

The Best Ways to Increase Efficiency



New research provides insights into boosting performance.

By Miriam Sowinski & Zach Garretson

Nonprofit organizations are always looking for newer, better ways to allocate resources efficiently. But is there a way to measure and predict such efficiency?

Seeking an answer to that question, the United Way of Northeast Florida (UWNF) partnered with the University of North Florida to gauge efficiency in the nonprofit sector. The university's Department of Accounting and Finance analyzed UWNF's tax and audit documents to see if there was any predictability in the performance of the 70 organizations' UWNF funds.¹

As is common at most universities, graduate students participate at the ground level of research by gathering data and providing preliminary reports. Although the larger study is incomplete, we as students used the information gathered thus far to devise a regression analysis for predicting nonprofit efficiency.²

Analysts know they can't measure

Aim to limit the growth of your infrastructure.

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nonprofits' and for-profits' performance the same way. For-profits focus on growth and earnings, while nonprofits aim for maximum efficiency of operations. Like most charitable organizations, UWNF management is concerned with what percentage of donations actually go to the cause. In fact, the rating system used by Charity Navigator (which awarded UWNF its highest rating of four stars) measures nonprofits according to such factors as program expenditures and fundraising efficiency.

In agreement with this standard, we considered program expenditures to be the key output in our study. Therefore, we measured the performance of UWNF-funded organizations by how efficiently they convert revenues to program expenditures. We define "efficiency" as the ratio of program expenditures to total revenue.³ The higher

this program-expenditure/revenue ratio is, the more efficient the organization is likely to be.

What the Research Shows

For a preliminary study, the results were pretty impressive. Three variables were significant in predicting organizational efficiency:

- 1. Whether the organization has a national charter.** Local-only organizations have program-expenditure/revenue ratios 13.4% higher than nationally-chartered nonprofits.⁴ Since local groups may have more knowledge of local needs, they may be more efficient when allocating funds to programs. Also, the infrastructure in national organizations may pull more funds away from program expenditures. Thus, organizations with national charters spend less on programs than local-only charities. This is an important finding, especially since watchdog organizations (such as Charity Navigator and GuideStar, which track nonprofit organizations and provide information on their performance) generally review nationally-chartered organizations and largely ignore local ones.

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2. The size of the organization's infrastructure as measured by its property, plant, and equipment expenditures. As these expenses increase, the organization's ratio of program costs to total revenues decreases. Clearly, the high expense of maintaining large infrastructures can lower the amount of funds allocated to programs.

3. The organization's "current ratio" (its assets divided by its liabilities). The "current ratio" is an accounting standard that measures an organization's financial strength. When assets are divided by liabilities, the ratio should be close to 1.0. If it drops below 1.0, the organization's ability to pay its bills is impaired. If it's too much greater than 1.0, the organization isn't using its assets efficiently.

How to Translate these Findings into Better Practices

Although our sample is just a preliminary snapshot, you can still draw some crucial conclusions:

- **Try to keep your current assets and liabilities about equal.** If you have too many liabilities, you risk financial instability. But if you have too many assets, you may be stockpiling cash rather than using it to improve your programs.
- **Aim to limit the growth of your infrastructure and your property, plant, and equipment expenses.** Organizations with large infrastructures generally use money less efficiently than those with small infrastructures.

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• **If yours is a national organization,** do all you can to listen to, facilitate communication with, and give authority to local chapters, which may be able to help you increase efficiency.

It's not surprising that the United Way of Northeast Florida received a four-star rating from Charity Navigator. It would be great to see more organizations adopting this organization's proactive attitude in analyzing which factors contribute to overall efficiency.

It's also good to remember that universities can assist nonprofits by initiating studies that otherwise would be infeasible due to funding limitations. If your organization needs help in conducting research, consider contacting the appropriate department of your nearest university. Such collaborations benefit everyone involved and can edify the entire nonprofit sector. ■

Put These Results to Use

To apply this research to your organization, see these *Nonprofit World* articles (www.snpo.org):

- **Do You Have Enough Cost Information to Make Good Decisions?** (Vol. 15, No. 6)
- **Nonprofit Doesn't Have to Mean Noncomfortable** (Vol. 18, No. 2)
- **Performance-Based Management Builds Funding & Support** (Vol. 23, No. 6)
- **Analyze Your Finances to Ensure Your Mission** (Vol. 19, No. 5)
- **Seven Steps to Forming New Chapters** (Vol. 14, No. 6)
- **Universities Offer Marketing Research Key** (Vol. 4, No. 1)
- **Evaluating Nonprofit Programs: Now It's Essential** (Vol. 12, No. 3)
- **How to Measure Your Organization's Efficiency** (Vol. 10, No. 3)
- **Is That Expense Justified?** (Vol. 20, No. 5)
- **Thirteen Ways to Cut Costs: Rate Your Organization** (Vol. 12, No. 4)

Footnotes

¹The data for this study came from Dr. Lynn Jones and Dr. Oliver Schnusenberg of the Accounting and Finance Department, University of North Florida, Jacksonville. Results of this research will determine future allocation of United Way funding.

²It is important to keep in mind that our sample applies only to charities that are already receiving aid from United Way of Northeast Florida. In addition, the data set we were given was not complete. As the study continues and more information is added, we hope to provide even more predictive results.

³We chose seven independent variables based on factors we believed might be affecting program revenues. To equate organizations of different sizes, we expressed our resultant variable — program expenditures — as a percentage of total revenues.

⁴We classified organizations as local or national based on information on their Web sites.

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