

**INTEGRATING FINANCIAL CONCEPTS  
OF NONPROFIT ORGANIZATIONS  
INTO THE FINANCE CURRICULUM**

**(paper proposal)**

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(Abstract)

Although nonprofit organizations are a major sector of economic activity and many of our students will eventually find employment in this area, it tends to be neglected in the finance curriculum. This is all the more unfortunate and surprising given the explicit Christian mission found at most CBFA schools. This paper will identify and discuss the unique problems and differences encountered by nonprofit's in their finance/treasury departments. Given this background, the paper will then propose how the finance curriculum could be enriched by suggesting specific nonprofit concepts that would be most useful for infusion into finance courses.

The argument has been made that economic criteria such as maximizing value or earnings dominate decision making in for-profit organizations. But, such criteria are secondary or nonexistent in nonprofits, especially service based nonprofits whose primary focus is providing aid to the indigent. Here there are competing criteria such as religious values, compassion, community needs and the primacy of the service ethic. Since not-for-profits (N.F.P.'s) technically don't seek to maximize profit, do these competing criteria significantly alter the related treasury/finance function in these organizations? This paper will delineate the similarities as well as the differentiating factors between

these two organizational forms specifically in the finance area. The purpose is to offer suggestions on how to incorporate the unique aspects and problems of nonprofits into our finance courses with the goal of increasing the mission fit and relevancy of the finance curriculum.

The methodology for the paper will consist of field and telephone interviews with several financial managers at nonprofit organizations. The purpose of the interviews is to illicit responses regarding the finance function in their organization as well as their views on the educational needs of financial managers at nonprofits. In order to make the study more manageable and to concentrate on those organizations who rely on voluntary giving as their primary source of revenue, the sample was narrowed by excluding hospitals, churches and educational institutions. Sample organizations include, among others, CRISTA Ministries, World Concern and Mercy Corps International. (Appendix A gives a listing of respondent organizations). Each respondent will receive a list of suggested discussion topics and questions (Appendix B). This will be followed several days later by a field or telephone interview.

The paper will be organized as follows: Section 1 will be an introduction. Section 2 will describe similarities in the treasury functions of for-profits and nonprofits. Section 3 will discuss unique problems and differences in the treasury functions. And, section 4 contains suggestions for transforming the finance curriculum to better fit our Christian missions and improve relevancy for our students.

## **SIMILARITIES IN THE TREASURY FUNCTIONS**

There were several areas of the treasury function where little difference was found between nonprofit and for-profit organizations. These were primarily in the cash flow and working capital management areas. For example, most respondents said their cash flow projection techniques and reporting formats were the same as in any organization. However, they all complained of cash flow problems and the lack of adequate reserves. Also, areas such as accounts receivable and accounts payable management were thought to be very similar. Accounting systems, for the most part, were also very similar to for-profit organizations. Finally, cash management systems and techniques appeared to be little different from those of similar size organizations. Most respondents reported that they used up-to-date systems for payroll, transferring cash and tracking funds in various accounts.

However, several respondents noted that they were likely to be more sympathetic in their handling of late payers than in for-profits. They tried to be sensitive to cases where the payer was in a dire economic situation, which, of course, well reflects the stated mission of the nonprofit. Gary Paisley of Food For the Hungry stated, “Our reason for existence is to help the indigent and the poor, so that same attitude carries over to late payers who have legitimate reasons for being delinquent.” And, Dan Busbee of the Wesleyan Center stated, “Most of our receivables are from nonprofit bookstores. We

make every effort to collect, but if judged uncollectable, we write the receivable off rather than taking them to a collection agency. We want to avoid an adversarial relationship.”

The above noted similarities give guidance in determining how to approach these topics when planning the finance curriculum. First, cash flow and working capital management should not be neglected in the finance curriculum as these are critical areas in the small to medium size organization which N.F.P.’s tend to represent. Second, the similarities in how the key finance functions are managed in N.F.P.’s and for-profits would suggest that stand alone teaching modules are not necessary. Since many of the unique issues facing N.F.P.’s are directly applicable to existing finance concepts, they should be infused into the existing curriculum. This saves precious teaching time and ensures a seamless flow as these topics are presented. This is not to deny the existence of unique financial management aspects found in nonprofits as well as different ethical issues faced by these organizations. Several of these will be discussed next. However, since there appears to be few differences in the operational aspects of these functions between for-profit and nonprofits, the key role of the professor is to ensure understanding of how to organize, report and manage financial areas regardless of whether the setting is for-profit or nonprofit.

## **UNIQUE PROBLEMS AND DIFFERENCES IN THE TREASURY FUNCTIONS**

The respondent interviews revealed a number of areas where unique problems are faced and where the treasury operation is different for nonprofits. A summary of these areas is listed here with further discussion to follow. 1. The use of rates of return and other financial performance measures in the decision making is not as evident. 2. Unique

cash flow problems. 3. Bank borrowing opportunities and arrangements. 4. Financial executives perceive that area managers are less knowledgeable about and concerned with bottom-line issues and measures than with human values and a commitment to compassion and service. 5. Difficulties in identifying the organization's customers. 6. Issues related to measuring and rewarding job performance. 7. Dealing with the regulatory issues related to fund raising.

## Measuring Financial Performance

For N.F.P.'s, the notions of maximizing net income, return on investment and stockholder value are not commonly used measures of organizational performance. However, in an attempt to have some measure of return and performance, all respondents utilized one or more forms of quantitative benchmarks. For example, most utilized some type of "cost per beneficiary" measure where the intent is to measure the cost of delivering services. Although none used rates of return, the notion of estimated useful life and "payback time" was used by some in analyzing capital expenditures. Also, obtaining and reporting a low overhead rate (administrative and fund raising costs/total revenue) was a key financial measure. Finally, the "return on investment" notion had the most meaning for respondents. However, it was used in the context of measuring the success of fund raising efforts. For them, the investment was committing resources to fund raising and they all spoke of maximizing the ROI ratio. A ratio of 5:1 was considered successful while 2:1 or less was thought to be a poor return. Several respondents expressed frustration in being unable to adequately formulate financial return measures for dollars invested in aid to beneficiaries. They perceived most of their effort

going toward minimizing costs rather than maximizing returns to the people they are committed to help. Although, mathematically they are the dual of each other.

## Managing Cash Flow

A problem mentioned by all respondents was cash flow management with two areas of concern commonly cited. One had to do with the continual battle to have enough cash available to make payroll and pay bills. The other had to do with the related difficulty of projecting income. Respondent organizations derived most of their income from voluntary giving which tends to produce uneven cash inflows. Several respondents pointed out how different and difficult it is to do projections of gift income versus sales income. Also, several respondents mentioned that their income was media driven. For example, relief agencies like Food for the Hungry and World Concern see an influx of income when a situation like the refugee problem in Rwanda hits the news. The income is certainly welcome, but the unpredictability of it makes long-term cash flow and staff planning difficult. Exacerbating the above problems, several respondents mentioned inadequate reserves. Cash flow problems certainly are not unique to nonprofits. However, the capricious nature of donor based income and low reserve levels create a particular set of problems for the financial manager in these organizations.

## Bank Funding Constraints

Contributing to the above problem, several respondents felt that banks do not understand their organizations. They found that banks tend to be leery of any organization whose income is based primarily on voluntary giving. Bill Brown of CRISTA Ministries stated, “banks are reluctant to lend to us because of the negative

publicity that might arise if they ever had to go through with a repossession.” For these and other reasons banks quite often imposed more stringent loan criteria and granted lines of credit that were relatively meager given the size of the organization in question. Gary Paisley of Food For the Hungry was frustrated that he could only secure a \$200,000 line of credit although he had a \$24,000,000 annual budget.

### Financial Integrity versus Humanitarian Needs

Financial managers at N.F.P.’s have the perception that area managers are less knowledgeable about and less concerned with bottom-line issues and measures and the reporting requirements that are essential to a well functioning financial control system. Several respondents mentioned that it is sometimes difficult to get area managers to comply with reporting requirements and budgeting systems. Area managers make them feel like they are an impediment to the “real” work of the organization. Respondents felt at times that there was a division between the “relief providers” and “administration” aspects of the organization. The administration was thought of as a “necessary evil” by the relief agency heads. While the old line versus staff tension is present in many for-profit organizations, this tension can be particularly acute in relief-based nonprofits. The grand, inspired plans of the field worker managers are often undergirded by the notion that in the name of human decency this project must be accomplished. The finance people who say it may have to be scaled back are thought, by the relief project managers, to be uncaring and concerned only with the financial aspects of the operation. Their commitment to compassion and service may be questioned by the operations people in the field. Several respondents mentioned, almost defensively, that if they didn’t stress the

need for financial integrity, then the organization would eventually die and no relief work would be accomplished, large or small. They felt that part of their job was balancing economic survival with unlimited worthwhile projects and communicating this dilemma to the relief agency leaders. Several mentioned how their hearts have been torn by seeing the pictures of hungry children or homeless, drug-addicted street people and having no way to meet that need through their organizations.

Related to the above, several respondents expressed frustration regarding the decision making process in their organizations. Quite often they were the only person on the management team with business training and/or experience. While they were used to and understood the need for long-range planning, budgets and efficient decision making processes, their colleagues, who were often trained in social work or sociology, were sometimes cumbersome in such matters. Cheryl Knudson of the Union Gospel Mission stated, "Rather than plan ahead for capital expenditures and contingencies, there is a tendency to make decisions only in emergencies." Bill Brown stated, "The decision process is longer here compared to my experience working for a for-profit company. There is less of a sense of urgency. On the other hand, people's feelings are considered here and I appreciate that aspect."

In a related area, several respondents felt that financial information and reporting systems for use by internal managers were lacking in their organizations compared to that typically found in for-profit firms. Alwin Lewis of World Concern stated, "I think that one of my biggest challenges is to provide strategic internal financial information to the leaders and managers in our organization." While external reporting is important, it can be guided with the help of the independent accountants who audit the organization. More

difficult is developing financial information for internal managers that is tied to organizational mission and goals. Part of this is that the financial manager has to advocate and train users in the importance of financial information in the achievement of organizational objectives. Often financial planning is not part of relief service planning and sometimes it is considered a “necessary evil” by the non-financial manager or leader. Respondents expressed the idea that financial planning, accounting and control needs to be viewed as a key to successful relief efforts, not a hindrance or a hurdle.

## Identifying the Customer

Another area where nonprofit treasurers differ from their for-profit counterparts is in identifying the organization's customers. I asked each respondent the question, "Who do you perceive your customer to be? The donor or the beneficiary of your services?" Most answered that the donor was the entity that most commanded their attention and influenced how they organized their accounting and reporting systems. There seems to be a tendency to focus on resource attraction rather than output results like delivery of services and attainment of goals and objectives. Kanter and Summers [1987] explain this focus by stating:

"Since nonprofit organizations tend to provide services that are hard to measure, there is rarely a new bottom line. Thus, planning becomes more concerned with fund-raising or resource inputs than with service, in part because of the greater ease of measuring the former. Although the success of nonprofits rests in part on resource attraction, products or specific benefits do not tend to be available to donors, and therefore performance criteria for resource allocation (service delivery) might be unrelated to criteria for resource attraction."

The notion of the beneficiary as customer and being driven to please that customer (which is a key theme in for-profit companies) can be difficult to carry over into the nonprofit environment. The beneficiary typically is not choosing between competing service providers. They are desperate for food, clothing, medicine and other social services and are not overly concerned with quality of service. Therefore, the notion of "please the customer or lose them" is not present. However, if the "customer" is the donor, the notion is present. If the "product" of N.F.P.'s is the efficiency with which they accomplish their mission

and that's what they "sell" to potential donors, then competition for donors is present.

Another problem is the lack of creative ways to measure whether you have effectively served the customer since there are no dollar sales or profits that result from delivering the service. Typically, N.F.P.'s stress minimizing overhead, maximizing percentage of funds raised going to recipients and maximizing return on dollars invested in fund raising. Bill Brown stated, "While it is true that typical measurement tools used by for-profits may not work well, my colleagues have not sought out other creative measures. If they really wanted to know the answer, they would find a way."

## Measuring and Rewarding Performance

Nonprofits differ in the area of employee compensation and bonuses. None of the respondent organizations utilized monetary bonuses to reward excellent work performance. The notion of monetary rewards seemed somehow sacrilegious in the culture of the nonprofit. When asked why this was true, the responses generally ran along the following lines. One, it is difficult to measure meritorious performance in a nonprofit organization because most of the services rendered or outcomes are qualitative, intangible or spiritual in nature. Without a reliable measurement system, bonuses would be awarded rather subjectively creating potential morale problems. Two, somehow bonuses are incongruent with the basic idea of a nonprofit. To receive a monetary payoff above your regular salary for helping people seems somehow crass. In such an organization, one is motivated to work hard and perform well because the calling is to a

higher value than money. One is motivated by the service ethic and the desire to contribute to the betterment of mankind. Both of these arguments help to explain a related characteristic of nonprofits. That is, several respondents said they could earn more money doing the same job in the for-profit world. However, most respondents said the non-monetary benefits of dedicating one's professional skills to a social service organization more than offset the imbalance in compensation.

## Regulatory Issues

A further issue that is unique to nonprofits is dealing with the regulatory issues related to fund raising activities. Agencies such as state's attorney generals, the IRS and the Better Business Bureau have become more pro-active and are quicker to bring action against offending organizations. In addition the nonprofits themselves have increased their self-regulatory activities. In the religious organizations, the Evangelical Council for Financial Accountability (ECFA) has become the centerpiece for financial accountability and has taken a more activist role by formulating new standards and principles for fund raising and handling donor money. Membership in the ECFA is prized as it gives the religious nonprofit a seal of integrity, thereby aiding them in their fund raising efforts.

For the treasurer in a reputable nonprofit this increased regulatory emphasis is a two-edged sword. Although following accepted guidelines and publicizing this fact to ones donor base lends financial respectability, virtually every respondent mentioned and complained about the increased time they spend on compliance and the related paperwork and reporting burdens. Dale Jones of Mercy Corps International stated, "Over the last five years, there has been a big increase in the time I spend on regulatory paperwork. I

spend approximately 15% of my time on such matters.” Melissa Orth of the American Heart Association stated, “I see much more public scrutiny of our financial operations now. I think financial integrity is more important for the nonprofit than it is for the for-profit firm.”

## **SUGGESTIONS FOR CURRICULUM IMPROVEMENT AND CONCLUSIONS**

Given the aforementioned problems and differences, Table 1 summarizes several nonprofit concepts that could be included in the finance curriculum.

Table 1. Integrating Nonprofit Material In Finance Courses

Key Concept	Nonprofit Concept
Goal of the Firm	How to measure performance Identifying the Non-Profits Customer
Financial Markets	How Lender Risk Perceptions Differ for N.F.P.’s
Valuation	How to Value Donor Pledges
Risk and Return	Difficulties in measuring return performance
Financial Analysis	How to interpret financial statements of N.F.P.’s Internal financial reporting and control systems
Financial Forecasting	Difficulties in Projecting Income in a Voluntary Donor Environment
Working Capital Management	Managing cash flow in a donor based income environment
Financing Options	Regulatory Issue and Fund Raising Activities

In summary, these nonprofit concepts should not be isolated as separate modules but infused throughout the regular finance curriculum. As the key finance topics are presented utilizing the for-profit framework, incorporate the unique nonprofit issues. Given these distinguishing concepts, encourage students to think about other ways to measure organizational performance; to control and report financial information; to deal with cash flow issues in an environment dependent on voluntary donors. The primary purpose of introducing nonprofit issues is not to provide solutions as these concepts often

raise more questions than answers. But to expose students to several fundamental issues and problems faced by nonprofit financial managers.

## REFERENCES

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- Olenick, A. J. & P. R. Olenick, *A Nonprofit Organization Operating Manual*, (Chicago, 1991), The Foundation Center.
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## **Appendix A**

### **LIST OF RESPONDENT ORGANIZATIONS**

1. The American Heart Association, Dallas, Texas  
Melissa Orth, Comptroller  
Annual Budget: \$49,000,000
2. CRISTA Ministries, Seattle, Washington  
Bill Brown, Vice President, Finance  
Annual Budget: \$30,000,000 (excluding World Concern)
3. Food For The Hungry, Scottsdale, Arizona  
Gary Paisley, Vice President, Finance and Administrative Services  
Annual Budget: \$29,000,000
4. International Center For The Wesleyan Church, Indianapolis, Indiana  
Dan Busbee, General Treasurer  
Annual Budget: \$20,000,000
5. Lakeside Bible Camp, Seattle, Washington  
John Ward, Treasurer  
Annual Budget: \$1,500,000
6. Mercy Corps International, Portland, Oregon  
Dale Jones, Comptroller  
Annual Budget: \$43,000,000
7. Union Gospel Mission, Seattle, Washington  
Cheryl Knudson, Director of Accounting and Finance  
Annual budget: \$9,000,000
8. World Concern, Seattle, Washington  
Alwin Lewis, Director of Finance  
Annual Budget: \$28,000,000

## Appendix B

TO: Respondent's Name  
FROM: Dan W. Hess, Seattle Pacific University  
RE: Interview issues and questions

I am writing a paper on the treasury and finance functions in non-profit organizations. My purpose is to determine the similarities and differences in these functions as opposed to for-profit firms and suggest ways to more effectively integrate these concepts into the finance curriculum at colleges and universities. I am interviewing a number of people who have practical knowledge and experience in this area and you were suggested as someone who could help me. The following are some of the issues and questions I would like to get your input on. I would appreciate about 30 minutes of your time in person or over the phone. I will be calling you in a few days after you have had a chance to collect some of your thoughts on the topic.

1. Some historical perspective....

- age of your organization
- growth rates
- departments and organizational form
- other important aspects unique to the finance function

2. Issues of mission

- Do you have your own mission statement for the finance area? If so, what is it?
- Do you find it difficult to find a focal mission/strategy upon which various managers at your organization can agree
- Does the finance mission or objectives ever conflict with the overall organization mission?

3. Issues relating to the various finance functions. Specifically, what are some of the unique aspects of each of the following in a Non-Profit (NP)?

- accounting systems
- cash flow management
  - systems used and sophistication of
  - unique problems and issues for your organization
  - key uncertainties in your forecasts
  - examples of cash flow projections and other documentation
- accounts receivable management
- accounts payable management
- capital project analysis and decision making process
  - standardized format, if any
  - decision rules used i.e. cost/benefit analysis, rate of return etc.
  - who makes final decisions
- pension management; level of funding, commitment to
- internal control systems
- other finance functions at your organization not mentioned

For each of the above, my interest is not so much in the details of how you perform these tasks. But, what are some of the unique aspects, problems faced in each as they are worked out in a NP.

4. Banking relationships (if any)

- unique aspects of in a NP
- unique numbers, statistics, ratios or data bank wants that differ from a for profit company
- do you have bank loans? If so...
  - types of loans i.e. short term, long term, payment schedules etc.
  - interest rates as compared to for profit firms
  - unique features due to being a NP.
  
- other lending/financing arrangements unique to a NP.
- other banking services used that are unique to a NP

5. Other issues

- could you provide an organization chart for your finance department?
- could you comment on your usage of the following techniques/criteria:
  - budgets
  - cost/benefit analysis
  - calculating project cash flows and related rates of return
  - notions of profit
  - computer spreadsheets, modeling, simulations etc.
  
- ethical issues that you encounter
- amount and level of training in areas of finance
- are financial incentives, bonuses paid to managers?
- in for profit firms, managers are rewarded for cost cutting, maximizing profits/earnings etc. what about in a NP? How is your performance measured and rewarded?

6. Given your thoughts on the above questions, what curriculum or educational needs do you see or changes/recommendations you would make in finance education at U.S. colleges?

7. I look forward to talking with you regarding these issues. If I have not touched on an area that is very critical in your work, please let me know.

Sincerely,

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September 28, 1994

Dr. E.J. Merkel  
Troy State University  
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Troy, Alabama 36082

Dear Dr. Merkel,

The enclosed manuscript is submitted for review for possible presentation at the upcoming MAEF meeting in Biloxi, Mississippi. I believe the paper would fall either under the area of small business or nonprofit financial management. Thank you for handling this matter.

Sincerely,

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