

State of the Arts Study in Delaware

**Provided by
Nonprofit Finance Fund**

**In Partnership with
Delaware Division of the Arts
The Welfare Foundation**

March 2008



Special Thanks

NFF would like to express its appreciation to the Delaware Division of the Arts (DDOA) and the Welfare Foundation for their generous support, assistance, and leadership on this endeavor to examine and understand the financial characteristics of Delaware arts organizations.

In many ways, this study breaks new ground as there are few existing surveys that approach the financial analyses of individual nonprofit “sub-sectors” (by program type and geographic base).

A special thanks to Paul Weagraff of DDOA and Peter Morrow of the Welfare Foundation for providing valuable direction and input.

NFF also would like to thank and recognize the nonprofit organizations represented in this survey for the tireless work they carry out every day.



Summary of Key Findings

From its extensive work in the nonprofit sector, NFF often observes the dilemma of organizations operating near the margin, barely covering annual expenses. Organizations that operate with thin margins over time are often forced to devote much of their time and attention to *survival* rather than the delivery of critical programs. With little opportunity to set aside reserves for crucial needs (such as facility repairs, growth, or “rainy days”), organizations risk their very existence in the long-term.

Nonprofit arts organizations in the state of Delaware are no exception. NFF’s analysis of 33¹ Delaware arts organizations reveal ongoing hardships and a financially precarious position. Key findings of this study are:

1. The vast majority of organizations were small to medium-sized, yet only the eight largest players drove the majority of economic activity.
2. Organizations operated near the break-even point from year to year.
3. Expense growth remained less than the inflation rate during most years.
4. Organizations cannot rely on a single income stream and must generate revenue from a combination of sources in order to cover annual expenses.
5. Facility growth was significant for one key player but remained modest for most organizations.
6. Without adequate preparation and resources, facility ownership can endanger organizations’ financial sustainability. For example, facility owners in this study tended to have less of a cash cushion than their counterparts.

Given these findings, NFF encourages further discussion by the wider community about *what will it take* (in the form of dollars and cents, support, and assistance) to fully capitalize this arts community? *See Slide 37.*



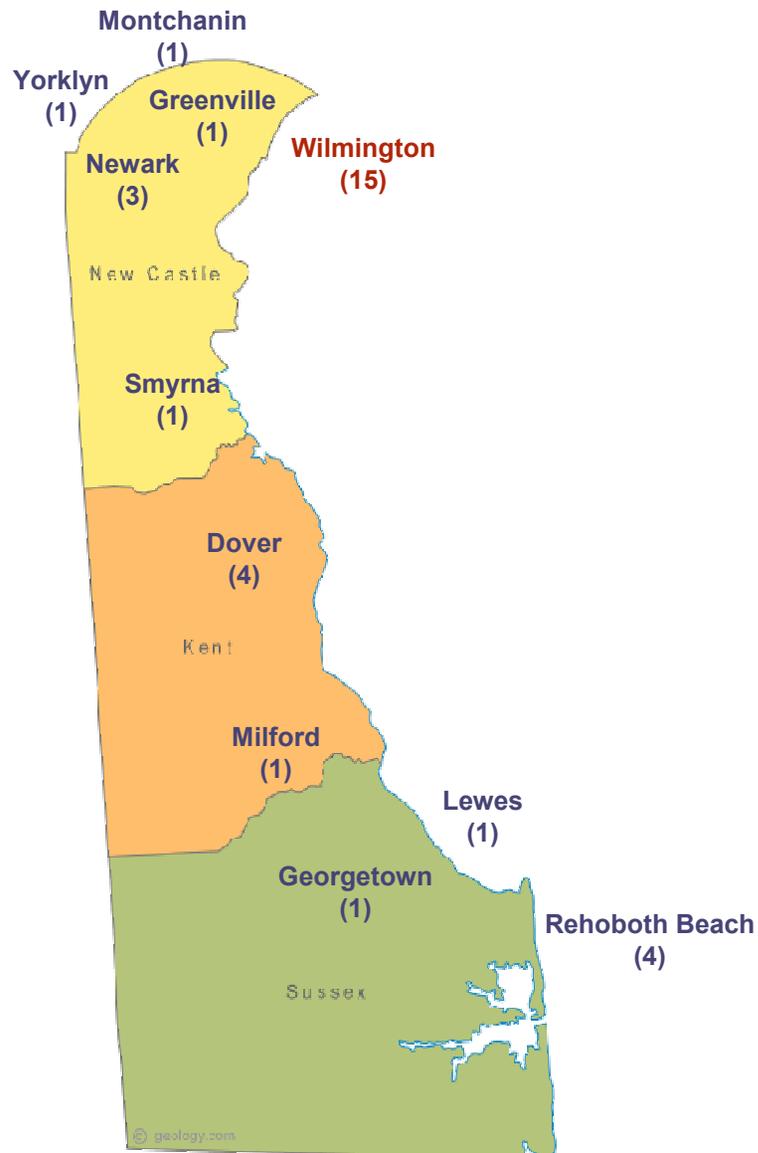
1. Note: 2006 data was not available for 1 organization with a reported expense size of \$38,000 in 2005.

Key Finding #1

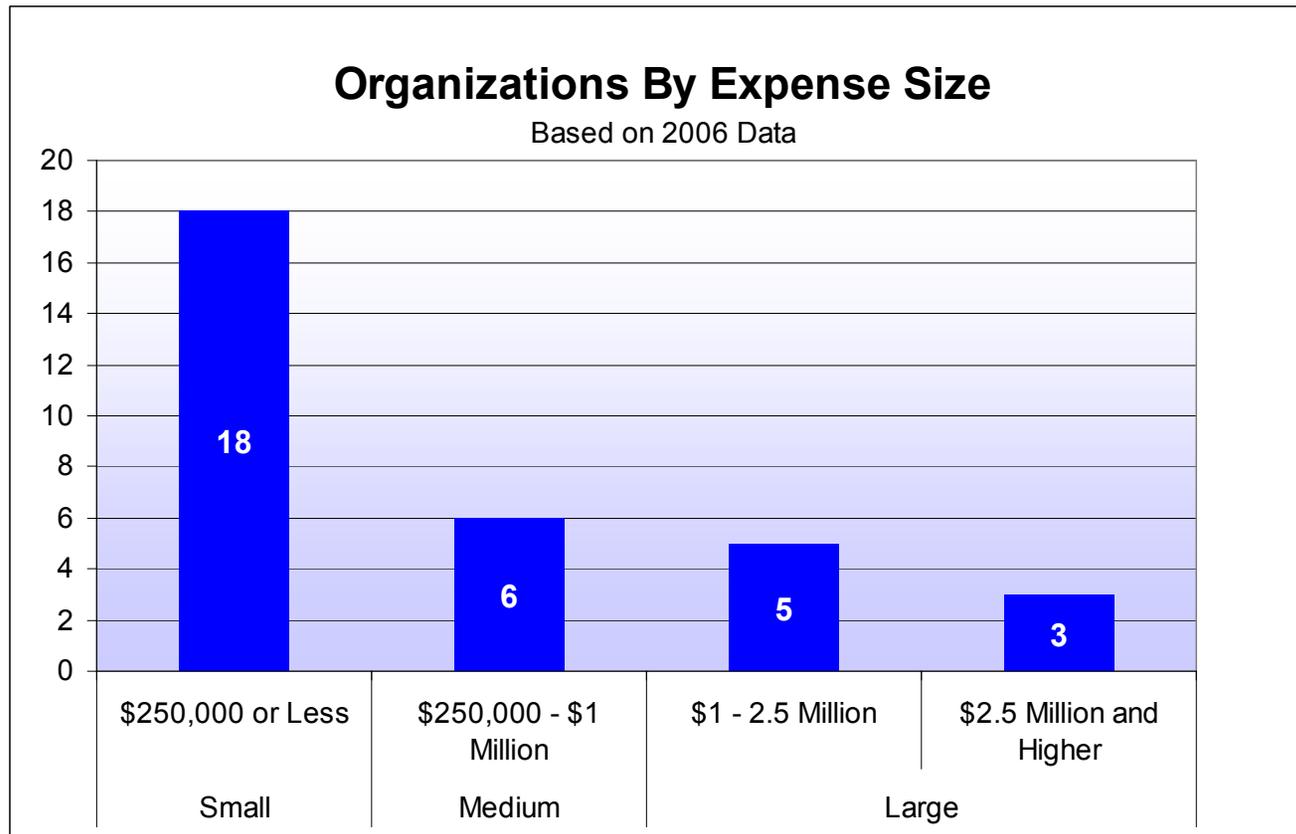
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Nearly half of the organizations were based in the city of Wilmington.



Over 75% were small to medium organizations (budgets of \$1 million or less).



Notes: Budget categories are based on information from The Alliance For the Arts.

Budget Categories

Small organizations

Annual budgets of up to \$250,000.

Medium organizations

Annual budgets between \$250,000 - \$1 million.

Large organizations

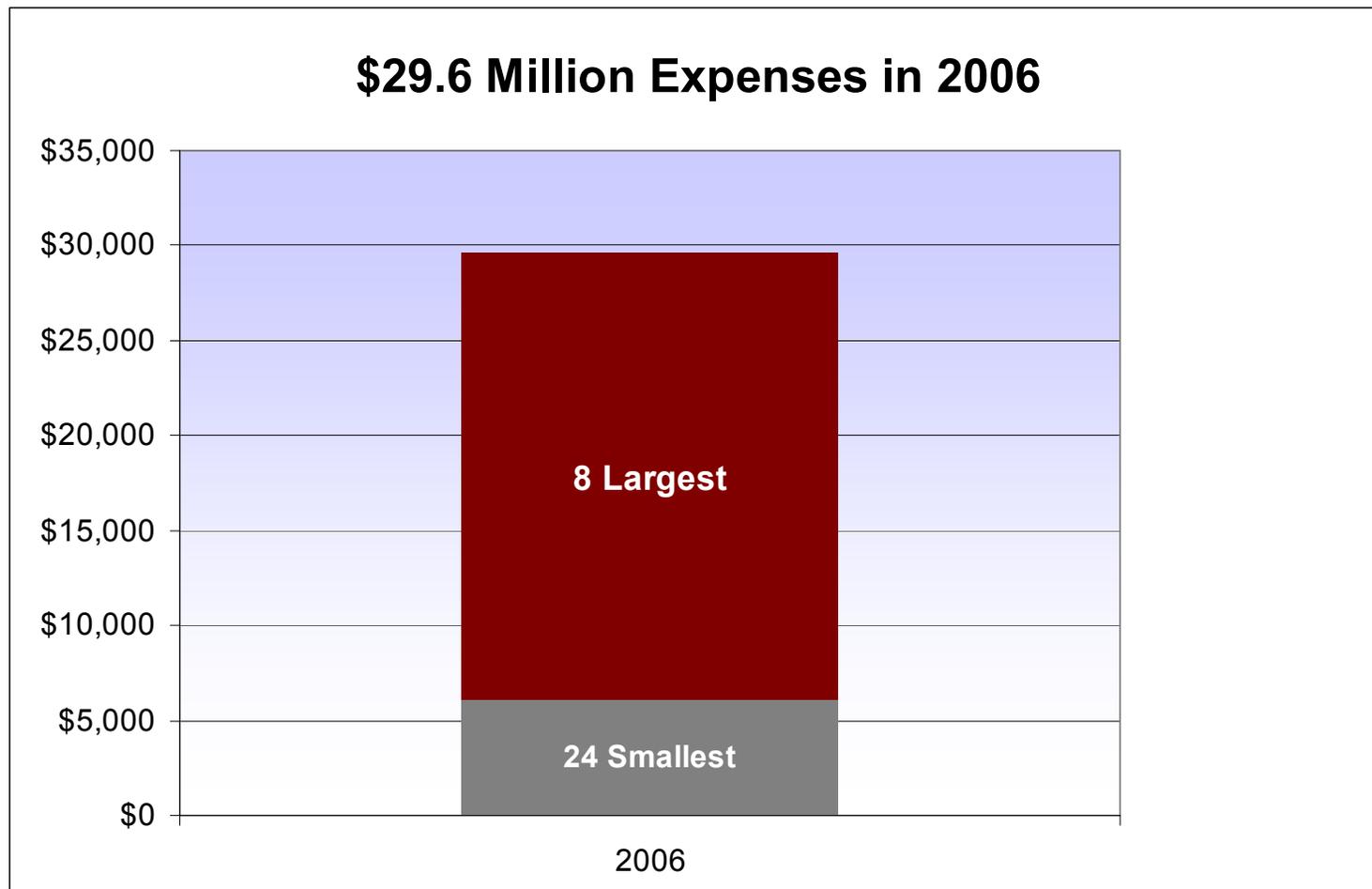
Annual budgets between \$1 million - \$10 million.

Very Large organizations

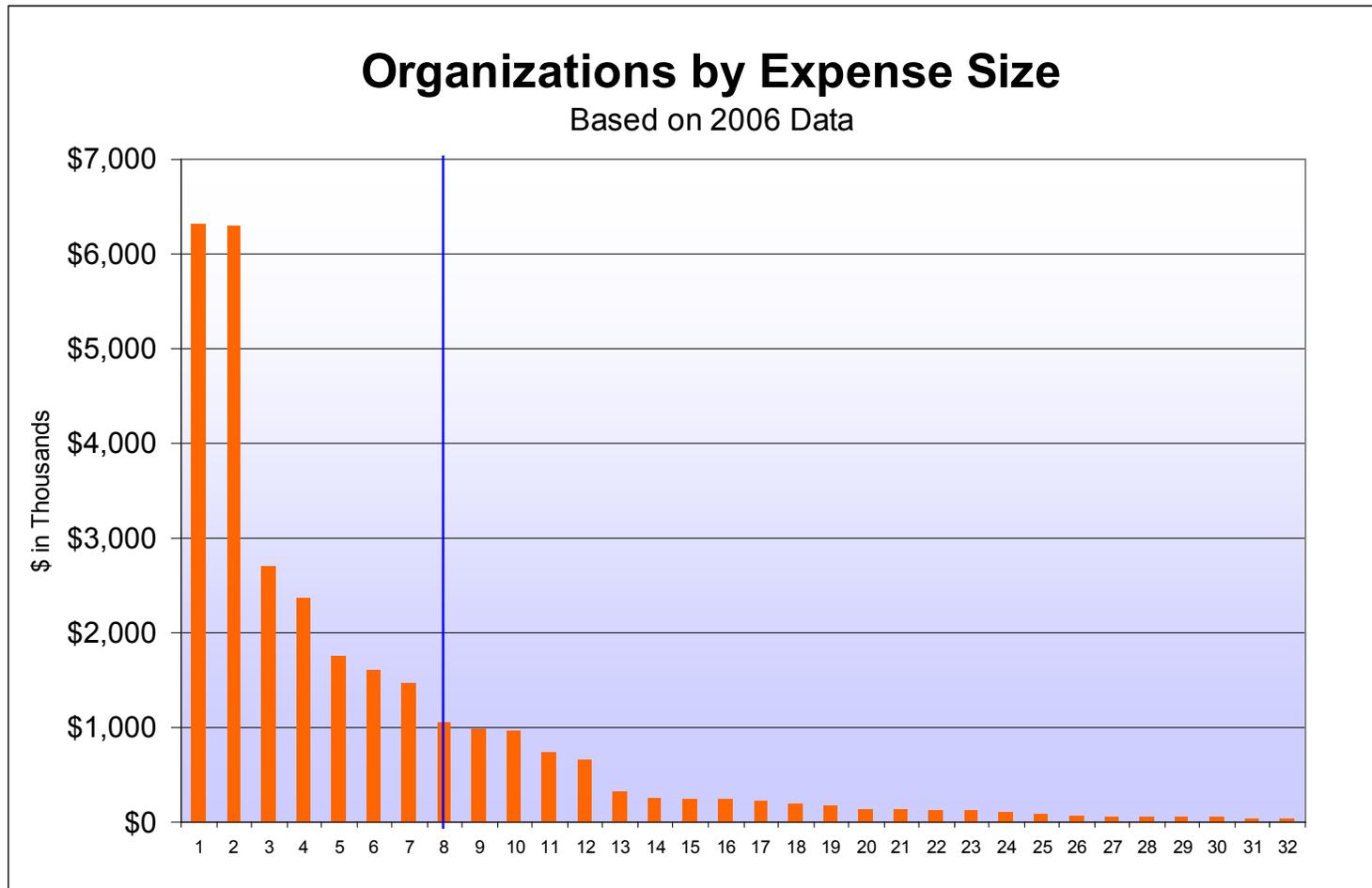
Annual budgets greater than \$10 million.



In 2006, the group generated \$29.6 million in operating expenses – 80% was generated by the eight largest organizations.



The eight largest organizations had operating budget sizes of \$1 million or higher.

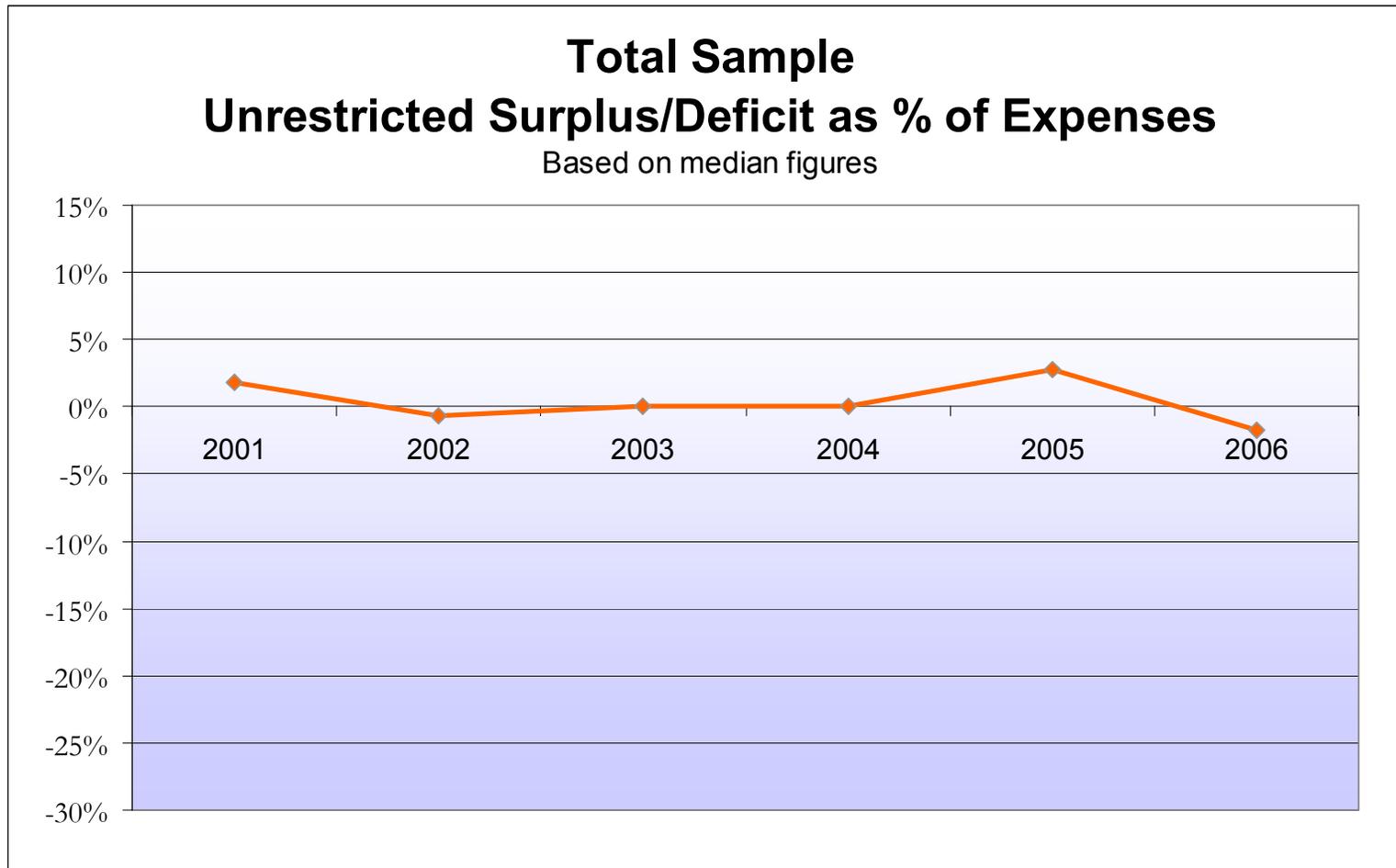


Key Finding #2

1. The vast majority of organizations were small to medium-sized, yet only the eight largest players drove the majority of economic activity.
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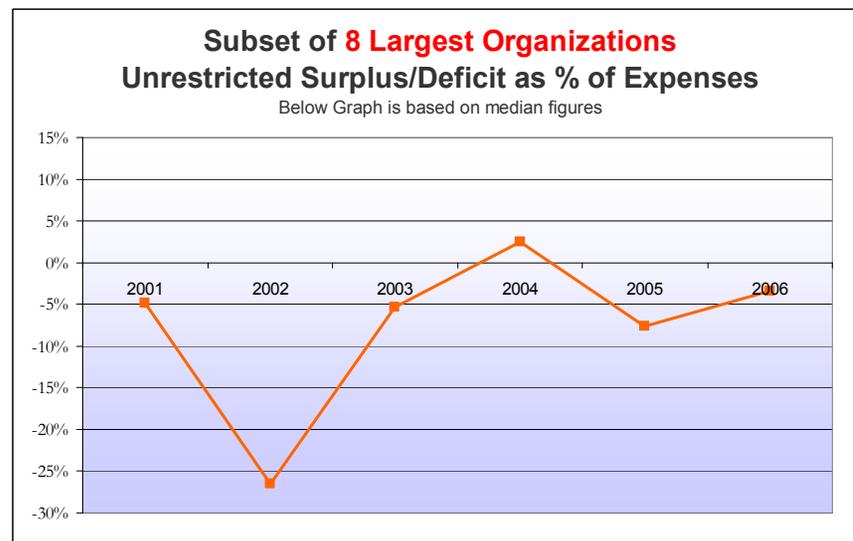
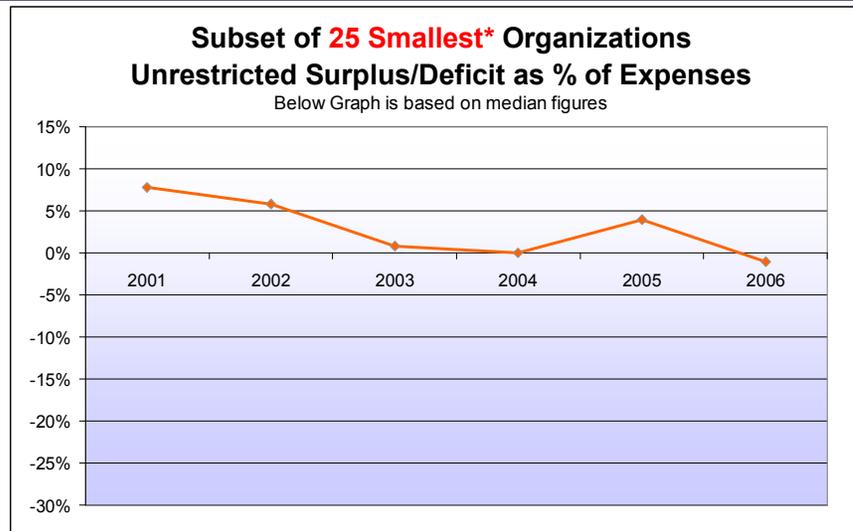
Organizations narrowly covered operating expenses from year to year.



Notes: (1) The “unrestricted surplus/deficit” is defined as the change in unrestricted net assets; (2) In the cases in which organizations did not report restricted categories of net assets, NFF assumed that “total net assets” were unrestricted.



The 8 largest organizations demonstrated more severe operating volatility than their smaller counterparts.



*Note: 2006 data was not available for 1 organization with a reported expense size of \$38,000 in 2005.

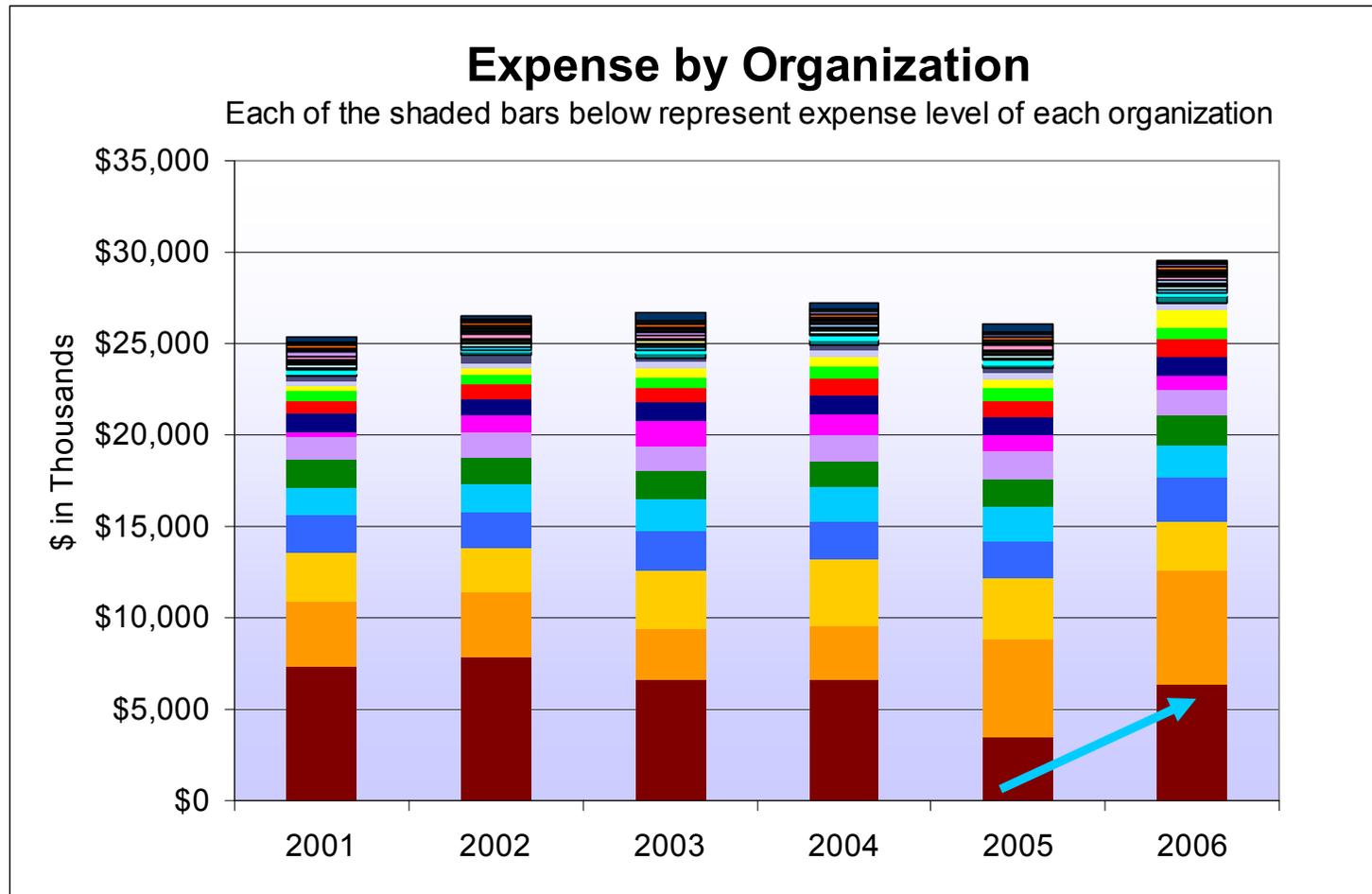


Key Finding #3

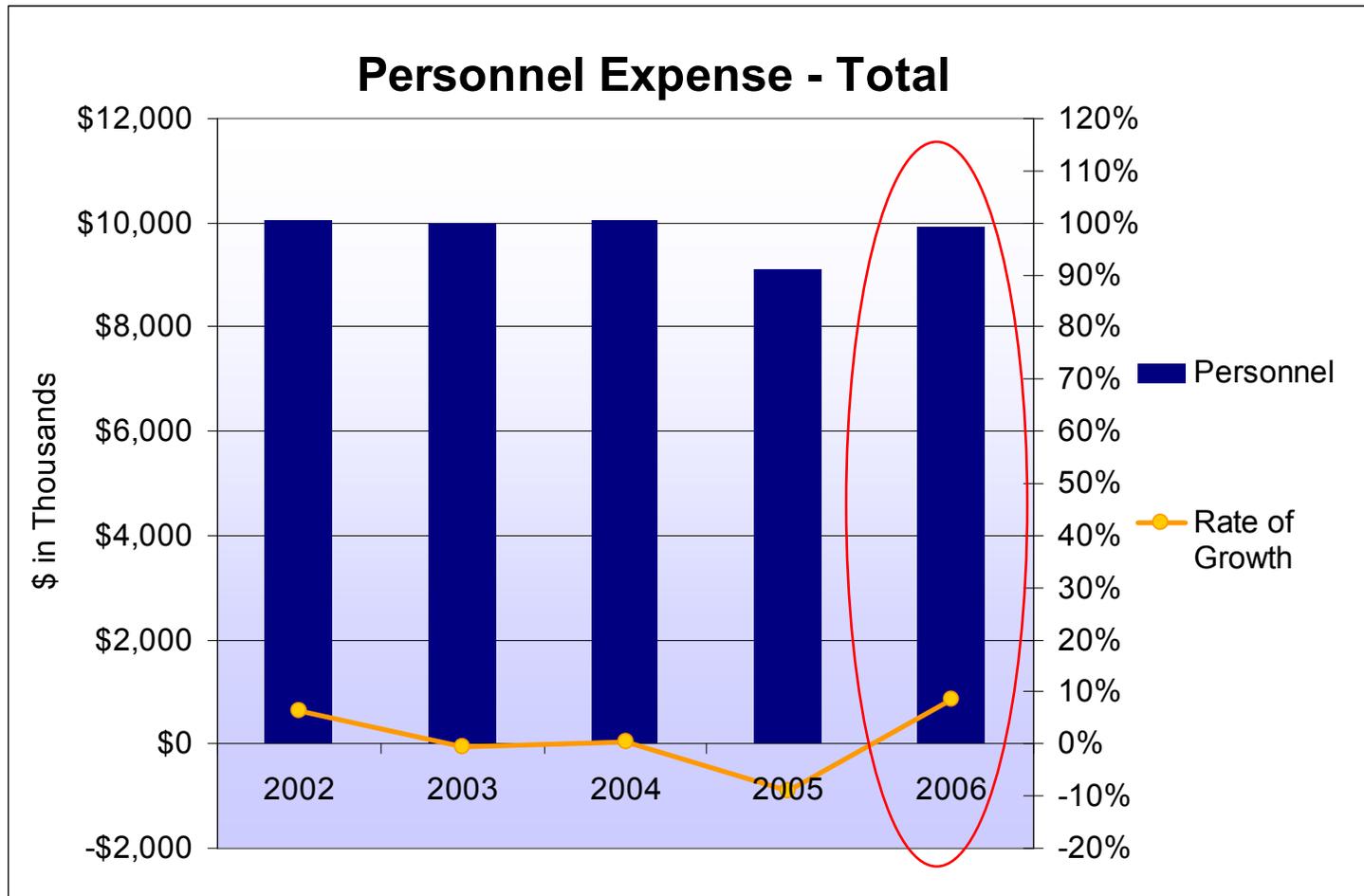
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Aggregate expenses grew at less than the rate of inflation between 2003 – 2005. In 2006, expenses grew by 14% and was primarily driven by 1 organization.

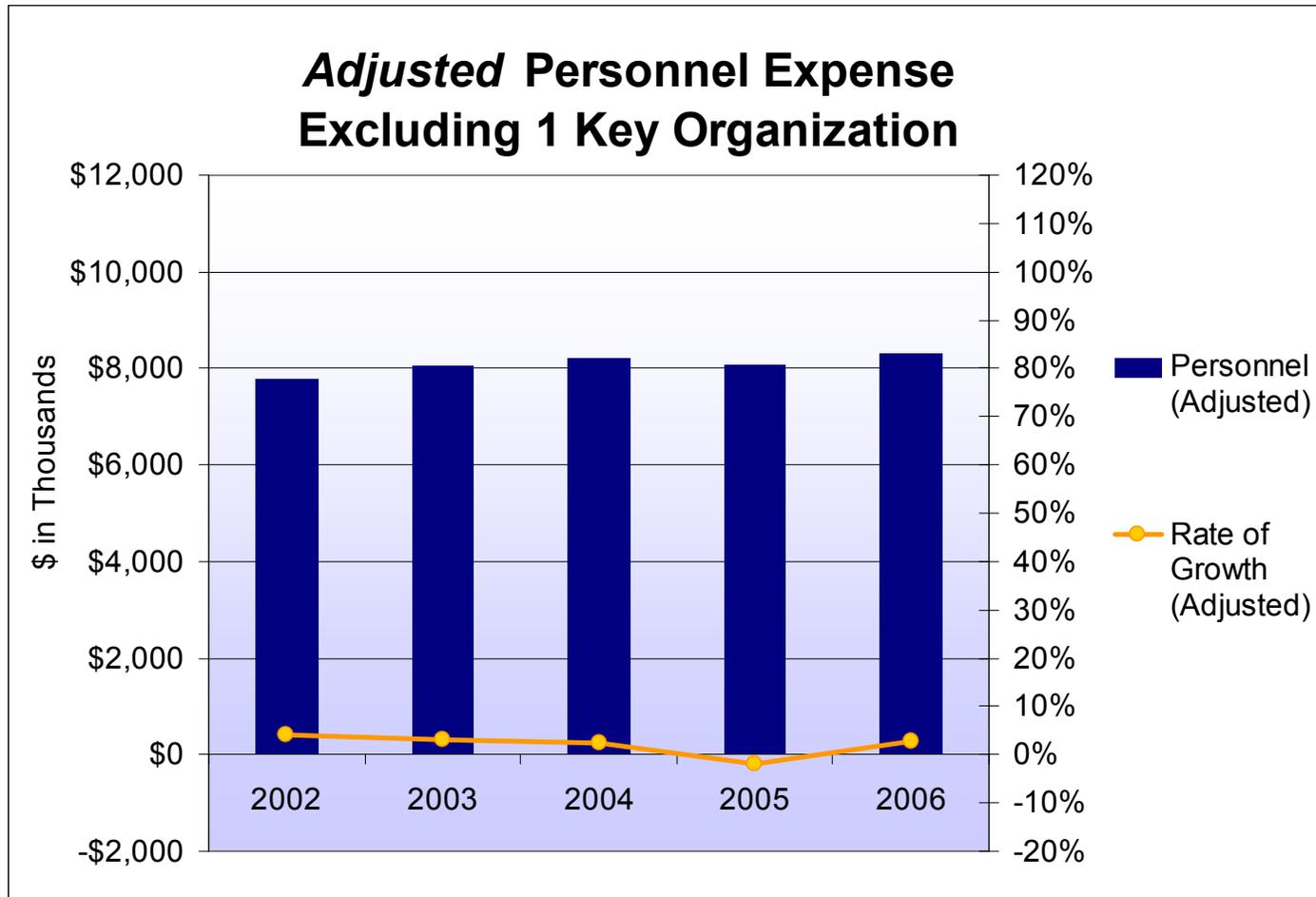


Personnel expense grew by 9% in 2006, and was also driven by the outlier organization.

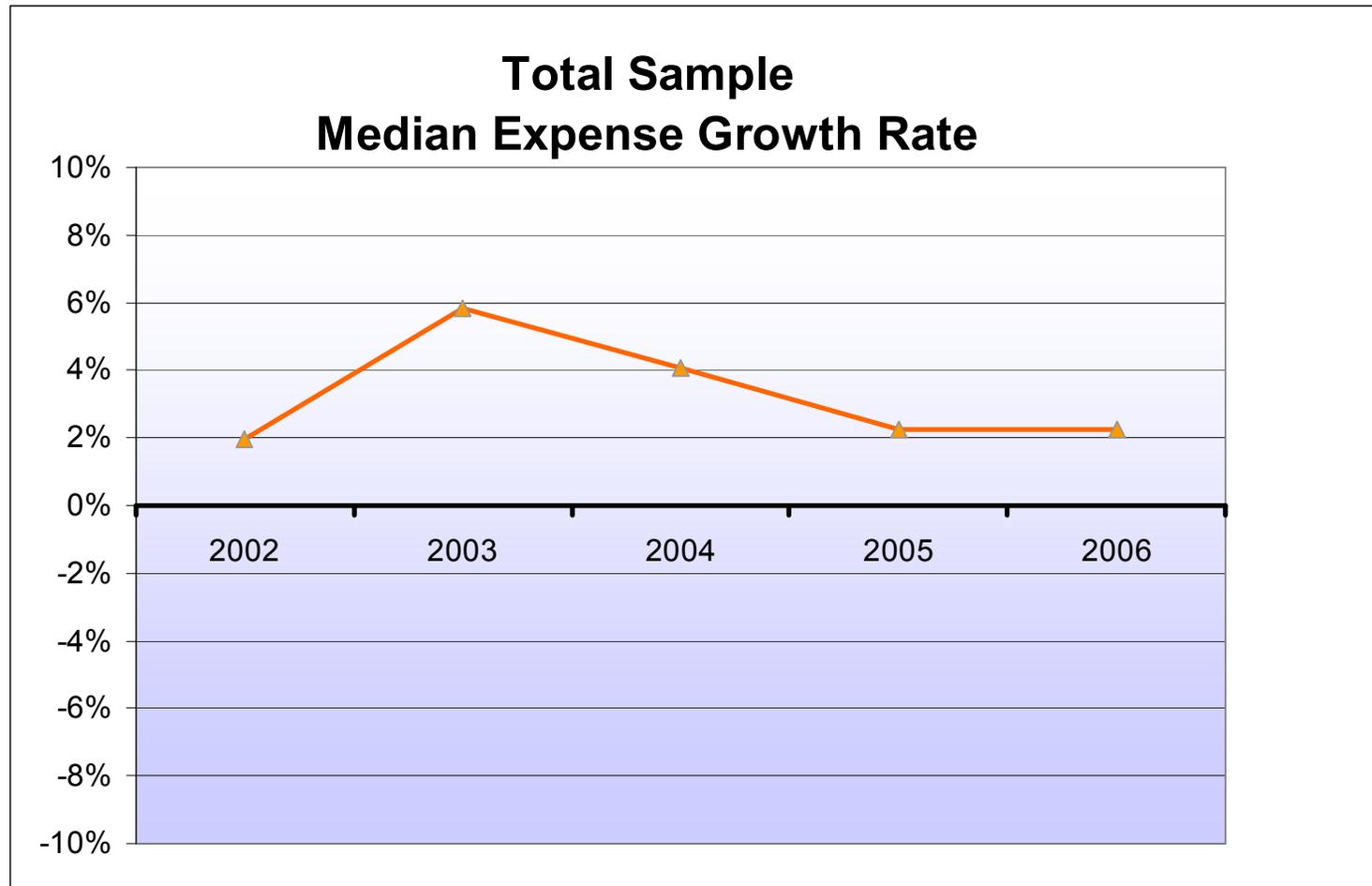


After adjusting for this organization, the rest of the group managed personnel expense at minimal growth throughout the six-year period.

After adjusting for the outlier organization, the average annual growth rate of personnel was 2% during the period.



The median expense growth rate suggests minimal cost increases. The median leveled off at the 2% level in 2005 and 2006.

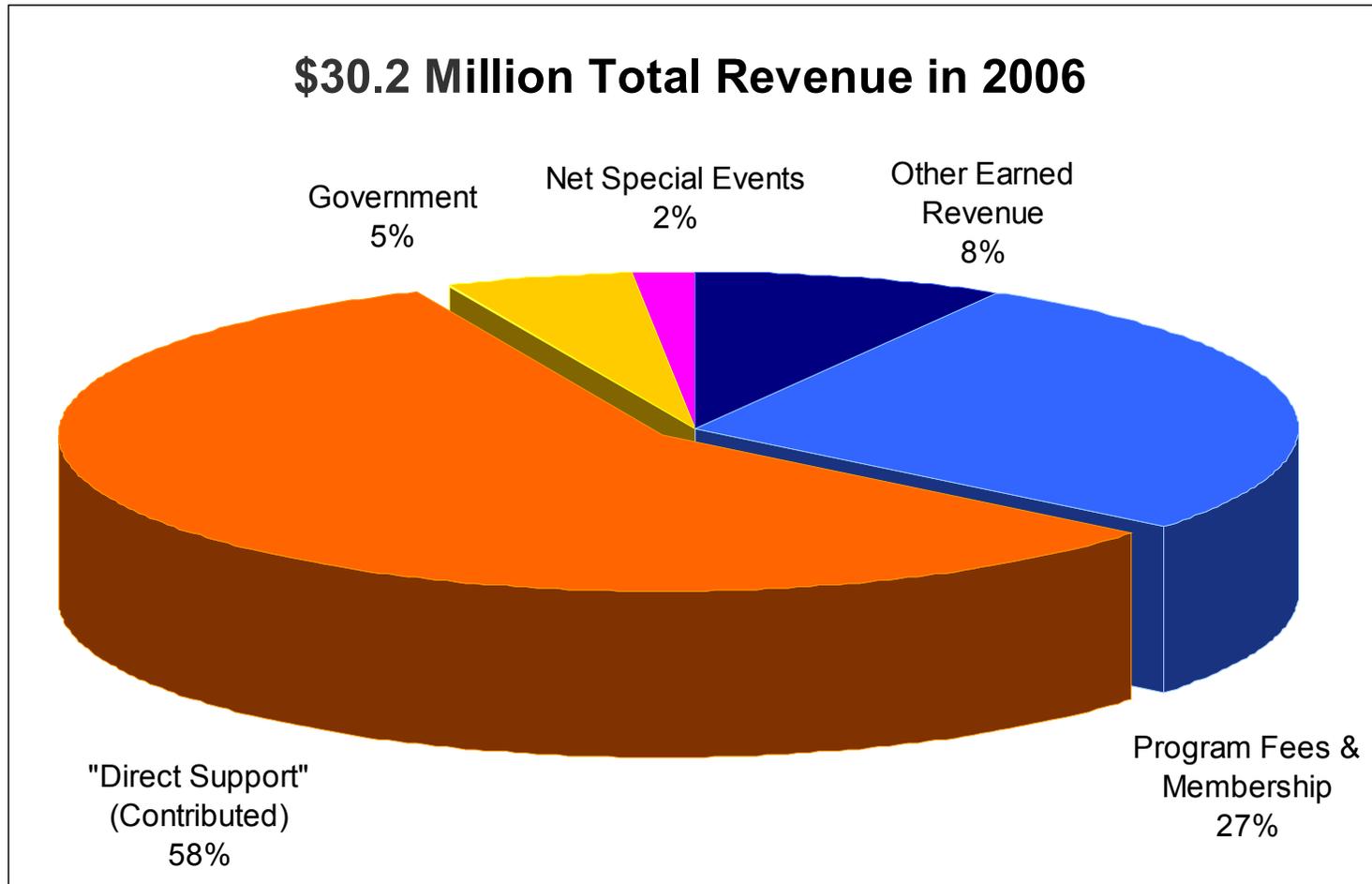


Key Finding #4

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Revenue mix was divided between a variety of sources, with contributed funds representing close to 60% in 2006.



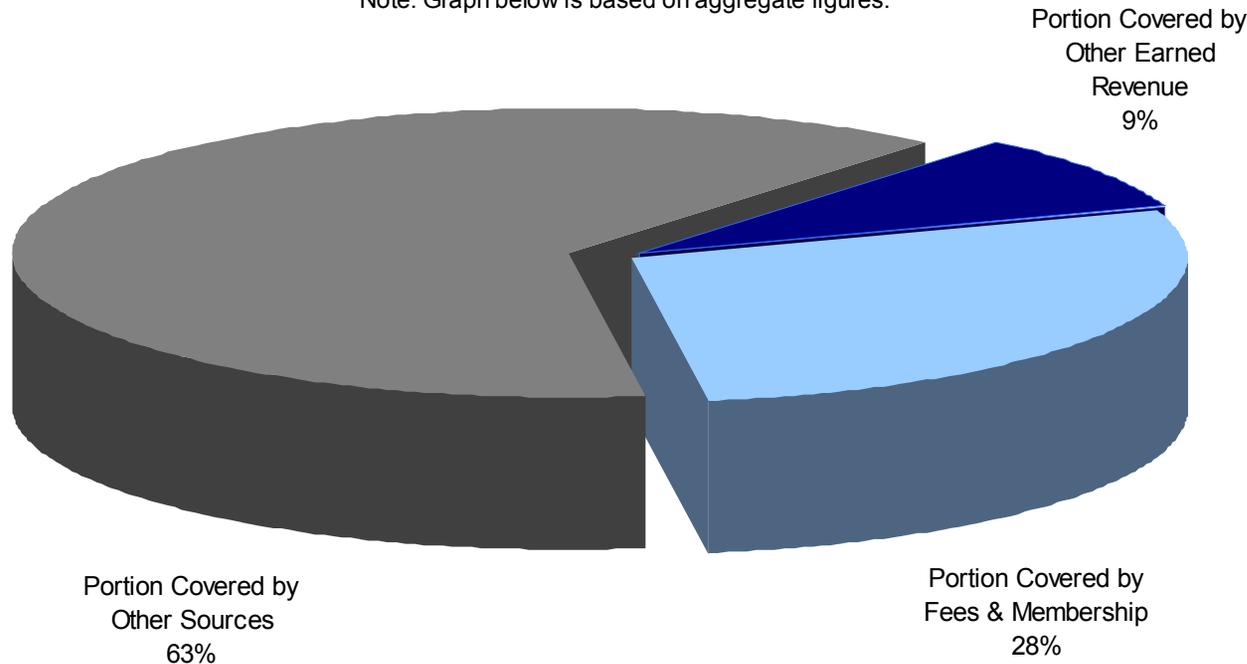
Notes: (1) "Direct support" typically includes a wide variety of contributed funds, such as individual donations and foundation/corporate grants; (2) "Other earned revenue" consists of investment, rental, advertisement and other income; (3) Given the nature of IRS Form 990 data, revenue figures are based on "total" revenue, which includes any restricted funds.



Organizations had to cover over half of total operating expenses with fundraising dollars in 2005.

\$29.6 Million in Expenses in 2006

Note: Graph below is based on aggregate figures.



Notes: "Subsidy dollars" typically consist of contributed or fundraising revenue.

In 2006, earned revenue from program fees and membership dues covered 28% of total expenses. Dollars from investment, rental, advertisement and other income covered another 9%.

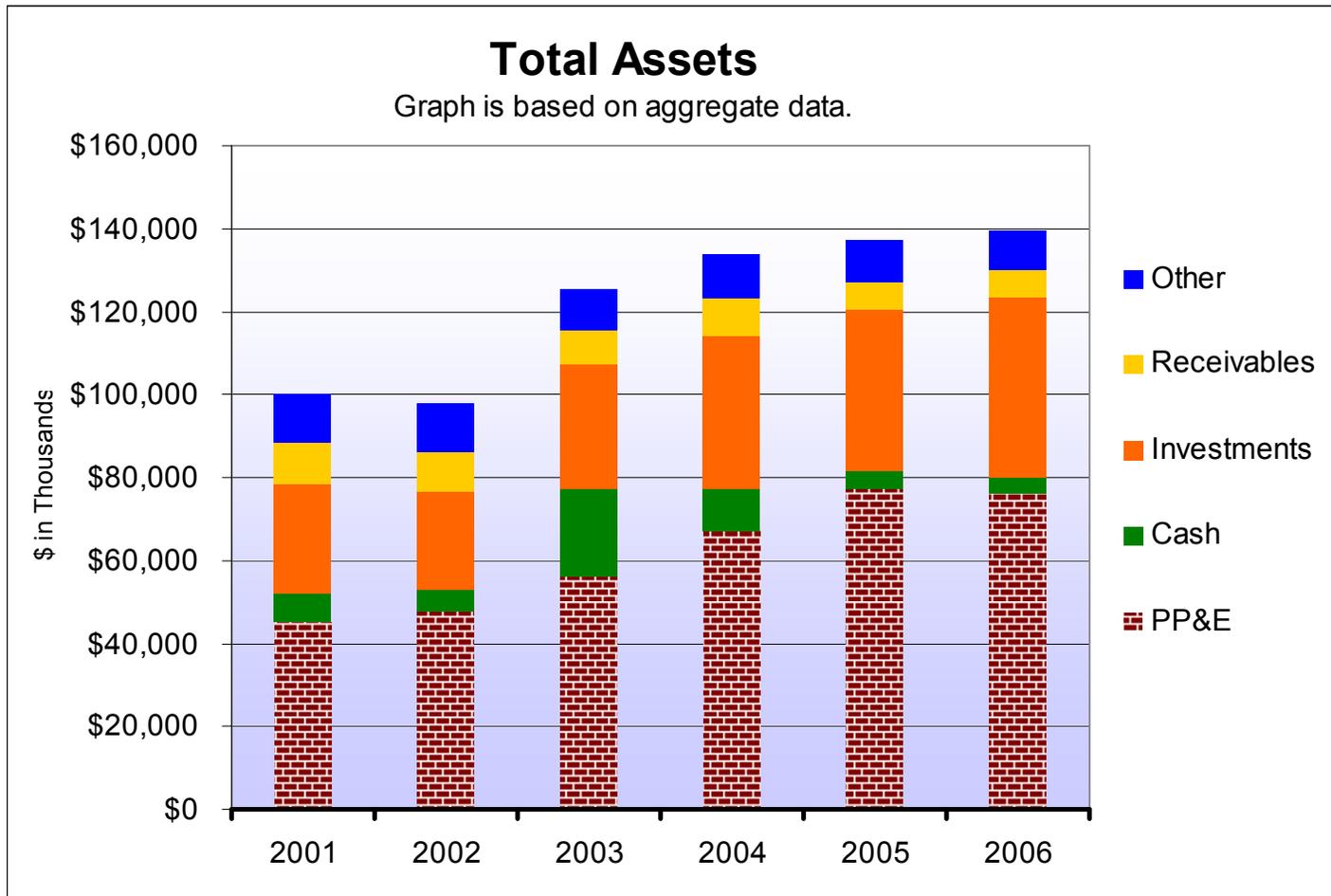
In order to cover the rest of expenses, organizations have to raise "subsidy dollars" and invest in fundraising.

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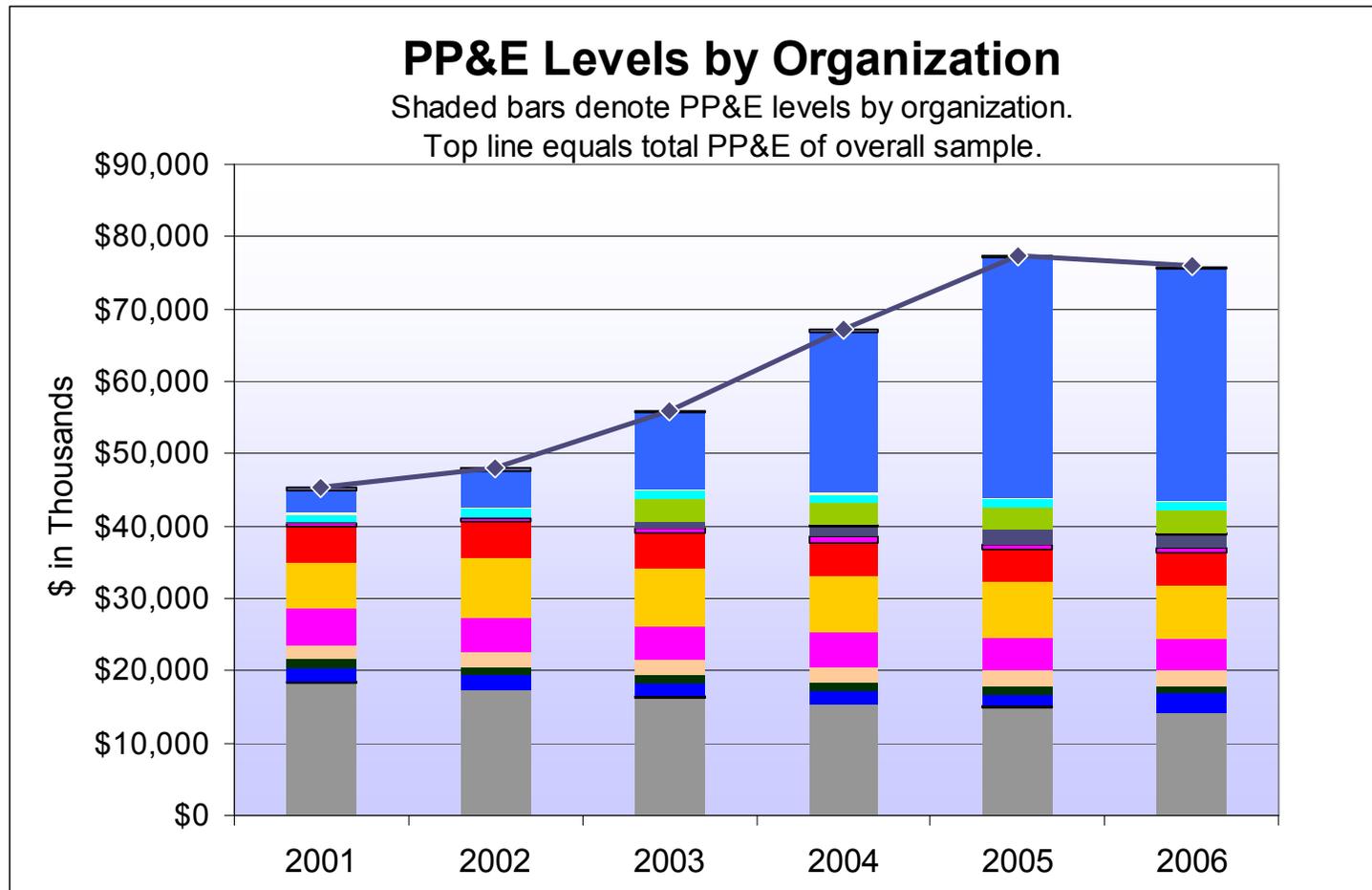
Combined assets grew by 39% between 2001 – 2006, driven in large part to a 62% growth in facility investments (i.e. “PP&E”).



Note: “PP&E” is defined as “property, plant & equipment” and is denoted in bricks above.



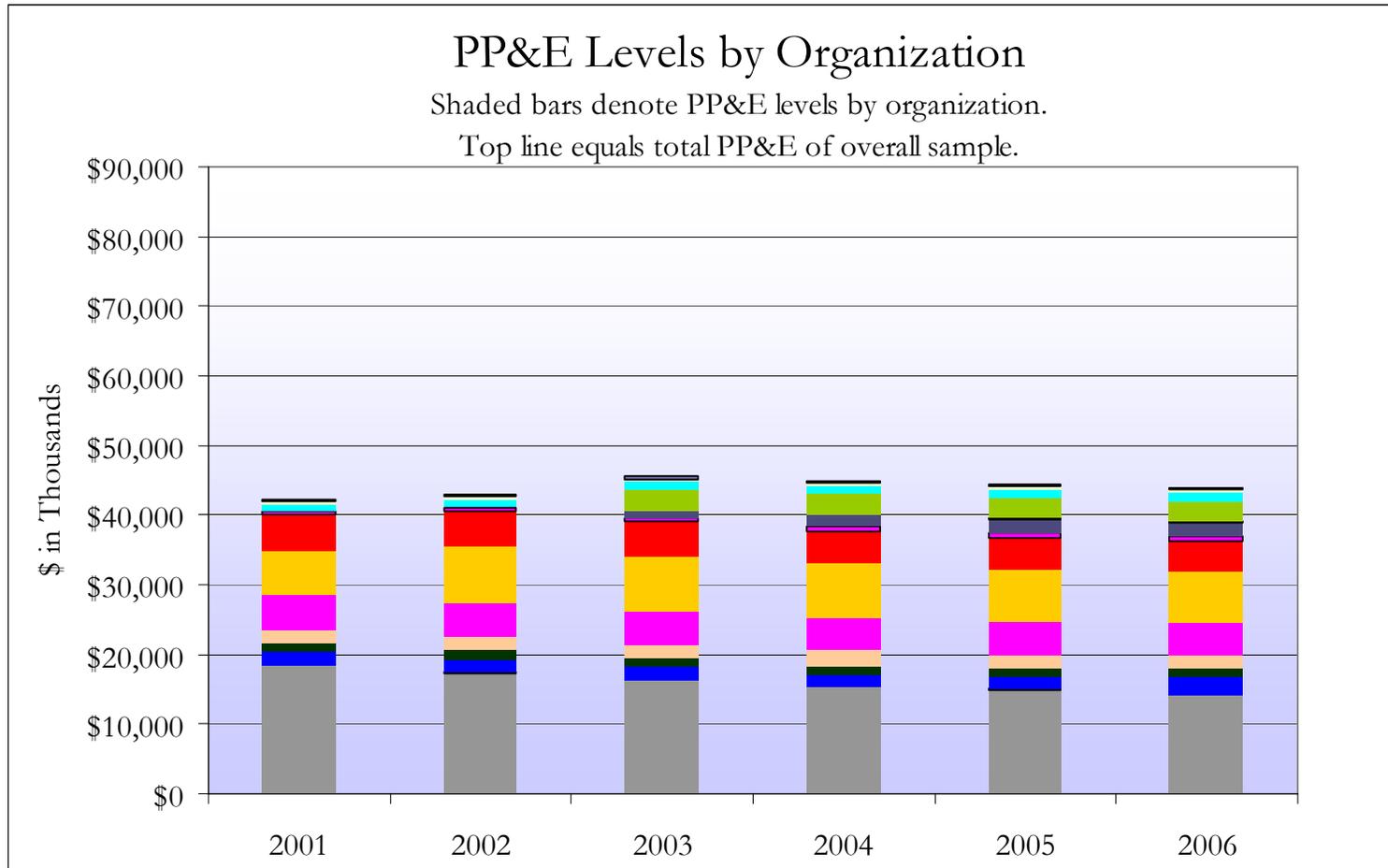
Yet, much of PP&E growth was driven by one key player.



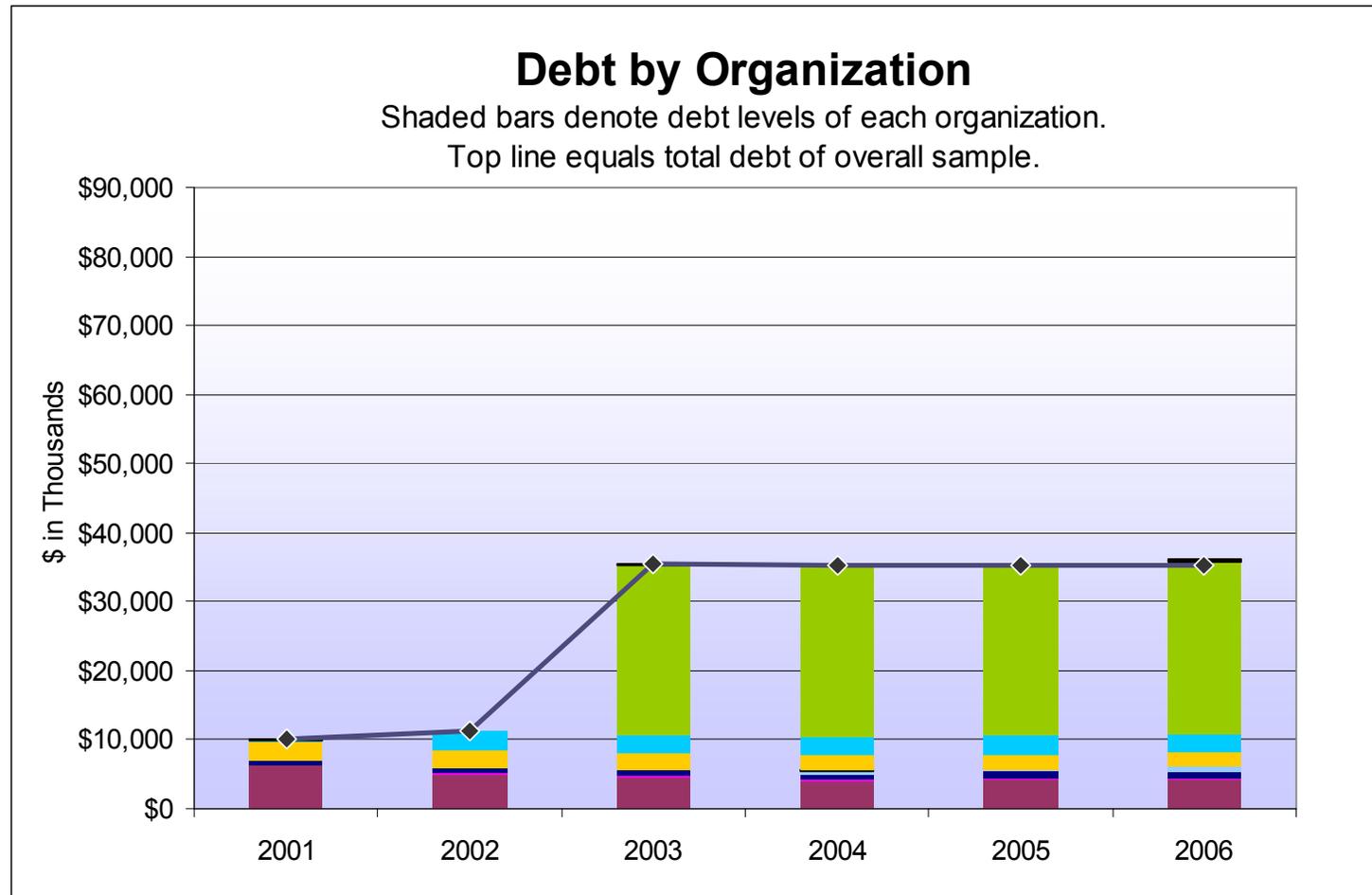
Of the 33 organizations in the sample, only 16 are facility owners and are represented in the shaded bars above. In 2006, combined net fixed assets totaled \$76.0 Million – of which 42% (or \$32.0 Million) was held by one organization.



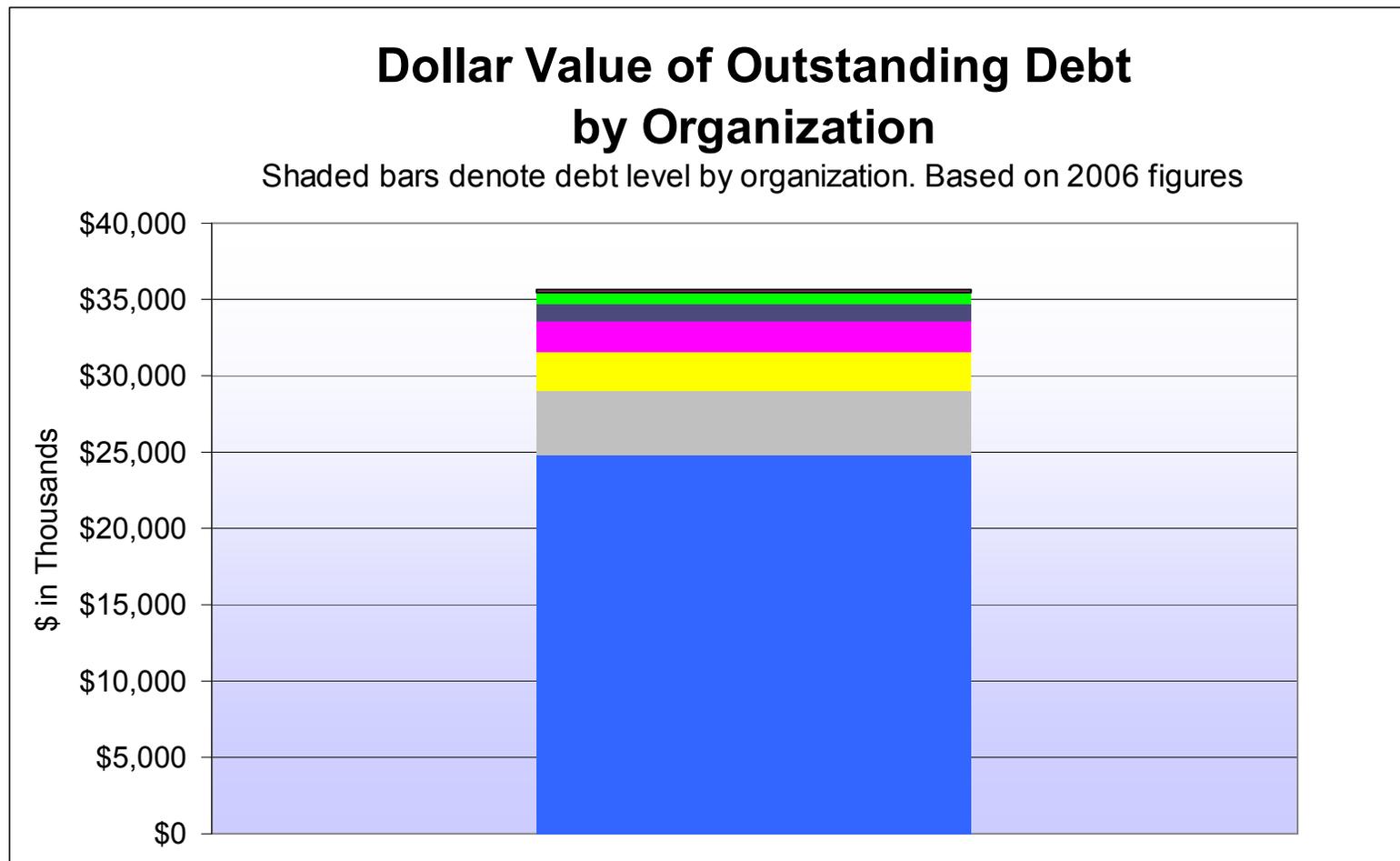
After excluding this outlier, the sample's PP&E remained relatively flat (average annual growth rate of only 1% between 2001 – 2006).



Similarly, debt was significant for this single agency. For the rest of the sample, debt remained relatively constant (1% average annual growth rate between 2001 – 2006).



At year-end 2006, outstanding debt totaled \$35.3 Million – of which 99% was carried by *only* seven organization with large facilities (i.e. gross PP&E of \$2 million or greater).

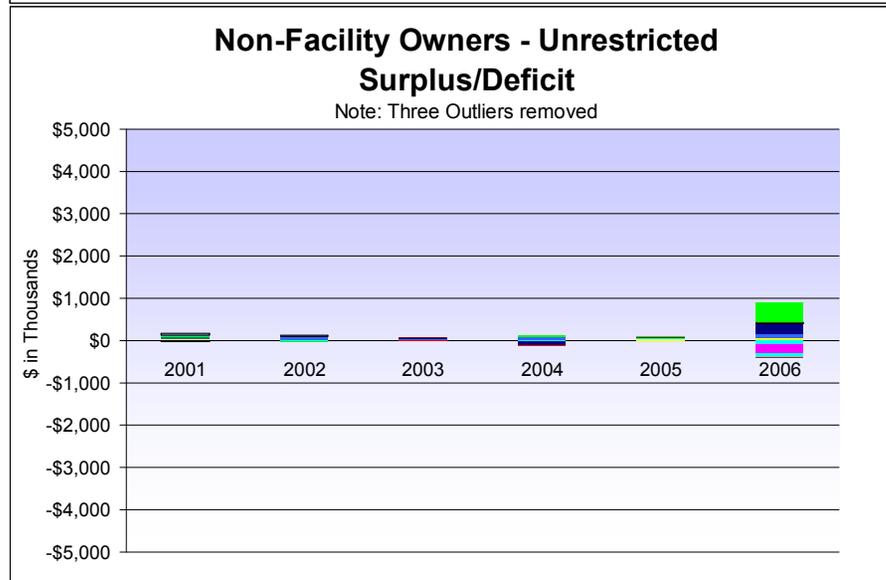
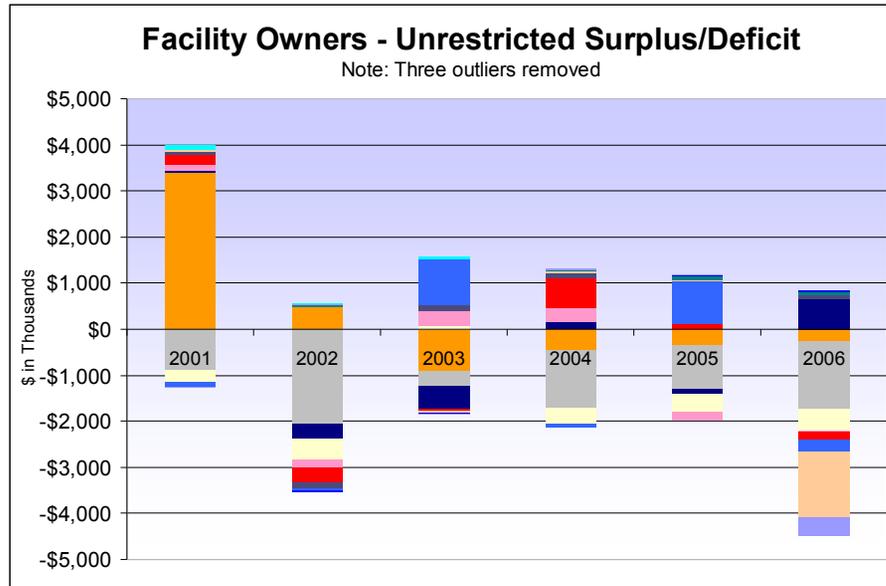


Key Finding #6

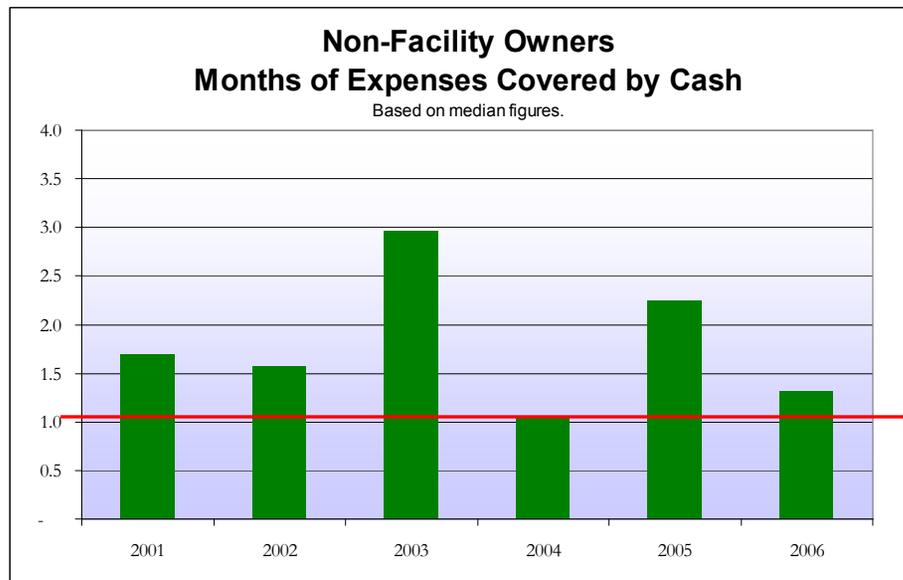
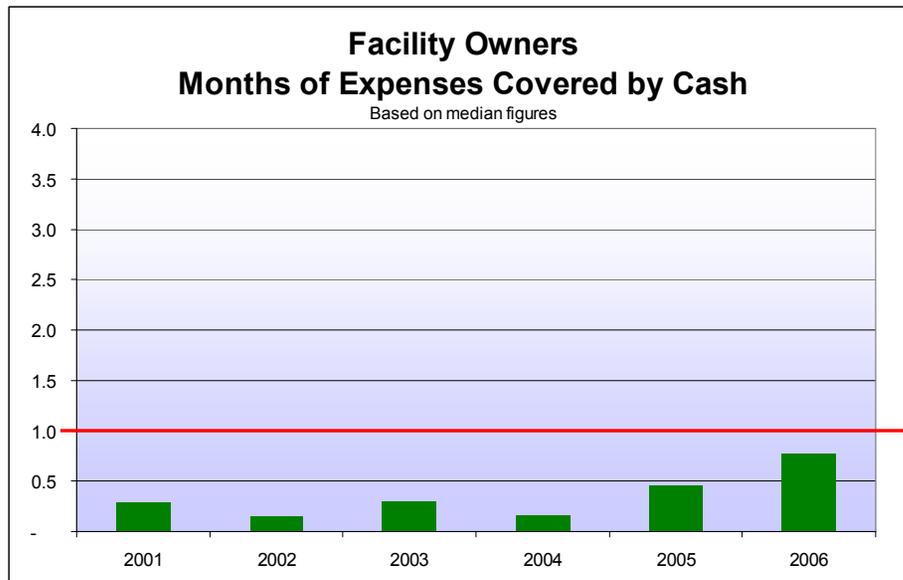
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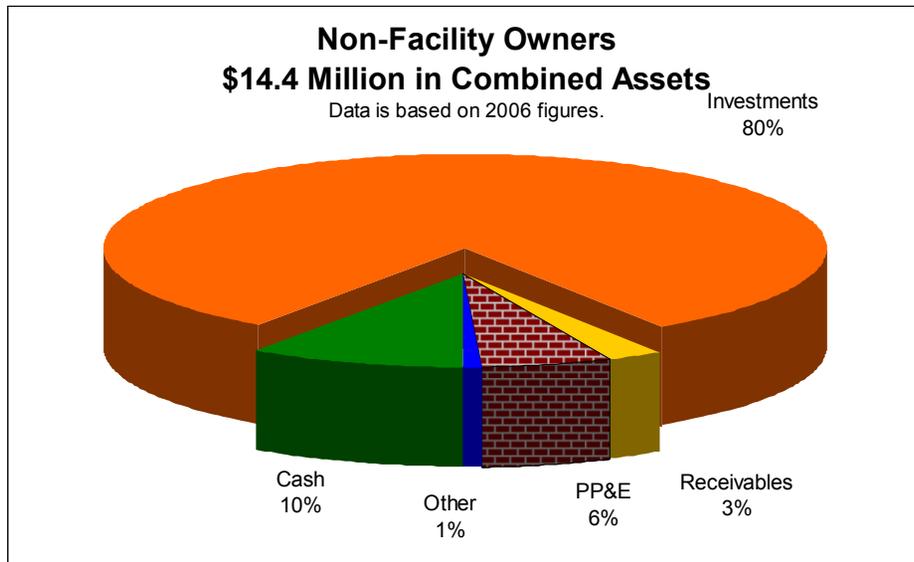
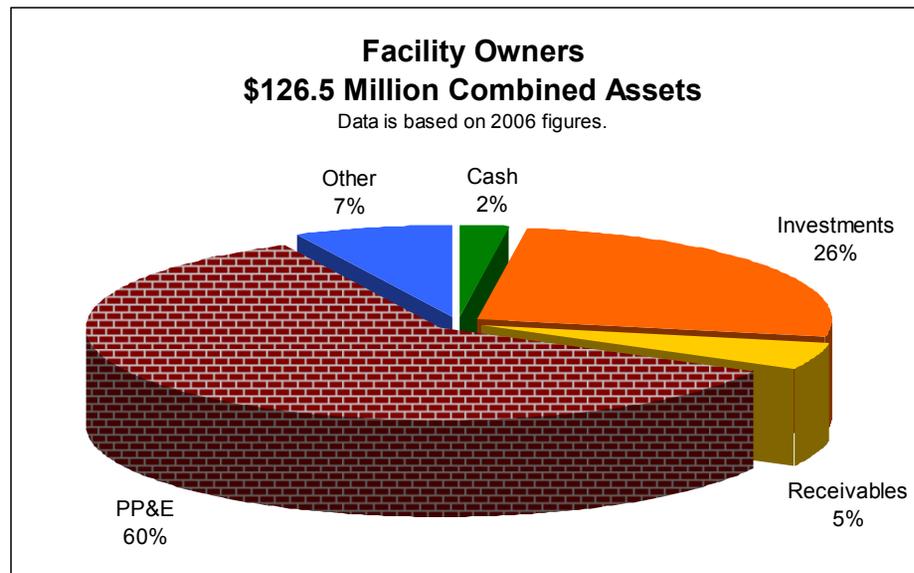
While non-facility owners tended to straddle the margin, facility owners showed greater volatility.



Facility owners tended to have lower levels of cash on hand, as compared to their peers.



Facility owners had low levels of flexible assets (i.e. cash and investments) relative to their peers.

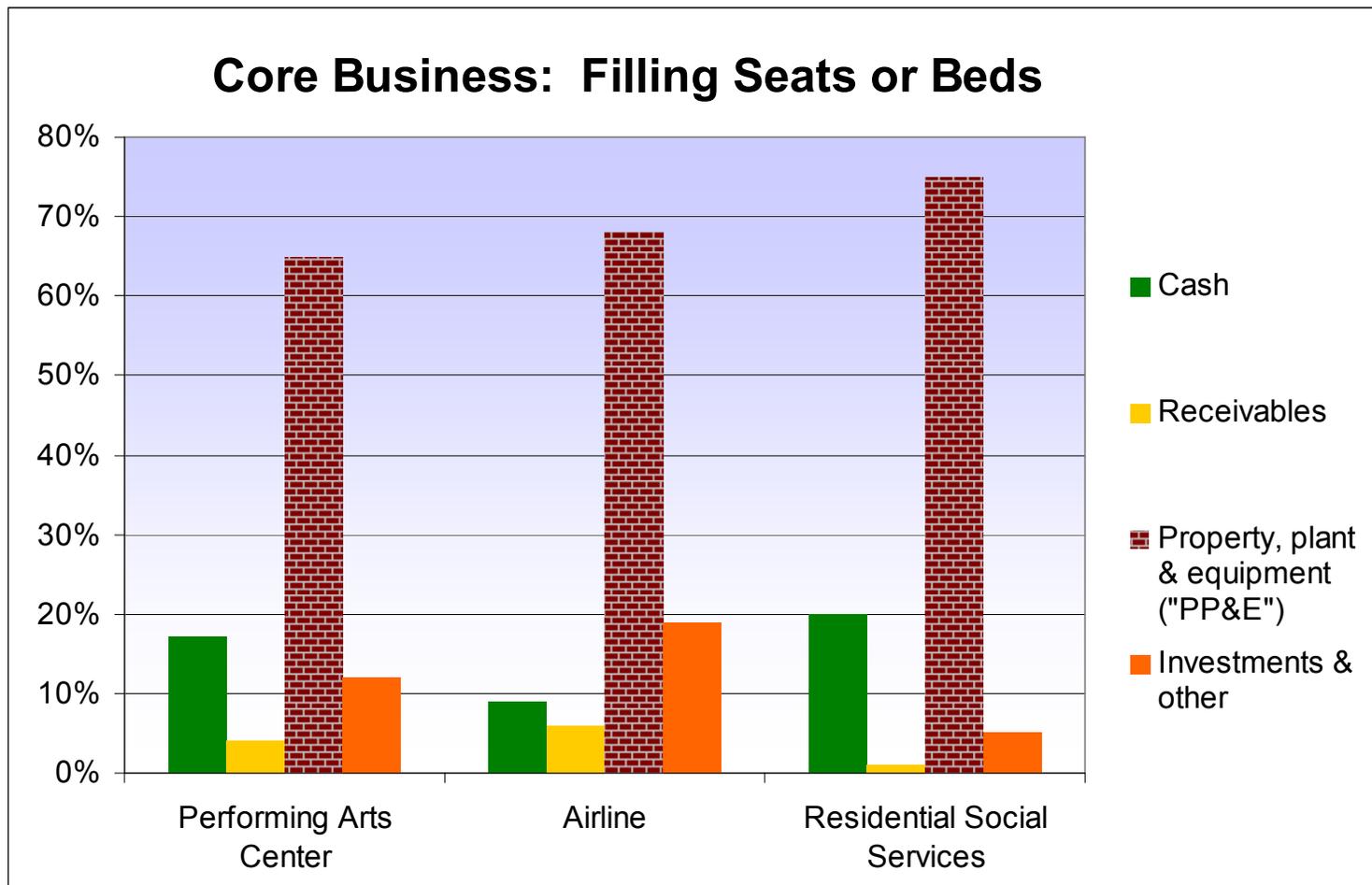


In order to approach the conversation about financial health, organizations and their investors need to understand the difference between program and “core business.”

- Any conversation about the financial health of the Delaware arts sector *must* distinguish between *business* and *mission*. For example, many organizations in this study share common “mission” goals.
- However, those that are in the “business” of facility ownership have capital needs that are dissimilar to their peers. Understanding this difference is a key requirement to answering: what does it *really* take for an organization to maintain “financial health”?
- Identifying the “core business” of an organization is an essential part of this process. *See the following slides.*



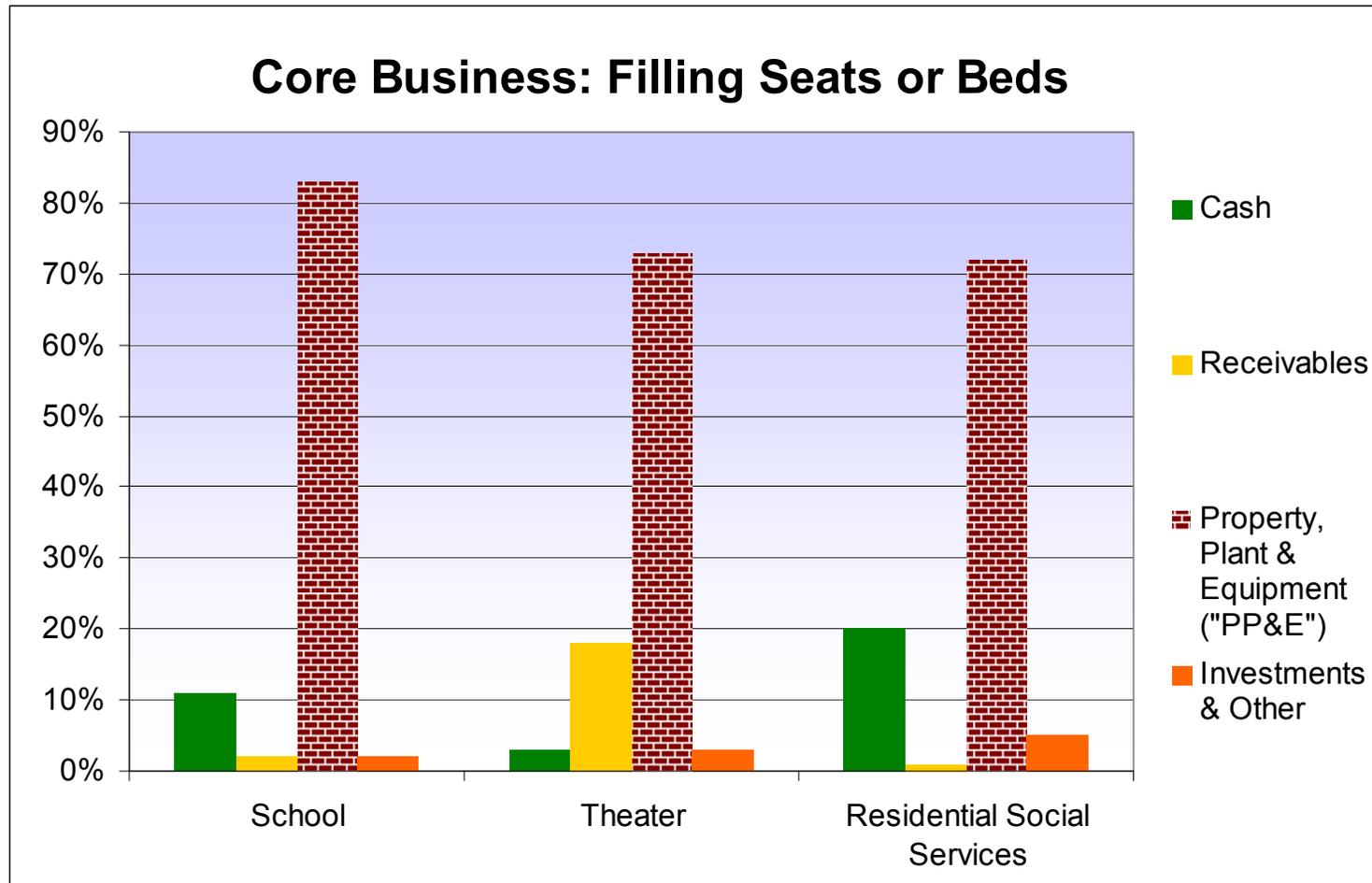
An organization's asset allocation reveals its underlying "core business."



The above graph is based on data outside of this study, and is intended to serve for example purposes only.



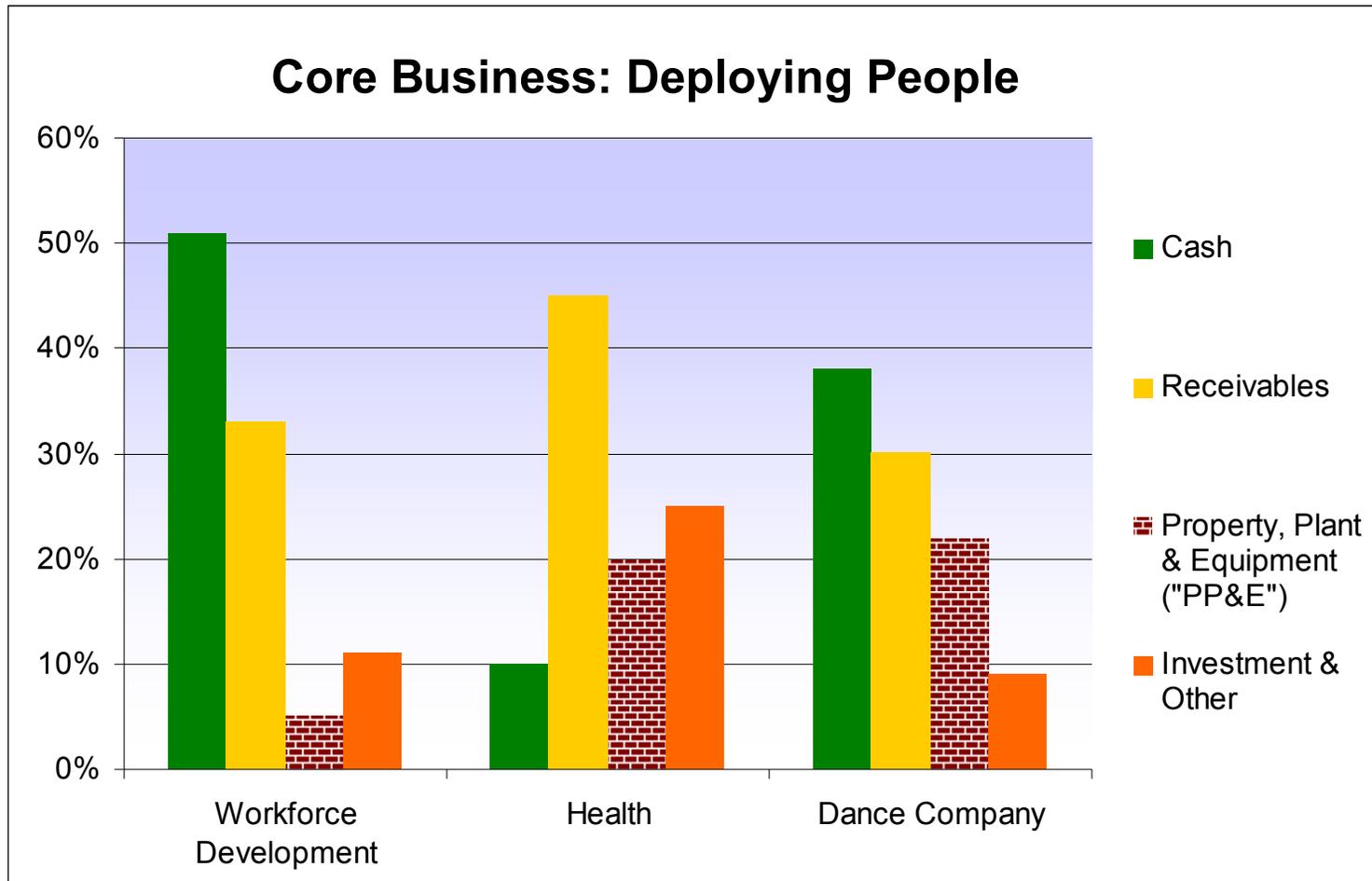
Organizations can share the same core business but operate in different sectors.



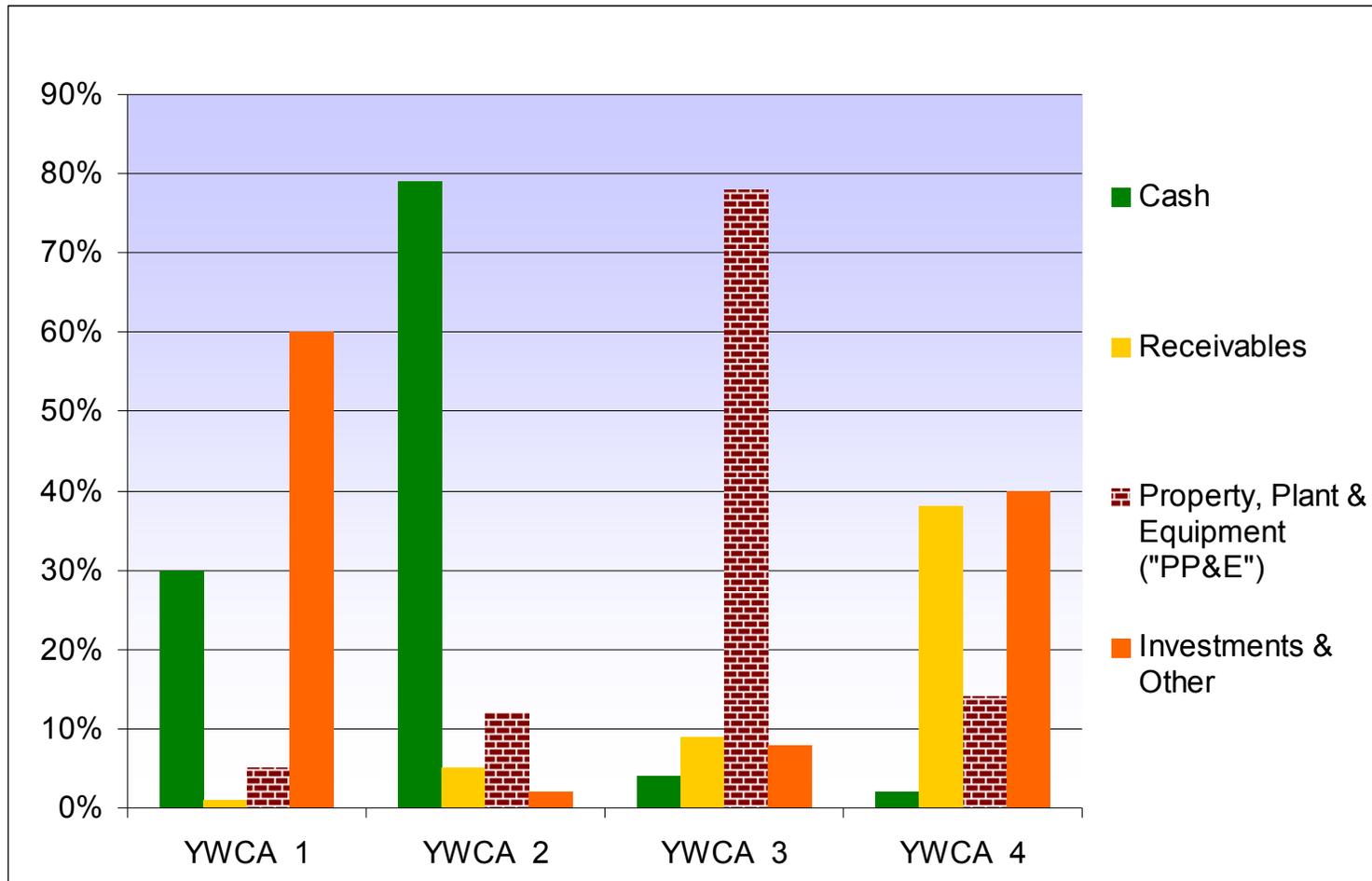
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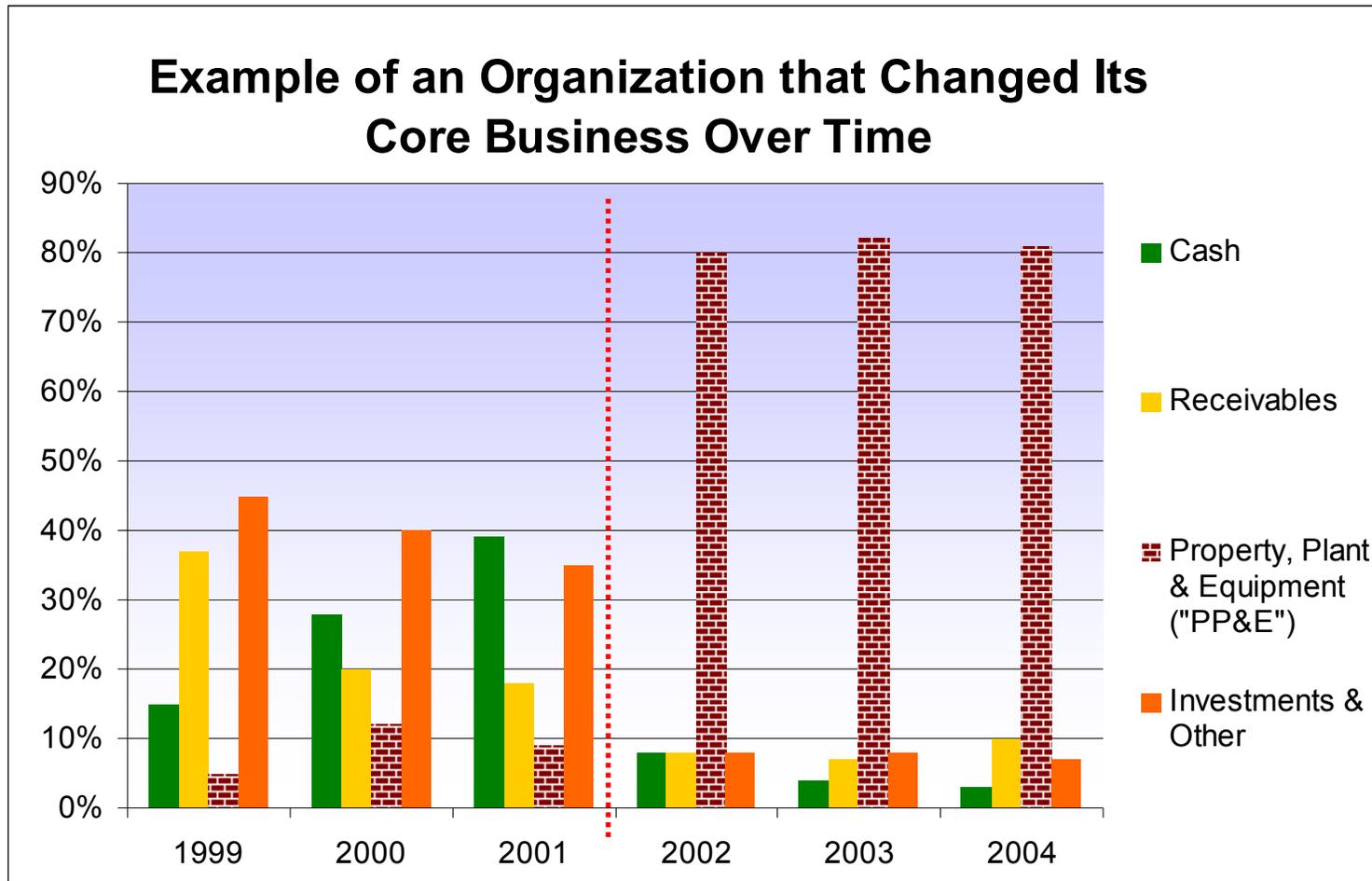
Organizations can have similar missions, yet have very different core businesses.



The above graph is based on data outside of this study, and is intended to serve for example purposes only.



Organizations facing facility ownership decisions must prepare for an even greater need for cash – so that programs do not suffer in the long-term.



The dotted line denotes a building purchase. The above graph is based on data outside of this study, and is intended to serve for example purposes only.



QUESTIONS FOR CONSIDERATION



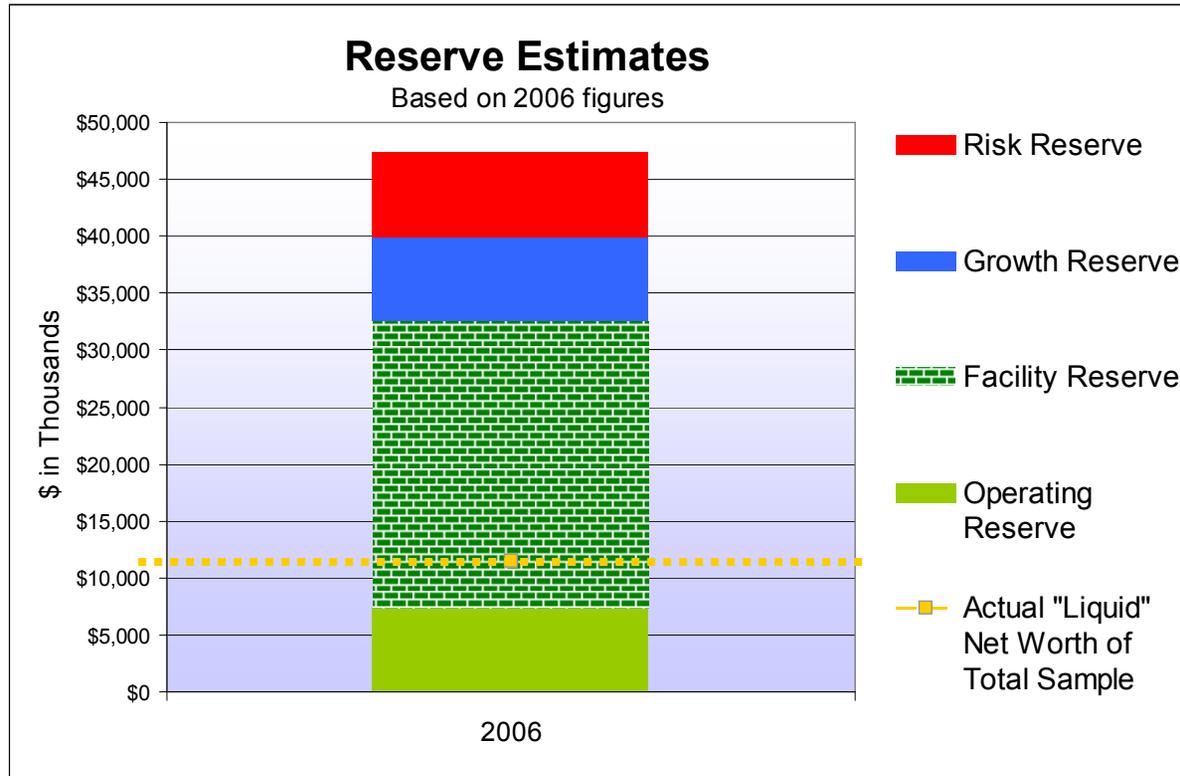
Questions For Consideration

Representing a cross section of Delaware's arts community, this sample reveals ongoing financial challenges: organizations continuing to operate near the margin year after year, barely covering short-term financial needs (i.e. covering expenses), and having little flexibility to respond to long-term capital needs. Some key questions for the wider Delaware community to consider:

- What does Delaware want from its arts community? Who is willing to pay to keep arts organizations strong and sustainable in order to reap the benefits they can offer? How do arts groups compete for funds with those who raise money for other important needs, such as education and human services?
- Are thin margins hampering innovation and creativity? Have arts organizations cut back too much on capacity?
- How can potential donors and the organizations themselves be educated to understand the capital needs of the arts sector, allowing them to make important financial decisions regarding facility ownership, reserved income, sustainable growth and expanded reach of their services?
- What additional alternatives need to be explored to support sustainability for the arts? What underlying structural and operational issues need to be addressed in order to build capacity for arts organizations and leverage available funding resources?



What might it take to fully capitalize the organizations in this study?



In the graph above, NFF removed from the "liquid" net worth calculation any investments restricted to debt covenants.

According to 2006 figures, one estimate for full capitalization of the organizations in this analysis would be \$47.3 million (for discussion purposes only). This figure compares to the \$11.5 million in the sample's actual "liquid net worth" at FYE 2006.

CALCULATIONS FOR RESERVE OPTIONS:

Operating Reserve

Equal to 3 months of operating expenses.

Facility Reserve

Equal to value of accumulated depreciation of the total sample.

Growth Reserve

Equal to 3 months of operating expenses.

Risk Reserve

Equal to 3 months of operating expenses.

APPENDICES



Appendix A

Methodology – What was criteria for selecting sample?

- NFF analyzed IRS Form 990 data for fiscal years 2001 – 2006 (public information available and imported from Guidestar) for 33 Delaware nonprofit organizations.
- Selection criteria was based on:
 - Self-reported NTEE Code “A” for “Arts, Culture, & Humanities” and guidance from the Delaware Division of the Arts
 - Availability of IRS Form 990 data for each year between 2001 – 2006
 - Additional notes:
 - The analysis excluded the Henry Francis Du Pont Winterthur Museum. The Museum was eliminated in order to avoid large deviations, given the size of the organization’s revenue and asset base.
 - The Delaware Symphony Association & Supporting Foundation hold separate Form 990s. This analysis relies on combined data for the consolidated entity. Because the Foundation’s Form 990 was unavailable for FY 2004, NFF has relied on comparative data from the 2004 audited financial statement. As a result of the consolidation of the two separate entities, marginal errors for the combined entity remain – primarily as a result of inter-company transactions (e.g. receivables and payables balances).



Appendix B

Understanding the Limitations of Form 990 Data

- IRS Form 990 data was the selected data source for this analysis, due in large part to its role as the *only* publicly available source of financial information for nonprofit organizations.
- NFF has found that IRS Form 990 information is generally reliable, especially for mid-sized to large arts nonprofit organizations. While Form 990 data can provide valuable insight into the financial characteristics of nonprofits, special consideration should be given to the limitations of this data:
 - Form 990 data is self-reported in nature, and therefore data quality heavily relies on the precision of the form’s preparer.
 - **For organizations that receive restricted funds or generate “non-operating” revenue (e.g. contributions for a major capital project), Form 990 revenue and surplus figures are often overstated:**
 - Form 990s do not present the restricted nature of revenue for nonprofit organizations. For example, Form 990s report “total” revenue figures and do not distinguish unrestricted vs. restricted revenue.
 - Revenue totals also do not distinguish “operating” vs. “non-operating” income (i.e. revenue figures include funds that are earmarked for capital expenditures, such as a major facility project).
 - Additional revenue details do not tend to distinguish between government contracts and government grants; in-kind (non-cash) contributions; and pass-through (re-grant) dollars.
 - Lastly, Form 990 data often do not capture affiliate organizations that hold a separate 501(c)(3) status.



Appendix C

Breakdown by Total Expense Size

LARGE ORGANIZATIONS

\$2.5 Million +

Delaware Art Museum
Delaware Symphony Association & Foundation
Grand Opera House

\$1 million - \$2.5 Million

Christina Cultural Arts Center Inc
Delaware Center For Contemporary Arts
Delaware Theatre Company
Opera Delaware
Wilmington Music School

MEDIUM ORGANIZATIONS

\$1 Million - \$250,000

Center For The Creative Arts Inc
Delaware Institute For The Arts In Education
Friends Of The Capitol Theater Inc
Rehoboth Art League Inc
Sewell C. Biggs Trust
Smyrna-Clayton Heritage Association

SMALL ORGANIZATIONS

Up to \$250,000

Brandywine Baroque Inc
Brandywiners Ltd
City Theater Company
Coastal Concerts Inc
Delaware Chamber Music Festival Incorporated
Delaware Childrens Theatre
Delaware Music School Inc
Delaware Performing Arts Center Inc
Dickinson Theatre Organ Soc Inc
Dover Art League
El Centro Cultural Inc
Henlopen Theater Project Inc
Mid-Atlantic Ballet Academy
Newark Symphony Orchestra Inc
Rehoboth Beach Film Society
Rehoboth Summer Childrens Theatre
Society For Preservation & Encouragement Of
Barbershop Quartet Singing Americans
VSA Arts Of Delaware Inc
Wilmington Drama League Inc

Notes: (1) The above expense figures are based on FY 2006 data; (2) Breakdown of "large," "medium," and "small" organizations is based on The Alliance For the Arts.



**For more information about NFF, visit our
website:**

nonprofitfinancefund.org

