



Don't shy away from discussing overhead costs

One of the duties of a nonprofit's board of directors is to ensure that the organization has adequate resources to fulfill its mission.

These resources include administration of the organization, which some people call unallocated costs and others call overhead.

Challenging economic times bring these costs into sharp focus. Donors ask more questions, especially about overhead and fundraising costs.

Sadly, too many nonprofits do not account for these costs properly and, therefore, cannot give accurate answers.

Overhead costs are the on-going expense of running an organization. Lumped into these costs are those things that are necessary but are not directly related to program or service delivery. These costs include rent, utilities, payroll taxes and employee benefits. Even those organizations with no paid staff have annual regulatory filing fees, insurance costs, and the costs of telephone, Web site and postage. All nonprofits have fundraising expenses.

There are direct and unintended consequences to not funding administrative costs adequately. These include low pay and benefits that contribute to high staff turnover; hiring and training staff is very expensive. Moreover, compensation

affects the ability to attract people with the right talent to fill needs in the organization. In addition, some organizations have inadequate computer systems because they are using a collage of used, donated equipment, and other organizations rent inadequate facilities.

If all of these conditions were present in an organization, it would be able to report low overhead costs, and, sadly, low scores on effectiveness. Are organizations with the lowest overhead costs the best stewards of donations?

The National Center for Charitable Statistics found that you get what you pay for (www.coststudy.org). Nonprofits that limit spending on administration and fundraising are less effective than comparable organizations. Furthermore, pressure to report low overhead costs leads to misrepresentation of the true cost of delivering a program or service. So how much overhead cost is too much? The American Institute of Philanthropy, an industry watchdog, holds that 40 percent or more for overhead is too much. (www.charitywatch.org/tips.html). This is not true for a fundraising special event, however. It is common for the cost of the event to be half of the amount raised.

Ellison Research conducted a study in early 2008 and found that Americans think nonprofits spend 36 percent on

overhead, but believe that spending 22 percent is reasonable

(www.ellisonresearch.com/releases/0208_ERWhitePaper.pdf).

How can a nonprofit counter the pressure to reduce overhead costs? The nonprofit consulting firm Bridgespan Group (www.bridgespan.org) suggests that nonprofits become more proactive. First, organizations need to develop a strategic plan that explicitly recognizes infrastructure needs; framing discussion on what is needed to achieve goals is more productive than focusing entirely on costs. Second, everyone in the organization needs to understand the rationale and benefits of spending on overhead; complete internal buy-in reinforces the value to donors and prospective donors. Last, because it's difficult to compare individual organizations, nonprofits need to benchmark their spending against sector or industry averages. Most important is that spending be measured against goal attainment.

In this time of growing need and unstable funding, it is vital that nonprofits be honest with themselves and with donors about what it costs to provide programs and services. This is not the time to be afraid to talk about overhead costs.

Resource Use

- Support nonprofit leadership
- Board development/training
- Strategic planning

Nonprofit Business Column of The Tribune

The San Luis Obispo Tribune publishes a column every other week in the Business section dedicated to the business practices of nonprofit orgs. Barry VanderKelen, Executive Director of the San Luis Obispo County Community Foundation writes the bi-

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