UF IFAS Extension UNIVERSITY of FLORIDA

UF/IFAS PEER REVIEWED FCS3371

https://doi.org/10.32473/edis-FY1510-2022

Nonprofit Revenue Generation[1]

Micayla Richardson, Marlen Barajas Espinosa, Jennifer Jones, and Kimberly Wiley[2]

Nonprofit organizations rely on multiple types of revenue, including program fees, donations, and earned income. It is a commonly held belief that nonprofits should seek as much diversity in their revenue streams as possible (Hager & Hung, 2020). Benefits of this revenue diversification include flexibility, autonomy, and community embeddedness. However, having too many revenue streams can lead to increased risk and vulnerability (Fulop, 2012). Additionally, diversification of funding sources can increase administrative costs. Instead, the organization needs to be strategic. Not all sources of revenue are appropriate for all organizations. Therefore, nonprofit leaders must decide which revenue sources make the most sense for their organization. This publication was designed to help nonprofit organizations develop a strategic revenue generation plan that aligns with their mission and organizational capacity. The publication discusses steps in choosing a revenue strategy, as well as common mistakes to avoid.

Step 1: Examine how your revenue sources vary.

The nonprofit sector consists of mission-focused subsectors such as human services, environment and animals, public/societal benefit, health, and arts and culture (NCCS Project Team, 2020). Each subsector has its own "typical" revenue structure. For example, religious organizations rely primarily on donation and program revenue, while health organizations rely primarily on program revenue (California Association of Nonprofits & The Nonprofit Institute, 2019; Jones et al., 2016). Health organizations that provide patient care typically charge co-pays and bill insurance to cover health care delivery costs. In contrast, it would not make sense for a hospital to rely primarily on donations when their natural source of revenue is fee-for-service.

Therefore, the first step in generating an optimal revenue plan for your organization is to benchmark your organization against others in your subsector. You can do this by reviewing the latest report for your region or by looking at reports for similar regions. A list of reports is available (National Council of Nonprofits, 2022). Additional resources include 990 tax forms and Guide Star profiles. Then, compare the numbers on the report to your organization. If you do not know your current revenue breakdown, review Part VIII of your most recent IRS Form 990 or the organization's most recent annual report. The goal is not to mirror your subsector, but to consider how and why your organization might be different and whether your revenue breakdown should change at all.

Step 2: Evaluate the autonomy of revenue sources.

There are benefits and challenges to each revenue type and source. One way to examine the benefits and challenges

1. This document is FCS3371, one of a series of the Department of Family, Youth and Community Sciences, UF/IFAS Extension. Original publication date May 2022. Visit the EDIS website at https://edis.ifas.ufl.edu for the currently supported version of this publication.

2. Micayla Richardson, research assistant, Department of Family, Youth and Community Sciences; Marlen Barajas Espinosa, research assistant, Department of Family, Youth and Community Sciences; Jennifer Jones, assistant professor, Department of Family, Youth and Community Sciences; and Kimberly Wiley, assistant professor, Department of Family, Youth and Community Sciences; UF/IFAS Extension, Gainesville, FL 32611.

of funding sources is to analyze the nonprofit's level of autonomy in choosing how to use that money (Pratt, 2002). High-autonomy revenue sources give the organization the most choices. These sources include small- to medium-sized individual contributions, endowments, memberships, fees for services, and foundation operating grants. Medium-autonomy sources give the organization some flexibility, but come with important stipulations. These sources include larger individual contributions and corporate charitable contributions. Finally, low-autonomy sources give the organization no choice in how to use the money. They include party reimbursements, government project grants, ongoing government contracts, and foundation project grants.

Autonomy is critical. An organization cannot survive on low-autonomy sources alone because it will not be able to pay for expenses that are not approved for those sources. For example, low-autonomy funding may cover program expenses, but the organization would also need high-autonomy funding for overhead and utilities.

Thus, the second step is to examine the degree of funding autonomy with your current revenue mix and identify whether you need more autonomy. You also want to identify whether your current organizational capacity is enough to manage the stipulations from various funding sources. Multiple sources of revenue, especially those low in autonomy, require a high organizational capacity (Searing, Wiley, & Young, 2021; Wiley, 2020). For example, you might need to hire more finance staff or purchase a better software program to ensure that funds are used appropriately.

Step 3: Identify "natural" funding streams based on your organization.

Each organization will have natural funding streams based on its mission and capacities. A natural funding stream is a stream that fits the organization's unique position in the community. For example, a community health organization may sell health education courses. This is a natural funding stream because it draws upon that organization's unique capacities. Similarly, a hospital's natural funding streams would likely be program service fees paid by patients, insurance companies, and the government.

The third step in developing an optional revenue model is to consider your organization's mission and capacities to identify new funding streams. You will want to ask questions such as:

- Who (or what institutions) are the natural stakeholders of this mission?
- Who benefits from achieving this mission?
- What are our core capacities?
- What resources do we have to share?

For example, leaders of a small nonprofit farm might address the questions above as follows. They might identify the natural stakeholders as their customers (individuals, restaurants, grocery stores), the local government, and business communities. They might identify the beneficiaries as their customers, the local community, and future generations. They might consider their core capacities to be farming in general, farming heirloom tomatoes specifically, and educating consumers about the value of community-based agriculture. They might also identify the following resources to share: farmland, gazebo space, and food processing equipment. After answering these questions, the leaders might realize they could incorporate new revenue streams. For example, they might consider pursuing a small business grant, teaching classes on how to grow heirloom tomatoes, or renting out their gazebo for birthday parties or weddings.

Step 4: Develop your funding model.

Once you have examined the variation of revenue by subsector, considered the autonomy of your funding sources, and identified new funding sources based on your unique organization, it is time to develop your revenue model. A revenue model is a "methodical and institutionalized approach to building a reliable revenue base that will support an organization's core programs and services" (The Bridgespan Group, 2021). It is as simple as identifying what percentage of the organization's revenue will come from which sources. Doing the work of the first three steps will allow you to make these decisions strategically rather than clamoring for every available dollar.

The fourth step is to develop your optional revenue model. You can create this based on the first three steps. Alternatively, if you would like some examples to follow, scholars have identified funding models (Foster, Kim, & Christiansen, 2009; The Bridgespan Group, 2021). Foster, Kim, & Christiansen (2009) developed ten funding models: Heartfelt Connector, Beneficiary Builder, Member Motivator, Big Bettor, Public Provider, Policy Innovator,

Beneficiary Broker, Resource Recycler, Market Maker, and Local Nationalizer. Each model varies based on the organization's mission and natural funding sources. For example, a Heartfelt Connector organization appeals easily to donors (e.g., a feed-a-child program). A Public Provider organization provides services typically paid for with government funding (e.g., homeless shelters). These models are a general guide that can help you understand what revenue streams make the most sense for your organization.

Mistakes to Avoid in Developing Revenue Streams

Leaders commonly make three mistakes as they work to determine the best revenue mix for their organization.

Letting the Mission Drift

Nonprofits may alter their mission or programming to meet the needs of grant funding. This can lead to a short-term increase in funding. In the long term, it is expensive and can deter the organization from accomplishing its mission. For example, imagine a farmers' association that operates a sustainable agriculture certification training. The program teaches that environmentally sustainable agricultural practices reduce environmental pollutants. The organization wants to apply for a youth association grant, but it would have to add a separate program involving youth. A youth program may be aligned with the organization's mission, but it adds a population not specified by that mission. This adds organizational expenses and responsibility that may not be worth the cost.

Glorifying Earned Income (Social Enterprise)

Social enterprise is a term used to describe a continuum of commercial activity related to a social mission (Jones & Donmoyer, 2015; Jones, Kraysnska, & Donmoyer, 2021). At one end of this continuum are for-profit businesses developed to raise and funnel money into nonprofit organizations (e.g., Newman's Own). On the other end of this continuum are social programs that raise money as part of achieving their mission (e.g., Girl Scout cookie sales). At face value, earned income is highly sought-after. Many funders recommend it as a way to develop a steady and autonomous funding stream. Most nonprofit organizations already have earned income revenue streams. However, most organizations are not equipped to rely primarily on earned income activities for a number of reasons. For example, the nonprofit may not have the skill set to manage a business or may find it cost-prohibitive to run a business that also addresses its social mission. Earned income is good, but it is not advisable to assume earned income is the only or best revenue source.

Misusing Debt

Some funding sources pay in reimbursements rather than provide upfront costs. In this case, the organization is required to fund the program; the payment finally arrives once the program is completed. Leaders often turn to debt to manage the grant until funding arrives. This is dangerous and can lead to insolvency. In contrast, a strong nonprofit organization will: project its cash flow over the year; accept reimbursement funding only if it can afford to cover the program costs until reimbursed; and have sufficient operating reserves on hand to cover months where cash flow is negative. In this case, the nonprofit leaders maintain their fiduciary duty to their organization by becoming financially resilient and developing surpluses to protect the organization during the ebb and flow of funding (Hager & Searing, 2014).

Conclusion

While it may be tempting to pursue all revenue streams, organizations should emphasize reliability and autonomy rather than diversity of sources. Specifically, nonprofits should focus on the reliability of revenue sources to "increase resiliency, adaptability, and fuel innovation" (Fulop, 2012). This can be achieved in four steps: compare your revenue sources to other organizations' revenue sources within your nonprofit subsector, evaluate the autonomy of revenue sources, identify "natural" funding streams based on your unique organization, and develop your funding model. The goal is to ensure funding is reliable and can be used to meet the organization's needs.

References

The Bridgespan Group. (2021). Funding Models. https://www.bridgespan.org/insights/library/nonprofit-management-tools-and-trends/funding-models

California Association of Nonprofits & The Nonprofit Institute. (2019). Causes Count: The Economic Power of California's Nonprofit Sector. https://calnonprofits.org/publications/causes-count

Foster, W., Christiansen, B., & Kim, P. (2009). Ten Nonprofit Funding Models. Stanford Social Innovation Review. https://www.bridgespan.org/bridgespan/images/articles/2009sp-feature-foster-kim-christiansen/2009SP_Feature_Foster_Kim_Christiansen-(1).pdf

Fulop, M. (2012). Seven Principles for Building a Nonprofit Revenue Model. Facilitation & Process. http://facilitationprocess.com/seven-principles-for-building-a-nonprofit-revenue-model/

Hager, M., & Hung, C. (2020). Is Diversification of Revenue Good for Nonprofit Financial Health? *Nonprofit Quarterly*. https://nonprofitquarterly.org/is-diversification-of-revenue-good-for-nonprofit-financial-health/

Hager, M. A., & Searing, E. A. M. (2014). 10 Ways to Kill Your Nonprofit. *Nonprofit Quarterly*. https://nonprofitquarterly.org/10-ways-to-kill-your-nonprofit/

Jones, D. (2019). National Taxonomy of Exempt Entities (NTEE) Codes. https://nccs.urban.org/project/national-taxonomy-exempt-entities-ntee-codes

Jones, J. A., & Donmoyer, R. (2015). Multiple Meanings of Social Entrepreneurship and Social Enterprise and Their Implications for the Nonprofit Field. *Journal of Nonprofit Education and Leadership*, *5*(1). https://js.sagamorepub.com/jnel/article/view/6171

Jones, J. A., Hunter, C. J., Irani, T. A., Kumaran, M., Lindsey, A. B., & Pracht, D. (2016). *The Pulse of the Sector: Nonprofit Organizations in North Central Florida.* Gainesville: University of Florida Institute of Food and Agricultural Sciences.

Jones, J. A., Krasynska, S., & Donmoyer, R. (2021). Mission-First Social Enterprises: A Case Study of How Three Nonprofit Organizations Avoided Mission Drift When Forming and Operating Social Enterprises. *International Journal of Nonprofit and Voluntary Sector Marketing*, *26*(4), e1701. https://doi.org/10.1002/nvsm.1701

National Council of Nonprofits. (2022). Research, Reports, and Data on the Nonprofit Sector. https://www.councilofnonprofits.org/research-reports-and-data-the-nonprofit-sector

NCCS Project Team. (2020). The Nonprofit Sector in Brief 2019. *The Urban Institute*. https://nccs.urban.org/publication/nonprofit-sector-brief-2019

Pratt, J. (2002). The Dynamics of Funding: Considering Reliability and Autonomy. *Nonprofit Quarterly*. https://nonprofitquarterly.org/the-dynamics-of-funding-considering-reliability-and-autonomy/

Searing, E. A., Wiley, K. K., & Young, S. L. (2021). Resiliency Tactics during Financial Crisis: The Nonprofit Resiliency Framework. *Nonprofit Management and Leadership, 32*(2), 179–196. http://doi.org/10.1002/nml.21478

Wiley, K. (2020). Implementing Domestic Violence Policy: When Accountability Trumps Mission. *Affilia*, *35*(4), 533–551. https://doi.org/10.1177/0886109919894649