CalNonprofits
CALIFORNIA ASSOCIATION OF NONPROFITS

The Financial Realities of Operating a California Nonprofit

A POLICYMAKER'S GUIDE TO HOW NONPROFITS ACTUALLY RUN

California relies on nonprofits to deliver essential public services that the private sector overlooks and the public sector cannot provide alone. Nonprofits fulfill critical community needs by providing efficient, flexible, culturally relevant, and locally-tailored services that other sectors cannot.

But what are the true costs of service delivery and sustainable community-led work? Nonprofits navigate intricate, often volatile financial environments, yet public funding and contracting policies remain tethered to outdated misconceptions about how these organizations actually run. On average, less than 30% of nonprofit revenue comes from private contributions. The sector's revenue comes from a highly varied, sophisticated, and innovative mix of funding streams. Nonprofits operate as complex social enterprises.

To build a stronger social safety net, policymakers must first understand these operational realities. This report offers a deep dive for policymakers to understand these realities to advance better policies, stronger nonprofits, and improved outcomes for all Californians.

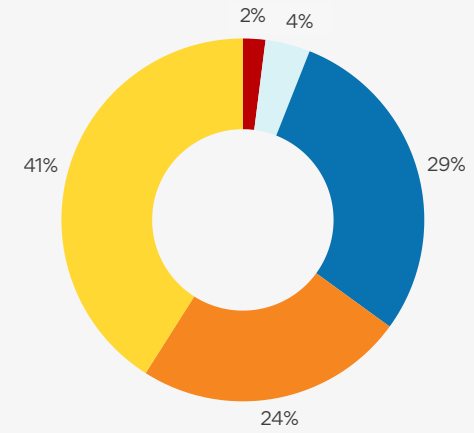
CalNonprofits latest polling shows the impact of nonprofits on Californians:

94% believe nonprofits are somewhat or very important to their communities

87% benefited from a nonprofit service in the last 12 months.

Source: Causes Count 3.0, CalNonprofits

Nonprofit Revenue



Source: IRS Form 990/990-EZ annual information returns, 2023 & IRS Business Master Files (BMF)

UNDERSTANDING THE TRUE DYNAMICS OF NONPROFIT FINANCES

Unlike for-profit businesses, nonprofits do not rely on predictable revenue or adjust services based on profitability. They adjust based on community needs, even when funding doesn't follow.

ONE MAJOR DIFFERENCE IN THE COMPLEXITY OF THE NONPROFIT BUSINESS MODEL: In most of the for-profit sector, the client pays for the goods and/or services provided to them by a business. In the nonprofit sector, however, the client is rarely the payer, and if they are, they are frequently one of many. Instead, one or more third party donors, funders, and contractors pay for the services provided to the client.

What Shapes Nonprofit Finances:

- **Unpredictable Funding Cycles:** Grants and donations are often one-time, short-term, or restricted, making long-term projections unpredictable and difficult to track.
- **External Risk Factors:** Factors such as legislative changes, economic downturns, and emergencies can upend budgets at any moment, adding uncertainty to long-term budget planning.
- **Limited Data to Forecast:** Many nonprofits, especially those innovating or responding to emerging needs, lack the long-term, historical data needed for precise financial projections.
- **Mission-Driven Adaptability:** Nonprofits prioritize fulfilling their mission, which may involve adapting programs, size of staff, and services based on community needs rather than financial optimization.
- **Variable Revenue Streams:** Donor behavior, economic conditions, and shifting priorities create constant fluctuation for incoming revenue, complicating long-term projections.

Key Takeaway:
Nonprofits operate in unpredictable funding environments, reflective of short-term, restricted and ever-changing funding structures. Real financial stability requires longer-term commitments, flexible dollars, and policies to match the realities of demanding community work.

💡 Policy Solutions	
Advance Payments	Implement wide-scale access to advance payments to allow nonprofits, especially those in underserved communities, to begin critical work without floating debt for the contractor(state, county, or other public agency).
Prompt Payment	Ensure the state pays nonprofits on time for services rendered to prevent cash-flow crises that lead to staff departures and service disruptions.
Contract Flexibility	Allow nonprofits to adjust service delivery during emergencies to meet changing community needs while still fulfilling the purpose of the contract or grant.
Streamlined Administration	Reduce unnecessary administrative hurdles and duplicative reporting so organizations can focus on community impact—not "red tape."

THE COMPLEXITY OF MEASURING SOCIAL CHANGE: **EVALUATION & IMPACT**

Nonprofits work on complex social issues that are multi-faceted and influenced by factors outside any single organization's control. Their impact is real but not always easily captured by traditional metrics, which often fail to capture the true value of their work.

What Shapes Impact and Evaluation:

- **Complex Social Issues:** Many nonprofits address deep-rooted social issues shaped by inequities and forces beyond their control. Isolating any program's effects amidst this complexity is difficult or even impossible.
- **Limitations of "Cost per Person Served":** This metric oversimplifies individualized and high-touch services, where the level of care and resources required can vary greatly from person to person. It fails to capture service quality and long-term impact, which are essential for achieving meaningful, lasting outcomes.

- **Short-Term Outputs vs. Long-Term Outcomes:** Nonprofits can report outputs like meals served or number of children reached, but demonstrating long term outcomes like improved livelihood or increased literacy rates require mulit-year tracking, significant resources, and a control group that may not exist.
- **Data Capacity Constraints:** Many nonprofits lack the tools and capacity to collect and analyze robust, reliable data, despite the expectations of funders and policymakers. Traditional evaluation models often reflect dominant norms and methodologies, overlooking community knowledge and qualitative impact.
- **Time and Cost Constraints:** Rigorous evaluation requires expertise and resources that most nonprofits cannot always spare in a tightening financial landscape.
- **Lack of Standardized Metrics:** Unlike how impact is evaluated in the private sector, measuring social impact is more subjective and lacks universally accepted or standardized metrics.
- **Risk Averse Funding Culture:** Innovation requires risk-taking, a privilege many nonprofits cannot afford if resources are scarce or tightly restricted. Therefore, nonprofits may have no choice but to focus on strategies or programs that have existed to secure acceptable measures of success.

Key Takeaway:
Nonprofits are deeply committed to delivering results aligned with their missions, but measuring meaningful impact requires time, resources, and a broader understanding of defining success. Their work is long-term, relational, and often preventative, which traditional metrics fail to capture.

💡 Policy Solutions	
Dedicated Evaluation Funding	Provide dedicated funding for data systems, evaluation staff, and technical assistance so nonprofits can collect meaningful, reliable impact data.
Long-Term Outcome Funding	Shift funding structures to support multi-year tracking and long-term outcomes rather than relying solely on annual outputs.
Streamlined Reporting	Reduce administrative burden by standardizing templates and eliminating duplicative data requests so nonprofits can focus on service delivery and meaningful evaluation.
Cross-Sector Data Partnerships	Facilitate data-sharing agreements with state agencies, researchers, and local governments to improve access to high-quality data and reduce duplicative efforts.

EFFICIENCY REALITIES:
MOVING BEYOND "DOING MORE WITH LESS"

Nonprofits vary widely in mission, communities served, and service models. Comparing them to for-profit businesses flattens the real cost of meaningful work and obscures what efficiency looks like in a community-based context.

What Shapes Nonprofit Efficiency:

- **Diverse Operations and Metrics:** Nonprofits operate with different missions and within highly variable community conditions, making direct comparisons in efficiency difficult and standardized comparisons misleading.

- **"Cost-effectiveness" is an outdated term:** Nonprofits have long been expected to "do more with less," which undervalues essential administrative and overhead costs. Real accountability means funding the full cost of programs (e.g., staff, compliance, governance, and indirect expenses) not just direct service costs.
- **Long-Term vs. Short-Term Impact:** Cost-effectiveness metrics rarely capture the long-term or holistic value of nonprofit work. Many outcomes like social stability, community trust, or environmental benefits unfold over years and are difficult to quantify or compare in short-term cost ratios.
- **Resource Variability:** Administrative and operational costs are not waste. They are the infrastructure that makes programs possible. Nonprofits may have varying levels of funding, volunteer support, and access to resources, influencing their cost effectiveness.

Key Takeaway:
Efficiency is not about low overhead. It is about providing resources to nonprofits based on realistic costs, accounting for community context, and valuing investment toward long-term outcomes.

💡 Policy Solutions	
Sufficient Indirect Cost Coverage	Guarantee that grants and contracts cover the true costs of service delivery, including operations and essential functions like finance, legal, IT, and HR.
Infrastructure Funding	Fund the administrative and operational infrastructure nonprofits need to deliver quality services, recognizing that efficiency varies with funding levels, staffing, and resource access.
Long-Term Cost Measures	Adopt metrics that capture long-term, preventative, and relational outcomes (i.e., stability, trust, and community well-being) rather than short-term cost ratios.

SUSTAINABILITY CHALLENGES:
CHRONIC UNDERINVESTMENT HINDERS TRUE STABILITY

Nonprofit sustainability is shaped by structural funding challenges, rising community need, and constant tension between mission and available resources. Organizations are navigating unpredictable revenue, short-term funding cycles, and increasing demand without the long-term investment required to plan, grow, or sustain impact.

What Shapes Nonprofit Sustainability:

- **Difficulty Diversifying Revenue:** Expanding funding streams requires staff time, relationship-building, and administrative capacity that many nonprofits simply do not have.
- **Unpredictable Donor / Funder Behavior:** Philanthropic and grantmaking priorities can shift quickly with economic conditions or political climates, creating sudden swings in revenue that nonprofits cannot control.
- **Ever-evolving Funding Environments:** Funding streams are shifting constantly due to changes in government policies, economic conditions, or social trends, making it challenging to predict future sources of support.
- **Competitive Funding Landscape:** Nonprofits compete for limited dollars while community need continues to rise, often forcing organizations to cut staff and services even as demand increases.

- **Mission vs. Funding Alignment:** Nonprofits must constantly balance staying true to their mission with adapting to funder priorities, navigating the tension between community need and what funders are willing to support.
- **Short Operating Runways:** Nonprofits constantly juggle short-term government grants, foundation partnerships, and private donations to secure necessary revenue. Yet, despite this diversification, long-term sustainability remains precarious. Because alternative funding streams cannot fully absorb operating costs and often have severe limits, legislative action to support reliable public contracting/grantmaking are essential for sector stability and uninterrupted community service.

Key Takeaway:
Nonprofits are not unstable, they are under-resourced. Their sustainability challenges reflect the funding, policy, and social environment, not a lack of planning.

💡 Policy Solutions	
Multi-Year Funding	Expand access to multi-year grants and contracts so nonprofits can plan, staff, and deliver services with stability rather than year-to-year uncertainty.
Flexible Funding	Increase unrestricted and flexible dollars that allow nonprofits to adapt to changing community needs and invest in long-term organizational health.
Stability-Focused Contracting	Design state and local contracts that reduce volatility, including predictable payment schedules, renewal pathways, and funding structures aligned with real program timelines.