow. Further cuts in the state budget will imperil programs that aid those most disadvantaged or destabilized by the sharp economic decline in recent months — some of which might be mitigated by federal stimulus dollars, but for how many, and for how long?

Recalibrating to this new level of ongoing financial support requires boards and local nonprofits to question past assumptions and plan for a less-expansive future. And it's not going to be easy because these are tough decisions.

Many local agencies lack significant operating reserves, putting even more pressure on staff and fundraising efforts. Nonprofit staff members, already balancing a full plate, now find themselves facing more demand for services as Ventura County residents cope with unprecedented unemployment and foreclosure rates.

Board members are having difficult conversations about budgets, about fundraising and the impact on the future of their agencies. Instead of overseeing their organization's growth, they are forced to leave positions unfilled, cut programs and even order layoffs.

In this environment, endowments may look like an attractive source of needed funds, particularly if painful budget choices loom. But true endowments are not reserve funds, and many were established to prevent access to principal, even in tough times. They are designed to be there for the long haul, far beyond even these extraordinary times. Donors established them to be preserved well into the future, not to be raided with the winter storms.

As we consider the possibility of future years of flat or negative growth, we must also look at the impact from future distributions. In the 1980s, many nonprofits adopted what later became known as the Yale plan, using a 5 percent annual rate of distribution that would preserve the core principal value — even after adjustments for inflation and fees — well into the future.

But now that we no longer face consistent bull markets, this 5 percent annual distribution must be balanced against the responsibility to preserve endowments in ways that respect the express intent of the donors. Some large foundations are looking at 3.5 or 4 percent annual distributions, to ensure the core remains for future use.

At the local level, with declines in values of 25 percent or more, nonprofits must adjust to a more sustainable level of operating contributions from endowments until growth returns to their portfolios. Expectations for year-to-year growth in portfolios need to shift to more moderate levels. Boards must be more cautious about commitments, staff more diligent in their expenses and the effort to identify new sources of funding takes on new urgency.

Even if nonprofits make these hard choices, the current environment will still force many nonprofits to take a breather until the resources catch up again with every nonprofit's dreams of creating healthier, more hopeful communities.

The impact on those served will be real, but some form of adjustment and realignment in our current nonprofit community seems inevitable. The good news is that both boards and staff have access to help weather these changes.

Next: VCCF can help with navigating these changes.

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(This is the second in a three-part series written by Hugh Ralston regarding nonprofits. His first commentary, “Nonprofits focus on long-term investments,” ran June 7. — Editor)