In the Time of Coronavirus: What the Data Say About the Risk to Michigan Nonprofits

by Jeff Williams

In chaotic times, leading an organization or board of directors and being responsible for charting a clear course forward for clients, employees, and the community becomes more crucial — and more challenging.

Mental models or frameworks can be a useful anchor and source of stability. While we cannot predict with absolute certainty how the coronavirus crisis will impact the nonprofit sector, we can use available data to anticipate where and how the greatest needs and challenges will arise. Increasing our general understanding of the state of the sector could provide some mental frameworks to help us all make decisions and deploy resources in this critical time.

So, from the perspective of the data and research team at the Johnson Center, we offer three thoughts on this crisis, grounded in the worlds of project management, disaster response, and solid data.

1 Before things get materially better or worse, we expect them to get weird.

A more colloquial version might be, "Embrace the suck." In times of great crisis — right when we are looking for certainty, even if it's bad news — events are likely to be unexpected in terms of magnitude, order, and topic. **Adopting a mental posture of extreme flexibility is key.** Being open about the impending storm in communications with service beneficiaries, clients, and staff is essential for maintaining staff morale, too.

2 There are three distinct financial threats facing nonprofits right now, each of which will impact different nonprofits in different ways. It will be best to know which one you are talking about in your conversations and deliberations.

With entire segments of our economy calving away, and the stock market continuing to tumble, nonprofits' revenue could suffer in three ways:

1. Decreasing revenue from annual campaigns and gifts,
2. Dropping demand for services and/or changes to contracts, and
3. Decreasing value in investments and stock market fluctuations.

Nonprofits are businesses. They pay out for salaries and rent, and they make purchases of supplies and equipment, just like any business. In the bigger picture, however, nonprofits serve a broader public mission beyond a typical business. Remember the airline safety briefing about oxygen masks in the event of an emergency? "Always secure your own mask before assisting others."

While businesses are closing and people are at risk of losing employment, there is likely to be an increase of demand for safety net agency services, many of which will be met by nonprofit organizations and their staff. But if a nonprofit cannot meet its business obligations, it will not be in a long-term position to assist its community in a time of need.

The nonprofit sector is not a monolith — at this moment there are more than 52,000 charitable and noncharitable nonprofit organizations in Michigan alone. We ran a quick analysis of IRS 990 data that we already had on hand for tax year 2015[1] to determine broad categories of financial threats — focusing in on the charitable sector.[2] The main takeaways from our analysis:

- The mix of revenue sources varies by organizational size. The larger the nonprofit, the less it relies on contributions and the more it relies on program revenue. Therefore, **in this wildly uncertain economy, smaller nonprofits are more likely to be worried about decreases in annual campaigns and gifts, while larger nonprofits are likely more worried about sharp drops in demand for services or cessation/curtailment of contracts.**

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- Very few charitable nonprofits receive more than 5% of annual revenue from investment income. Therefore, **conversations about what stock market fluctuations mean directly for Michigan's nonprofits are not the most immediate concern … unless the nonprofit is a foundation.**

Nonprofits systematically differ on how much they rely on charitable contributions for their revenue.

As expected, a typical Michigan nonprofit relies on contributions for the majority (53%) of its revenue.

Table 1: Total revenue and revenue from contributions for Michigan's charitable nonprofits

Annual Revenue (2015)	**Count of organizations (by unique EIN)**	**Average, total annual revenue**	**Average, percent of total revenue from contributions**
< $100k	3,660	$39,673	55%
100–499k	2,822	$236,623	54%
500k–999k	785	$711,234	52%
1–9.9MM	1,429	$3,187,827	51%
10–50MM	275	$20,943,625	38%
> $50MM	45	$107,663,494	29%
Grand Total	**9,016**	**$1,833,522**	**53%**

[1] Data for tax year 2017 is the most recent full year available, which we are processing now.

[2] There were 42,776 nonprofits in Michigan in 2015; of these, 32,183 were public charities (as opposed to noncharitable nonprofits — like mutual insurance companies and state-chartered credit unions, etc. — or private foundations). Of those public charities, 21,808 were "active" (meaning they filed at least one tax return within 36 months of 12/31/2015). Of the active public charities, 10,087 reported more than $25,000/year in revenue. We intentionally excluded 259 hospitals and institutions of higher education from the analysis, because most of these institutions dwarf the size of a "typical" nonprofit, and removed organizations that didn't have detailed information on file with the IRS. That left 9,016 Michigan charitable nonprofits where we could access total revenue and components of that revenue for tax year 2015.

Digging deeper into the data, however, we noticed two things:

1. Overall, the percentage of a nonprofit's revenue that comes from contributions decreases markedly for nonprofits above $10 million in annual revenue.

2. There are differences by category of nonprofit:
    - For arts-focused nonprofits, the percentage of revenue that comes from contributions increases as organizational size increases.
    - Education-oriented nonprofits held relatively consistent in share of revenue from contributions, mostly in the 40% range.
    - As the size of health and human services nonprofits increase, contributions as a share of their total revenue decreases substantially — mostly because as these types of organizations increase in size, program services revenue makes up a larger share of incoming funding.

Table 2: Percent of revenue from contributions, by size and type of nonprofit

Annual Revenue (2015)	**Arts**	**Education**	**Health**	**Human Services**	**All Other**
< $100k	48%	42%	63%	50%	67%
100–499k	49%	48%	54%	48%	68%
500k–999k	52%	44%	51%	46%	66%
1–9.9MM	59%	44%	39%	50%	68%
10–50MM	61%	35%	15%	42%	78%
> $50MM	60%	43%	7%	25%	55%
Grand Total	**50%**	**44%**	**48%**	**49%**	**67%**

What does this mean?

Funder and boardroom conversations about potential decreases in charitable contributions should be considered most urgent for nonprofits in this order: arts, all other nonprofits (e.g., environment, international), education, human services, and health — and the smaller the organization's annual revenue, the more important those discussions are regardless of the type of nonprofit.

Nonprofits that rely on programs for the majority of their revenue will experience different impacts over time.

Program services revenue — that is, earned income through direct fees or contracts to provide services to a community — sees effectively the reverse of the findings for contribution income.

How organizations are paid for providing those services is another crucial factor. For organizations where revenue increases with each additional person served, the challenge could be keeping up with a radically increasing demand for services at the present time (or very near future). On the other hand, if an organization's programs are funded on a fixed-price model, then these organizations are facing huge increases in demand with potentially little to no additional revenue.

- Arts organizations, regardless of size, hover around 33% of total revenue from services — which would primarily be ticket sales and other direct fees for service income (gift shop, concessions, special events, etc.)
- The big story here is the dramatic increase in the importance of program service revenue for health and for human services organizations — where the largest organizations receive more than 70% of their revenue directly from fees-for-service. And remember, this data excludes hospitals!

Table 3: Percent of revenue from program services, by size and type of nonprofit

Annual Revenue (2015)	**Arts**	**Education**	**Health**	**Human Services**	**All Other**
< $100k	33%	22%	14%	32%	15%
100–499k	41%	35%	34%	44%	20%
500k–999k	40%	44%	43%	47%	24%
1–9.9MM	33%	44%	55%	46%	21%
10–50MM	21%	54%	78%	55%	14%
> $50MM	32%	32%	89%	72%	37%
Grand Total	**36%**	**31%**	**39%**	**41%**	**18%**

What does this mean?

Funder and boardroom conversations about potential decreases in program services revenue are likely concentrated in health and human services organizations from two perspectives: handling increased demand in a fixed-fee world, or quickly scaling up to meet short-term demand … and then preparing to scale back down when the demand recedes.

For all other organizations, program revenue discussions likely hinge more on when customers/patrons are going to feel comfortable about returning to public life than on whether the organization itself is open for business.

Other than for foundations, very few charitable nonprofits receive more than 5% of annual revenue from investment income.

Stock market fluctuations are a direct concern for donors, for example, but most nonprofits will realize any changes in donor behavior as changes in contribution revenue and not changes in the nonprofit's own investment income.

Table 4: Total revenue and revenue from investment income for Michigan's charitable nonprofits

Annual Revenue (2015)	Count of organizations (by unique EIN)	Average, total annual revenue	Average, percent of total revenue from investment income
< $100k	3,660	$39,673	7%
100–499k	2,822	$236,623	3%
500k–999k	785	$711,234	3%
1–9.9MM	1,429	$3,187,827	3%
10–50MM	275	$20,943,625	2%
> $50MM	45	$107,663,494	2%
Grand Total	**9,016**	**$1,833,522**	**4%**

What does this mean?

Conversations about what stock market fluctuations mean directly for Michigan's nonprofits are not the most immediate concern.

We'll explore in a follow-up blog post the effect of investments on foundations, where investment income frequently composes the majority of a foundation's revenue.

3 The process of “restoring normal” is not linear. We expect multiple waves to occur as different sectors respond.

One of the clear lessons from disaster recovery and disaster philanthropy is that needs change over time. Though some disasters are a singular event (think tornado, hurricane, or tsunami), others can be more slow rolling (think the Great Recession, or spring floods in the Midwest).

In nearly all cases, however, the recovery is never a single event. Rather, it is a series of stages and processes — much like the five (or seven) stages of grief. (For a wealth of information about disaster philanthropy — including specific information about COVID-19 — visit the Center for Disaster Philanthropy’s website at https://disasterphilanthropy.org.)

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Thinking again of a mental framework, and leveraging the revenue picture from the IRS 990 returns above, we can envision a recovery process that could look like this:

- The sector — its organizations, donors, boards, executive leadership teams, and staff — are focused “right now” on matters of health care and direct emergency assistance (especially food). This phase continues for as long as schools are closed for an undetermined length of time and the spread of the virus is effectively uncontrolled.
- Sometime later, when the overall situation is stabilized — for example, schools are known closed through the end of this school year, and the virus curve has been flattened — conversations and funding will shift to education, housing, and human services. This will be doubly true if a “social distancing” policy becomes the norm for the rest of the calendar year, which could continue to have major effects for certain job markets and industries.
- Later than that, when the virus is contained through widely-available and known effective treatments (or a vaccine), we will pivot again to community recovery. This is where job training, child care, workforce development, and related concerns step back into the forefront.
- Finally, when people feel comfortable making longer-term plans to go outside their homes on a regular basis, the travel and leisure industries resume normal operations — which also unlocks full business output.

All of the above are true, until they are not.

We should stress that none of the frameworks discussed above are mutually exclusive or true for every single nonprofit. They are also quite fluid as this particular disease-fueled crisis unfolds. Instead, we intend them to be useful means of understanding what is likely causing the most financial worry at the majority or nonprofit organizations today.

In the coming weeks, we also plan to use additional IRS data to look at three more potential topics:

1. What trends do we see regarding "cash on hand" balances of nonprofits — especially by organization size, sector, or location in Michigan?
2. How will changes in revenue sources (especially investments) affect foundations of different sizes and types?
3. What do past economic shocks tell us about the pace of nonprofit organization creation and failure rates?

As researchers and thinkers, we welcome your comments on this topic and would love to hear in the coming weeks and months what models and mental frameworks are proving useful for your organization. Leave us a note in the comments section below, or contact us at jcp@gvsu.edu.

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