



**COMMUNITY
SOCIAL PLANNING
COUNCIL OF TORONTO**
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Executive Summary

Community Capacity Draining: The Impact of Current Funding Practices on Non-Profit Community Organizations

Community Social Planning Council of Toronto
In collaboration with the City Community Workgroup on Core Funding
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“The money that government gives us to deliver programs in our community does not cover the cost of program operation. We have to use our United Way grant and fundraise to make up the difference. Every year it gets harder to make ends meet and we cut back a little more. The most frustrating part is that despite all our work to raise funds, we have no money to address new local community issues. Our local school and the mall merchants cannot understand why we cannot help address the recent rash of vandalism in our community before it becomes chronic.”

I) Sounding the Alarm; The Impact of Nonprofit Funding Practices

Over the past decade there has been a profound shift in the way governments and most funding organizations give grants and contracts to non-profit community organizations. In examining this shift a number of recent studies have warned that the sector is not thriving amidst such change. The 2003 report *Funding Matters: The Impact of Canada’s New Funding Regime on Non-Profit and Voluntary Organizations*,¹ documented the central trend toward funding “programs” rather than funding “agencies to deliver programs”, noting the resulting instability and increased stress among agencies to find the funds to operate.

*Cracks in the Foundation*², the City of Toronto’s 2003 survey of community agencies confirmed that agencies are struggling, reporting high levels of program fluctuation, difficulty in training and supporting staff and volunteers, and high levels of staff turnover and burnout.

Recent reports on the status of human resources in the sector³ have identified a sizeable and growing salary gap between the non-profit sector, the for profit sector and the quasi-Government sector (hospitals and education) and warn of a looming human resource shortage in the non-profit sector.

II) Unravelling the Funding Puzzle; The Contribution of this Research

While the broad impact of the shift towards funding programs rather than funding organizations is becoming clear, the specific implications at the agency level have not been well understood. In part, this is a result of the complexities of the sector’s activities and associated funding arrangements.

Community organizations are among the most diverse of our voluntary organizations. They provide services to seniors and the homeless, daycare and parent drop-in services

¹ (Scott, 2003)

² (City of Toronto, 2003)

³ (Saunders, 2004)

for young children, after school programs, youth programs, mental health services, newcomer settlement services, supports for people with disabilities and more.

Since community organizations have multiple sources of funding and many different funders, no single funder has an understanding of overall agency funding. Fragmented funding has meant there has been no information overview on how the sector is faring so each organization has been struggling alone. This lack of financial overview has left agencies and funders making decisions without all the necessary information and has frustrated discussions of what funding changes might be needed.

This research was undertaken by the Community Social Planning Council of Toronto for the City/Community Working Group on Stable Core Funding in order to better understand the agency-level impacts of current funding practices, pinpoint the areas of concern, and inform recommendations for funding reform so that they may better address the structural challenges agencies face.

To achieve this objective we first developed a tool to collect consistent and comparable data. Working with both small and large agencies we were able to develop a workbook that met their diverse needs and could fairly reflect their financial situations. In this way the revenues and expenditures from a number of community organizations were analysed using a structured framework and common definitions. Data for this report was drawn from a sample of ten agencies operating 155 discreetly funded programs totalling 36.5 million dollars.

The detailed data analysis undertaken in this project has provided new insight into the complex tangle of agency financing. The information learned significantly enhances and alters current understanding of the financing of non-profit community organizations, and suggests clear directions for the reform of funding practices.

With this study we can now identify the extent of the deterioration of capacity in community organizations that has resulted from the systemic under-funding of service. We can see how this under-funding is draining community organizations of their ability to be active in their communities and reducing their organizational capacity to such an extent that their ongoing sustainability is in serious question.

As we gained an understanding of the detailed operation of multiply funded community agencies, we came to understand that not only is there a problem with levels of funding keeping pace with rising costs but the very models used to fund community agencies are not able to accomplish their objectives and do not adequately accommodate the reality of community agencies' capacities and operations.

This project is the third of three building blocks that lay the groundwork for funding reform.

- The first component is the Government of Canada's *Accord* with the Voluntary Sector and the *Code of Good Practice on Funding* that provides the policy framework for funding reform.⁴
- The second building block is the recent research profiling the difficulties facing the non-profit sector and making the case for funding reform to ensure the sustainability of the community non-profit sector.
- The third, the subject of this report, is a detailed analysis of agency financing using a common framework across programs, funders and organizations.

III) Summary of Research Findings

As currently structured, most government-funded programs in community agencies are not covering the complete costs of program operation. The delivery of government funded services are in fact draining community organizations of their discretionary and locally raised funds as agencies cover the difference between government funding and the full costs of running programs.

Program funding is, by definition, funding which an agency receives to deliver a service. That service is specified, often in great detail, by the funder. Agencies seldom have discretion over the content or structure of these programs or in determining who is eligible to receive the service. By applying all of their discretionary revenues to cover shortfalls in programs under contract to a funder, agencies have little or no capacity to respond to emerging community needs or develop innovative service models.

In this context, agencies are fundraising to stay afloat. Since agencies are responsible for program deficits, (surpluses are recovered by the funder but deficits belong to the community organization) they are having to apply the greater part of, if not all of, their non-government revenues to cover the shortfall in program funding.

Over the years we have become confused about the use and purpose of community-raised funds and the role of community organizations as providers of social services.

Community Organizations have two functions:

- To build strong, caring and compassionate communities
- To deliver government funded services in local communities

These functions are compatible, mutually enhancing but distinct activities. Locally raised funds should be deployed toward building strong resilient communities, while government funds should fully support social service delivery.

⁴ Voluntary Sector Initiative, *An Accord between the Government of Canada and the Voluntary Sector*, and *A Code of Good Practice on Funding: Building an Accord Between the Government of Canada and the Voluntary Sector*, Canada 2000

In contrast, our research concludes that community agencies are operating government-funded programs at a significant loss. The most significant areas of systemic government under funding are:

- Employee benefits;
- Front line supervision, and;
- Core organizational functions⁵.

As costs keep rising and funding remains inadequate, flat-lined community agencies are slipping away. Their staffing costs comprise 71% of total spending. Typically staffing costs in the human services are well over 80% and often in the 90% range.⁶

Our study findings on the under-funding of staff supervision and the erosion of core organizational capacity raise important policy issues of program quality and risk management that pose significant concerns for both agencies and their funders.

IV) Detailed Findings

- ***Overall, 85% of agency revenues came from program funding, 13% from other sources including fundraising and undesignated grants, and 2% from fees. Government funds account for 82% of the 85% of program funding. Program funding breakdown⁷: (Federal government 34%, Provincial government 36%, City of Toronto 12%, other 3%.)***
Program funding is tied to the delivery of a specified service and often has little flexibility. *Other source funding* is flexible funding the agency can use to meet emerging community needs, experiment with service innovation or improve organizational capacity. Nominal *fees* are charged for some programs. No agency in the sample covered program costs with fees alone.

- ***On average, the organizations were receiving 14% less funding than they needed to cover actual operating costs.***⁸
The chronic and pervasive under funding of programs is draining agencies of the discretionary funding they have traditionally used to build strong communities and address emerging needs. All but one agency received less funding than it cost the agency to deliver its programs.

⁵ Sometimes more narrowly conceived of as “administrative” functions, “core” functions are the essential activities, facilities and supplies that permit an agency to deliver its programs with the added value funders expect from the voluntary sector. These include functions of human resource management, financial management, governance, and administrative systems that support all programs (e.g. reception, data management and reporting).

⁶ 1998 City of Toronto Budget Staffing budgets as percentage of overall spending, Police Services 89.5%, Fire Services 94%, Public Health 83%.

⁷ Breakdown Percentages are of total funding

⁸ Data note: The average of the ten agencies is provided in this summary of findings as an indication of the size of the systemic gap in funding. Across the ten agencies however the actual amount of under-funding varied among agencies. See full report for breakdowns by organization.

- Agencies are fundraising to support programs provided under contract to government.**
 Agencies in the sample are coping, in the short term, by applying virtually all their flexible non-program income to cover off the pervasive under-funding of programs. The organizations’ “other income” - united way grants (6%), fundraised revenue (5%), other grants, miscellaneous income (2%), and fees 2% are being used to cover the shortfall in government funding.
- Not all organizations have equal capacity to tap alternative revenue sources.**
 The analysis shows smaller, newer organizations in developing communities had less capacity. Agencies noted that fundraised revenues are the most precarious and vulnerable of all revenue sources. The amount raised varies significantly from year to year and requires extensive staff and volunteer effort.
- Program Funders under-fund employee benefits an average of 22%.**
 The benefit packages among the sample organizations tended to be modest with the best of them near 20% of salary (the average was 18%), but even so, only one agency received enough funding to cover their costs. Funders contributed a total of 14% to benefits. Agencies had to find other revenues to pay for the benefits provided to program staff.
- Only one half of programs (53%) provided funds for the supervision of front-line staff.**
 Funders, especially of small grants, seem to expect the agency to provide supervision gratis. Of those funders that pay for supervision, the amount contributed varied enormously among funders and within funded programs. Overall, supervision costs were funded at 5% of total program costs, less than half of what is required.
 In the *Cracks in the Foundation*⁹ report, 34% of agencies reported they could provide supervision only sometimes or not at all to staff and 53% could not supervise volunteers. The under-funding of supervision raises important policy issues of risk management and program quality standards for both agencies and funders especially in light of recent court decisions on vicarious liability.
- Agencies have reduced staffing in their organizations to cope with rising costs and stagnant, unstable funding.**
 Over the years, “other revenue sources” have not kept up with funding shortfalls so in addition to redirecting agency discretionary funds, agencies have cut back on staffing. Across the agencies, staffing is down to an average of 71% of budget from a norm in human service organizations, of 85%-90%.
 Staffing has been the only variable agencies can adjust in the face of rising costs. Audit, insurance, rent, program expenses are all beyond the control of the agency.

⁹ *Cracks in the Foundation, City of Toronto, 2003* The City’s survey of community agencies.

As fixed costs rise and funding fails to keep pace¹⁰, agencies have reduced staff to balance their budgets. Since human resources are so central to a community organization's capacity to help, this loss of staff is concerning.

- ***Program funders are under-funding their share of core organizational costs by 58%.***

Program funders are contributing very little to common core organizational expenses. Shared core organizational costs are 13% of budget,¹¹ of this amount almost half is non-discretionary organizational expense such as insurance, audit, equipment leases etc. leaving little for core agency staffing. Senior managers report they have streamlined their core staff to the point of inefficiency. Community organizations are facing a crisis of organizational capacity.

- ***Funding instability is a serious issue for community organizations.***

Eight of the ten agencies identified one fifth (20%) or more of their programs as unstable. Six had more than 15% of their revenues tied up in unstable grants. Agencies report that even if funding is renewed, the threat of instability affects how they invest in and manage programs. Much energy is spent obtaining the grants, starting-up the programs only to wind them down a short time later. These grants are costing organizations considerably more to implement than they receive in funding.

V) Suggestions for Funding Reform

One of the objectives of our research was to identify those funding practices that are most helpful for organizations in allowing them to maintain organizational capacity and deliver quality and safe services. While there are many funding practices, the following are those practices that were identified as promising in the course of developing the workbook and analysing the financial data.

If every funder took responsibility for paying their fair share, and covering their own program costs and their share of common costs, we would have a sustainable model for Canada's community organizations.

1. ***Funding the Full Cost of Programs***

Funders, when contracting with a community organization to deliver a service, should pay the full costs of service provision including a proportionate share of organizational

¹⁰ Howarth, Rob, *Shaken Foundations: The Weakening of Community Building Infrastructure in Toronto*, Impacts of a five year funding freeze on Toronto's community-based service organizations, June 2003

¹¹ An additional 6% is program specific (used exclusively in a program) core expenses for a total of 19.4% total core costs.

operating costs and the actual operating costs of service delivery. In an optimal situation the funder would pay a community investment premium (equal to the business profit margin) to help build local communities.

2. *Moving to Global Budgeting*

Funders should implement a global budgeting approach where they approve a total budget amount and let service provider determine how best to spend the funds to achieve agreed service outcomes. Funders need to focus on accountability measures such as service outcomes and deliverables, not the day-to-day management of programs.

3. *The Strategic use of Lead Funding*

Governments should use a lead funding model (funding both program and organizational infrastructure) for services that further government policy objectives in a given service area, and in order to sustain long-term community capacity.

4. *Providing undesignated funding to support organizational capacity and service innovation.*

Funders should provide undesignated funding that agencies can spend flexibly as a preferred means to build local capacity, encourage service innovation and meet local needs.

5. *Fundraised funds and donations from united way funders and foundations should be used for service innovation, strengthening communities and addressing local needs.*

Locally raised funds should be deployed toward community building activities while government funds should fully support social service delivery.

VI) Making Change, Moving Forward

All the necessary pieces are in place to support a process of funding renewal - a policy framework for funding non-profit organizations, and the research on the human resource and organizational issues facing community agencies. Now, with this study, we finally have data demonstrating the significant shortfalls in program funding, the key areas of under funding and have evidence of the serious pressure this is placing on community organizations. The study findings raise questions about the suitability of current funding models to accommodate the realities and capacities of community agencies.

This project has produced strong trend data on the major areas of funding shortfalls and described how agencies are coping in the short term. It is clear from the information gathered by this project that current funding practices and funding levels cannot be sustained for much longer by community organizations. The need to reform program funding to community-based organizations is urgent.