Identifying and Understanding the Primary Causes of Financial Stress, and Measuring its Impact on Non-profit Performing Arts Organizations

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III. INTRODUCTION

Shortly after moving to New York City I was fortunate enough to land the position of Managing Associate/Company Manager at a historic and storied non-profit Off-Broadway theatre. It was essentially my job to take care of the day-to-day minutia in support of the Artistic and Managing Directors. During my time there, the theater had its share of notable successes including winning an Obie Award, producing one of the most critically acclaimed and financially successful revivals in its history, and expanding its reach to include a third venue. However, underlying all of these achievements was a prevailing sense that the theatre was just getting by. Rather than being able to operate in a state of financial stability, the staff was always instructed to spend as little as possible, cash flows and financial statements were never fully disclosed, and we were constantly left wondering how and what expenses were actually being covered. The company operated in this state for years until one day it simply could not go no further.

It was the day of our fourth quarter board meeting in 2009. During the meeting the staff waited in the theater's lobby while the artistic and managing directors met with the board. Then, halfway through the meeting our development director and board liaison came out and told us they were told to leave before the managing director gave his quarterly presentation. About 20 minutes later, our managing director came down to tell us he had resigned. He was gone the next day. Over the next two weeks, three quarters of our board would leave the company, our staff would shrink by over 50%, and we would discover that our company was in a critical amount of debt and our endowment had been completely cannibalized. Left essentially rudderless, I was thrust into the position of general manager, in which I discovered the full gravity of the situation, and was tasked with reducing our other overhead and finding consistent sources of income. The toughest thing I had to do was inform many of my colleagues and longtime friends that the company could no longer afford to employ them. Throughout the process of picking up the pieces, I could not help but wonder how we could have allowed the situation to become so dire. How could I have helped prevent it? Were we actually confronting the causes of our company's financial stress or were we simply finding quick-fix solutions to get us to the next day? What were the true causes of this financial stress, and was it fair to blame any one particular party for making it worse? This personal experience is the primary motivation behind this thesis. Ultimately, I hope the information found in these pages will help artistic directors, managing directors, board members and staff members of non-profit performing arts organizations recognize the various levels of severity of financial stress and how to change course before the compounding stress builds up to a full-blown fiscal crisis. I will accomplish this goal by examining the specific point at which financial stress moves from being problematic to life threatening for an organization. I will also provide supporting historical evidence from specific case studies and a set of tools with which to measure one's own financial stress that can be used by leaders of non-profit performing arts organizations as they navigate the financial ebb and flow of their own organizations.

IV. THESIS STATEMENT

Financial stress is a reality for any non-profit performing arts organization. Common symptoms of financial stress can include, but are not limited to, diminished amounts of working capital, difficulty in serving one's mission, the inability to take artistic risks, and company member burnout. The most common causes of financial stress for non-profit performing arts organizations are operating with low or negative working capital, poor management, the absence of proper governance and fiduciary oversight, limited revenue sources, and external X-factors beyond one's own control. Additionally, mission driven non-profit organizations are inherently more susceptible to the financial strains listed above than private commercial enterprises. Each of these causes contains numerous sub-causes, but if combined, unrecognized, or unaddressed, the compounded financial stress can eventually build up to a quantifiable breaking point. An organization that reaches this breaking point cannot properly serve its mission, may never regain its financial footing, and must face the reality of its own demise. This paper will provide an in-depth exploration of each of these primary causes of financial stress, and it will identify a quantitative breaking point as part of a financial stress range. This spectrum can then be utilized by non-profit performing arts organizations to measure their own financial stress, thus helping them avoid a financial watershed moment.

Starting with a definition of key terminology, this thesis will be organized into the following five sections:

1. How the basic mission-driven non-profit performing arts organization's business model is inherently more susceptible to financial stress than private commercial institutions.
2. How Financial Stress is defined as it pertains to non-profit performing arts organizations.

3. Tracking recent financial trends in non-profit American theater.

4. Laying out the Financial Stress Spectrum and identifying the breaking point.

5. Identifying the common causes of financial stress;

    a. Operating with low or negative working capital

    b. Poor organizational management

    c. Limited revenue sources

    d. External X-factors

V. DEFINITION OF KEY TERMINOLOGY

The following list includes important definitions of key terminology that will be regularly utilized and referenced throughout the course of this thesis.

- **Working Capital** [1]– The amount of liquidity (unencumbered cash and near cash) an organization has on hand or that is immediately accessible. Working capital can cover predictable periods when cash outflows exceed cash inflows due to seasonal or cyclical volatility. It can also be used to help cover basic operational costs associated with running an organization. Working capital equals current assets less current liabilities.
- **Financial Stress** – The level of difficulty an organization may have in meeting basic financial and operational commitments due to a shortage of capital.
- **Operating Deficit** – When a company's operating expenses exceed its revenue over a given period of time, usually a quarter or a year. An operating deficit essentially means a company is losing money, which is a practice that, if unchecked, cannot be sustained over the long term.
- **Operating Surplus** – The opposite of operating deficit. The state in which an organization's revenue exceeds its operating expenses over a given period of time. Again, this is usually a quarter or a year.
- **Cash Reserves** [2]– A cash reserve is money an organization sets aside to cover anticipated future costs such as capital projects, emergency/unexpected expenses, special programming, and general operating costs. For example, a company may plan to have a

[1] Nonprofit Finance Fund. *Glossary of Financial Terms: Working Capital*. New York: Nonprofit Finance Fund, 2001. Web.
[2] Matan, Roy. "Making a Case for Reserve Funds in the Nonprofit Sector." *Sobel & Co., LLC*, 2007. Web.

90-day cash reserve. This may also be known as emergency funds. These funds are often held in bank accounts, money market accounts, or in short-term stable investments that are not likely to lose value, and the organization should be able to withdraw funds easily or sell the investments without losing money.

- **Operating Budget** – An operating budget is a detailed projection of all estimated income and expenses based on forecasted earned and contributed revenue during a given period of time.
- **Earned Income –** Revenue or income received by an organization in exchange for its products or services, e.g. ticket sales, tuition, concession or merchandise, space rental (performance, rehearsal, or administrative), and/or contracted services.
- **Contributed Income** – Contributed income is donated revenue from individuals, foundations, corporations, or government agencies to non-profit organizations for which the donors do not receive any products or services from said non-profit organizations. Those making donations to non-profit organizations can claim their donations as tax-deductible when they file their taxes.
- **Endowment** [3]- Also called investment reserves. Endowments typically represent donated capital that is kept intact (and grown) to generate investment income. While the principal of an endowment is typically permanently restricted, unrestricted investment reserves can serve the same function, while providing leadership with a bit more flexibility with regards to its restrictions. The Non-profit Finance Fund encourages non-profits to prioritize raising flexible forms of capital since endowments need to be large in order to generate adequate annual income and may compete with other fundraising efforts.

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[3] Nonprofit Finance Fund. *Glossary of Financial Terms: Endowment*. New York: Nonprofit Finance Fund, 2001. Web.

- **Change in Unrestricted Net Assets** [4]**(CUNA)** – CUNA is the balance that remains after subtracting total unrestricted expenses from total unrestricted income. CUNA includes operating capital campaigns, depreciation, and realized and unrealized gains and losses.
- **Compound Growth Rate (CAGR)** [5]- A calculation that estimates average annual percentage growth over a specified period of time. For example, an organization that had $100K in revenue in 2000 and $500K in revenue in 2004 has a CAGR of 49.53%.
- **Balance Sheet** – This is a statement showing an organization's financial position (assets, liabilities, net assets) at the close of business on a particular date, and is usually calculated annually or quarterly.

[4] Barr, Kate. *Analyzing Financial Information Using Ratios*. Minneapolis: Nonprofit Assistance Fund, 2008. Web.

[5] Nonprofit Finance Fund. *Glossary of Financial Terms: Compound Growth Rate*. New York: Nonprofit Finance Fund, 2001. Web.

VI. THE NON-PROFIT PERFORMING ARTS BUSINESS MODEL

In order to fully comprehend the causes, impact and varying degrees of financial stress in the non-profit sector, we must first review the basic business model of mission-driven non-profit performing arts organizations. While many may point to over-simplified causes of financial stress, such as poor ticket sales, dwindling foundational support, and poor operating practices, among other examples, I believe the business model itself may inadvertently make non-profit performing arts organizations more susceptible to financial stress than private commercial business models in other industries, particularly in the areas of amassing Working Capital (or lack thereof), basing financial opinions on mere snapshots of an organization's existence, limited revenue streams and funding priorities, regional limitations, competing artistic and managerial agendas, and the inherent financial implications and sustainability of a guiding mission statement.

We must first begin with the basic structure of non-profit organizations, which we will examine from the following standpoints.

1. Legal Entity and Tax Classification
2. Revenue Options
3. Financial Reporting
4. Organizational Structure
5. Mission and Programming

LEGAL ENTITY and TAX CLASSIFICATION. Non-profit organizations are considered public charities by the Internal Revenue Service and, as such, are provided tax-exempt 501(c)(3) status. A corporate figurehead does not own a non-profit organization, nor does a non-profit organization have investors or shareholders. One of the primary benefits of this tax classification is that non-profits are not required to pay certain taxes that private enterprises and individuals must pay. These include exemption from federal income taxes, property taxes, and, depending on the state where the non-profit is based, sales taxes. They are, however, required to pay payroll taxes for their employees, Unrelated Business Income Taxes (UBIT), and, in some cases, miscellaneous local taxes.

REVENUE OPTIONS: Tax-exempt public charities can accept contributed income in addition to generating earned income. Any profits at the end of a given period of time are reinvested into the organization rather than distributed to any shareholders or private investors. Individuals who donate to non-profits are able to claim that donation as a deduction on their annual tax return, which can help provide incentive for giving money without the expectation of receiving any tangible goods or services in return. Earned income can come from the sale of goods, services, tuitions, royalties, and/or ticketed admissions. As previously discussed 501(c)(3) tax-exempt organizations do not have to pay any federal income taxes on their net income (earned or contributed), unlike their counterparts in the private commercial sector.

FINANCIAL REPORTING: A key part of operating any business is financial reporting. This is no different for non-profit organizations, which are required to file annual audits and 990s, both of which lay out the organization's financial activity during the previous fiscal year. Form 990 is an informational return that allows the reviewer to determine if the non-profit organization is primarily spending its money on its mission-driven programming or on general operating overhead. The annual audit provides an outside statement of financial activities from a financial professional, thereby making misstatement or deception by those running the organization more difficult. It is not uncommon for institutional funders to require one or both of these documents as part of a grant application to show that the non-profit organization's financial activity aligns with its mission and statement of programmatic activities. Additionally, Form 990 is always made available for public viewing so that individual donors can have the opportunity to scrutinize an organization's financial activity before they decide to either donate or renew a gift.

Internally, non-profit organizations also set up their own systems of financial reporting, as well as checks and balances to maintain financial solvency on a more immediate basis. Examples of internal financial reporting systems may include, but are not limited to, quarterly reports for the board of directors, monthly reconciliation reports, weekly cash-flow statements, and payroll reports. Responsibly compiling the aforementioned annual and semi-annual financial reports is essential to ensuring a non-profit organization's overall fiscal health and longevity.

ORGANIZATIONAL STRUCTURE: Non-profits can have varying operational structures, but all non-profits have a board of directors, managers (business, general, etc.), and a staff who run the organization's day-to-day operations and executes its programming. While a non-profit organization is allowed to structure its general staff any way it sees fit, all non-profits are required by law to have a governing body made up of board members who are supposed to offer fiduciary oversight for the organization.[6] Within the board of directors there is at least always a President, Treasurer, and Secretary. The board remains apprised of the organization's activities and financial status through communications with the organization's executive leaders (Artistic director, managing director, producing director, etc,) at regularly scheduled meetings. The size of the board of directors and the timing of board meetings varies depending on the needs and scope of each non-profit organization.

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[6] Proscio, Tony and Clara Miller. *How Steppenwolf Excelled, First on the Boards, Then in the Boardroom, and Ultimately on the Balance Sheet*. New York: Nonprofit Finance Fund, 2003. Web.

MISSION and PROGRAMMING: Non-profit organizations are meant to serve a mission in support of a specific community or cause. Some non-profit organizations might be environmentally focused, such as Greenpeace, and some may be medically focused, like the Alzheimer's Association. To summarize its purpose, every non-profit organization has a mission statement. A mission statement is a formal summary of the aims and values of a specific organization. Nearly every decision about whether or not to undertake a specific project or activity should be measured against the organization's mission statement. Furthermore, income derived from contributed income and earned income is reinvested in the organization in order to further support the continued execution of its mission.

To help fulfill its mission, a non-profit organization undertakes programs or programming. Oftentimes, an organization's mission is compatible with a much larger range of programmatic activities than it can reasonably undertake. This means organizations have hypothetical flexibility for creative growth, but in more practical terms it means the organization must make hard choices about the programs it wishes to execute and how to allocate its limited financial resources to those programs. When I spoke with New York Theatre Workshop's former Managing Director, Billy Russo, he put this equation in very simple yet elegant terms. He said, "A well run organization understands that its values and resources will inform its business strategy to serve that mission and the operation that is put in place to execute it." [7]

NON-PROFIT SUCEPTABILITY VS COMMERCIAL ENTITIES: Now that we have a basic understanding of the non-profit business model we must ask ourselves, "What is it about this model that helps an organization's financial health? And what about this model makes

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[7] Russo, W. (2014, August 7) Phone interview.

organizations more susceptible to financial stress?" Starting with the pros of this business model, non-profits can take advantage of the following:

1. Non-profits enjoy 501(c)(3) tax-exempt status, which eliminates the burden of paying some of the federal, state, and local taxes.
2. Non-profits can sometimes generally enjoy lower rates and costs associated with the procurement of goods and/or services than their commercial counterparts. This can be manifested in a beneficial lower rate that is established for non-profits and/or simply by the fact that non-profits do not have to pay regular sales taxes.
3. Non-profits can accept contributed income without the expectation of repayment or a direct return on investment.
4. Non-profits can provide tax deductions for those who make contributions to the organization (individuals and corporations).

The above benefits provide us with only half the picture of what it is like to operate a non-profit organization. We must also examine how the above business model might also negatively impact an organization's financial health and make it more susceptible to certain kinds of financial stress:

1. Financial reporting periods tend to be short-range (annually or quarterly) and rarely take into account the bigger picture that comes with long-term projections and analysis. Many non-profits, especially on the smaller scale, do season--season projections rather than multi-year ones, which are more common for larger non-profits that have significant subscription bases and multiple season slots to fill. Still these projections are rarely more than two or three seasons out at the most.

2. There is the potential for an imbalance or a conflict of power between artistic and administrative leadership.
3. Non-profits not amassing the appropriate amount of working capital as a way to demonstrate “need” to its donors and foundations.
4. Non-profits have a limited number of income sources, and their mission may prevent them from increasing certain areas of earned revenue, such as ticket prices.
5. Performing arts organizations, in many cases, are tied to a specific region or geographic location, which limits their capacity for growth into other markets.

SHORT-RANGE FINANCIAL REPORTING PERIODS: Private companies or larger non-profit organizations with missions that serve other sectors may be more adept in viewing the larger financial picture, while their performing arts focused brethren can tend to operate on a shorter timeframe that is more closely linked to immediate needs and short-term projections, rather than long term planning. Projections also tend to be for shorter windows of time because expenses can vary quite significantly depending on what is being produced in a particular season. Alternatively, social, environmental, and other kinds of non-profit organizations that are not geared towards the performing arts have expenses that are more consistent from one fiscal year to another so long as they do not add new programs or undertake new initiatives. Reviewing or making operational plans on such short financial periods can be detrimental to an organization, as it might not provide an accurate overall picture of that organization’s successes and failures. An organization with an operating deficit at the end of its fiscal year might not actually be in trouble as that deficit might be balanced against years of surpluses, or it might be an intentional deficit that indicates recent expansion. Conversely, it could be rash and irresponsible to assume that an organization with an operating surplus at the end of a single fiscal year is in “good shape." The devil is not only in the details of that bottom line, but also in the organization's overall history. The importance placed on the immediate and the aversion to plan beyond more than a year or two can make it harder for non-profit performing arts organizations to operate with a clear vision for the future.

Of course, poor planning or shortsightedness is not unique to non-profit performing arts organizations. Even commercial companies and private for-profit organizations can suffer from not adequately planning for the future or monitoring the overall historical trajectory of its business. The primary difference is in the scrutiny that private commercial institutions must undergo in order to successfully survive. They must constantly assure those with vested interests in the company that they are a sound investment that will produce results well beyond the return of the initial capitalization required to begin the venture in the first place. To accomplish this they have statements and reports that must be prepared for their shareholders, proposals and plans that are required to receive business loans, and/or earnings reports for their own boards Private companies must constantly demonstrate growth or, at the very least, a steady history and solid projection for the future in order to maintain the confidence of their backers, employees, consumers and, in some cases, even their competition, be that a small business owner who must show that bank that provided them with their initial startup business loan, or CEO's and CFO's of major corporations who must strive to maintain the confidence of their investors and maintain the value of the company's shares. At the end of the day, while non-profit performing arts organizations should make sure their donors and audiences are happy with and interested in their work, they ultimately answer to a mission and not a contingent of shareholders or investors.

SUSTAINABILITY: The discussion of serving a mission versus shareholders or a bottom line is a significant one when comparing non-profit entities to for-profit commercial entities. It is particularly important when you consider whether or not a mission is sustainable and if it inadvertently hinders an organization's growth both artistically as well as financially. When speaking about the non-profit performing arts, the word "sustainability" must be all encompassing and not solely limited to either the financial or artistic output. In his article "Making Sense of Sustainability," Scott Chamberlin cites the Non-Profit Assistance Fund's definition of sustainability as, "the ability to carry out activities that will achieve its mission while also developing and maintaining capacity for mission relevance in the future[8]." It is just as if not more important for the non-profit's mission to be sustainable and not just its finances. Kate Barr from the Nonprofit Assistance Fund explains, "Ask yourself this: what's the worse-case scenario? I'd hate to have to call my board chair and say, 'I just found out that we are out of cash and I don't know if we'll make payroll next month.' That's a nightmare for executive directors but it's a technical problem. The worse-case scenario is this call: 'We just finished a complete review and discovered that our programs don't work. We are making no progress at all to improve or help our community.' That's fatal. The number one component for sustainability is to do great work that will result in progress for your mission, which means you have to define what it is and how you'll know."

Kate and Scott go on to explain that nonprofit sustainability should be viewed in three key layers: [9]

1. **Financial Sustainability**, which is an organization's ability to generate financial resources to meet immediate needs without compromising the organization's future life.

[8] Chamberlin, Scott. *Making Sense of "Sustainability" and its Uses and Misuses in the Arts*. Boston: Nonprofit Quarterly, August 26th, 2015. Web.

[9] Chamberlin, Scott. *Making Sense of "Sustainability" and its Uses and Misuses in the Arts*. Boston: Nonprofit Quarterly, August 26th, 2015. Web.

2. **Organizational Sustainability**, which is the ability to build, adapt, and refresh an organization's capacity to fulfill its mission in relation to an ever-changing environment. This can cover everything from having the right staffing structure, hiring people with the right skills, to maintaining the necessary equipment and facilities.
3. **Programmatic Sustainability**. This, of course, is the ability to develop, mature, and do away with programs in order to meet the changing needs of an organization's constituency over time.

An organization can thrive over the long run when these three layers of sustainability are balanced and in sync, or alternatively it can flounder if there is imbalance. The common organizational characteristic among the three is flexibility – the ability to respond to events and new conditions as they happen in real time.

Ironically, embracing the idea of sustainability as a purely financial characteristic might do more to contribute to an organization's own financial stress. Focusing solely on financial stability as a measure of an organization's success is a for-profit business model mindset. Non-profit leaders and board members should also measure the success of their programming and organizational activity as well. To be sustainable, a non-profit organization must ensure that it has a sustainable mission that serves the passions and needs of its constituents. Ticket buyers, donors, and foundations do not give money to organizations for them to stay in business. They provide funding and buy tickets because they are moved and inspired by the programmatic activity the organization puts forth.

MISSION & VALUE IMPOSED CEILINGS: Another key difference between the non-profit and for-profit business models is that some non-profit performing arts organizations are either unable or are averse to raising prices on items that generate earned income. This primarily includes ticket and admission prices, but it can also relate to tuition costs for classes and workshops or venue rental fees. A major obstacle for raising prices on something like tickets could be directly linked to an organization's mission if one of its key values is to offer artistic programming at a low cost to its constituents. This goes back to the previous point of whether or not a sustainable mission has been established.

For a few seasons I was actually the managing director of a company that ran into this issue, called Exit, Pursued by a Bear. EPBB was an up-and-coming young company in New York City that produced a unique brand of theater in non-traditional venues. Performances were usually epic in size and length, each night the company would prepare a full meal for its audience, and admission was completely free of charge. Audience members were asked to make a cash donation on their way out to help defray the costs of the evening, but after producing eight shows EPBB realized that it had ultimately reached a ceiling in terms of the revenue it could expect to generate from its shows. The only way to generate more "earned" income was to produce shows in spaces that could accommodate a fast growing audience. Unfortunately, the costs associated with larger spaces and preparing food for larger audiences outpaced the amount of income it could reasonably expect to make. Changing the engrained value of free admission would have fundamentally altered part of what made EPBB a special company. The company decided to remain true to its value of free admission, and set out to find an affordable space to produce its ninth show in, but unfortunately has been unable to do so primarily due to cost restrictions. EPBB has subsequently been dormant since its last production in 2013.

For-profit companies can be much more calculating and can have greater flexibility in setting the pricing for whatever goods or services it provides. Their ability to have flexible pricing that responds to the market, demand, and the needs of consumers is something non-profits cannot as easily practice.

REGIONALITY: Another impediment that non-profit performing arts organizations might face is being tied to a local region, and therefore having a limited reach to a specific market. That does not mean that their reach cannot go beyond the cities and states where they are incorporated or based, but that is more of an exception rather than the norm. While dance companies and orchestras might be more adept at having a portion of their season include touring, the same cannot always be said for non-profit theater companies. According to TCG's Theatre Facts from 2013, only 8% of the reported $10.8 million derived from tickets sales, admissions, and subscriptions came from touring productions. Another manner in which companies can reach beyond their regional limitations is through licensing properties that were initially developed or produced by their company. This, of course, assumes the organization has the right to participate in the future subsidiary income of the works they produce, which is never a given. Even if the organization has subsidiary rights or royalty income it still takes a significant amount of future production activity in order to generate an aggregate of income that would have a truly positive impact on the organization's bottom line. Unlike many of its commercial counterparts, non-profit performing arts organizations are far more limited due in large part to their inherent regional anchors.

There are numerous factors that can contribute to an organization's positive or negative financial health, many of which will be explored in the next section, but it is important to note that non-profit performing arts organizations like theaters might already be at a disadvantage thanks to a fundamentally difficult business model that can easily create obstacles outweighing the natural benefits that comes with non-profit status.

VII. DEFINING FINANCIAL STRESS AND THE FINANCIAL STRESS SPECTRUM

Financial stress is a condition in which a company or an individual cannot meet, or is having difficulty meeting, its financial obligations to creditors, vendors, and its own overhead. The inability to meet financial obligations due to the presence of financial stress will have a directly negative impact on both the immediate and long-term primary functions and goals of an organization or individual. The company's cost of borrowing additional capital will usually increase, making it more difficult and expensive to raise much-needed funds for operating and fulfilling its mission in an effective manner. In an effort to satisfy short-term obligations, management might pass on reputable longer-term projects. Employees of an organization under financial duress may experience lower morale and higher stress caused by the increased pressures from upper management to keep costs low while at the same time scrounging for every cent of income. The chance of bankruptcy and the possibility of being laid off will also weigh heavily on the employees who have to shift their thinking from serving a mission to simply trying to survive. Suffice it to say employees in this situation can be much less productive when under such a burden.

To help one understand the varying degrees of severity of Financial Stress, I have created a Financial Stress Spectrum, which in both qualitative and quantitative terms can help individuals measure their organization's own level of Financial Stress. The spectrum lays out appropriate levels of Financial Stress that simply come with the territory of running any business, and then it shows the more extreme levels of Financial Stress including cash-flow shortages, operating with ongoing deficits, and the eventual threat of bankruptcy. Being able to understand and recognize the Financial Stress is essential if one wishes to operate a successful non-profit performing arts organization. The following Financial Stress Spectrum is a tool that, when used correctly, can help address compounded stress before it reaches a breaking point.

As you will see, each level of Financial Stress can be identified by certain specific characteristics. Some of these are more quantitative and some points are more subjective observations that, when combined and considered in full will be able to provide organizations with an accurate sense of their financial well being. At the core of each of these levels are a few basic equations. The equations are as follows:

- WORKING CAPITAL CURRENT RATIO: Working Capital, also known as the Current Ratio, essentially measures an organization's short-term liquidity. In other words, this ratio helps determine how well an organization can meet its current short-term debt obligations. The formula for this ratio is **Total Current Assets divided by Total Current Liabilities**. A ratio of over one is desirable as that demonstrates that the organization should be able to meet its short-term debt obligations.
- DEBT TO EQUITY RATIO: This ratio is meant to measure the long-term liquidity of an organization. While the Current Ratio is an incredibly powerful tool for measuring the immediate health of an organization, it really only provides a snapshot of a specific moment, rather than the full picture. The Debt to Equity Ratio can provide a much fuller picture of an organization's financial status, and it is calculated by **dividing Long-term Debt by Total Net Assets.** In this scenario a low ratio is preferable, as high-debt ratios could be a sign that an organization has long-term liquidity problems.
- CHANGE IN UNRESTRICTED NET ASSETS: This is a simple yet effective formula that can help chronicle an organization's growth or loss of Unrestricted Net

Assets. To find one's CUNA an organization must **subtract its Total Unrestricted Expenses from its Total Unrestricted Income.**

Each non-profit performing arts organization is unique, and as such they must consider many different factors and circumstances when performing self-evaluation to determine their level of fiscal health. To that end, it is difficult to create a one-size-fits-all test that's perfect for each and every organization. However, this Financial Stress Spectrum provides a common foundation from which one can begin to build a comprehensive understanding of a non-profit organization's solvency as it relates to its ability to financially support its mission and operation.

1. **<u>MINIMAL STRESS</u>**
    a. **Organizational Characteristics**
        i. The organization has a sustainable mission and has struck a balance between programmatic, financial, and organizational capacities[10].
        ii. The organization has generated 3+ consecutive years of operating surpluses, has a long-term Debt to Equity Ratio of 15% or less, and has a Working Capital/Current Ratio of 150% or higher.
        iii. The organization has three or more years of positive CUNA growth.
        iv. The organization maintains a healthy cash reserve or emergency funds that are equal to 25% of its operating budget or three months of general operating costs.[11]
        v. The organization's staff can focus a majority of its energy on directly serving the mission, and not stress about making payroll, keeping the

[10] Nonprofit Finance Fund. *Linking Mission and Money*. New York: Nonprofit Finance Fund, 2001.

[11] Voss, Zannie Giraud, Glenn B. Voss, Ilana B. Rose, and Laurie Baskin. *Theatre Facts 2012: A Report on the Fiscal State of the Professional Not-for-Profit American Theatre*. Page 34.New York: Theater Communications Group, 2012. Web.

lights on, or burning out due to lack of organizational and financial support.

vi. The organization has been able to identify and take advantage of numerous revenue streams that are appropriate for the size and scope of the company, while also maintaining an appropriate level of overhead. This speaks to the organizations strength of financial and organizational stability.

2. APPROPRIATE AMOUNT OF STRESS

a. Organizational Characteristics

i. The organization has operated with balanced budgets for at least two years. Any operating surplus or deficit equals less than 1% of the annual operating budget, and can be covered by the organization's net assets, which shall not be less than 10% of the organization's total asset base.[12] The organization has a long-term Debt to Income ratio of 15-25%, and a Working Capital/Current Ratio of 50-100%.

ii. The organization has at least two years of positive CUNA growth.

iii. The organization has an emergency reserve fund that is either 15% of the total budget and/or can cover at least two months of general operating costs.

iv. The organization can take some risks, but are fewer and more calculated. A risk that does not pan out might require the organization to make up for that loss in other areas of operation or programming.

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[12] Miller, Clara. "Hidden in Plain Sight: Understanding Nonprofit Capital Structure." *The Nonprofit Quarterly* 10.1 (Spring 2003). Web.

3. OPERATING UNDER THE UMBRELLA OF STRESS

a. Organizational Characteristics

i. The organization has two or more years of accumulated operating deficits, and net assets of less than 10% of the total asset base.

ii. It has as a long-term Debt to Equity ratio of 75 - 100%, and a Working Capital/Current ratio of 0-50%.

iii. The organization has two years of negative CUNA.

iv. There is one month or less of operating expenses worth of emergency reserve funds.

v. It pulls from temporarily or permanently restricted funds to cover cash flow shortages or other costs that are not associated with said funds. They may also have to take out bridge loans to cover gaps in funding on a more regular basis than companies in the previous two categories. This organization may also be more reliant on up-front capital such as earned income that is derived from subscriptions or memberships.

vi. Leadership puts a greater emphasis on earned income (ticket sales, subscriptions, space rental, contracted work).

vii. The organization has a limited number of outlets for contributed income. It might be heavily reliant on a few major donors and not have a wide base of smaller or mid level donors

viii. The contributed funds it raises are split evenly between programming and general operating costs.

ix. The artistic leadership and departments cannot take risks, and must make "safe" choices with its programming (programmatic instability)

x. The organization has to regularly make sacrifices in order to produce its seasonal programming such as smaller or fewer productions, hiring freezes, or staff layoffs.

4. <u>THE BREAKING POINT</u>

a. Organizational Characteristics

i. An organization that has reached this point has amassed over three years of accumulated operating deficits, and has net assets that are equal to less than 5% of total basic assets.

ii. It has a long-term Debt to Equity Ratio of over 100%, and a negative Working Capital/Current Ratio.

iii. The organization has experience three or more years of negative CUNA.

iv. It relies on a maxed out line of credit or loans to pay basic expenses.

v. Its leaders borrow against restricted assets such as an endowment or takes out a mortgage to cover costs.

vi. The organization cannot plan for the future because it is living season to season.

vii. There are no reserve funds available to the organization should there be an emergency.

viii. The organization cannot take any artistic risks.

ix. It is terribly susceptible to economic fluctuations or to factors beyond their control.

x. Its leadership and board have to undertake a SOS fundraising campaign.

xi. The organization's mission takes a back seat to the bottom line.

xii. The chances of the organization pulling off a significant recovery are very slim.

5. <u>THE END</u>

a. Organizational Characteristics

i. The organization is unable to overcome years of accumulated debt.

ii. It has to eliminate all programming.

iii. Its staff and board can no longer raise contributed funds.

iv. The organization's liabilities disproportionately outweigh assets.

v. The governing board votes to dissolve the company and sell its remaining assets to pay off its debt.

The impact of Financial Stress on an organization is as varied as the factors that make up the levels of severity. Healthy organizations, which occupy the first two spots of the Financial Stress Spectrum, have struck a balance between their programmatic aspirations, organizational structure, and financial capabilities. The staffs, leaders, and boards of these organizations can plan for the future in a way that does not compromise the present. Additionally, employee morale has a better chance of being higher at well-run organizations that are not dealing with major Financial Stress. The dark cloud of potential financial ruin, layoffs, or closure can take its toll on workers who are otherwise just looking to do their jobs. Of course, workers can be stressed or unhappy even at successful organizations, but I believe they do not have to deal with the additional stress that comes with working in an unstable organization that is slowly reaching the Financial Stress breaking point.

VIII. FINANCIAL TRENDS AND CHARACTERISTICS IN THE NON-PROFIT AMERICAN THEATRE

In order to fully grasp the varied levels of Financial Stress it is important to review the current financial trends in the non-profit American theatre. This will give us a snapshot of what different sized organizations are grappling with in the current market, and how Financial Stress impacts these organizations in different ways. In the Theater Communications Group's 2012 Theater Facts report, wherein information was compiled from over 178 profiled theaters through a detailed survey, TCG was able to determine some fascinating trends about the business operation of large theatres (budgets of $5 million or more), mid-sized theatres (budgets from $1 million to $4,999,999), and smaller theatres (budgets below $1 million).[13] This report provides a context that demonstrates certain financial trends within the landscape of non-profit theaters, and the Financial Stresses they are up against. The year 2012 is important because it is largely perceived to be the point at which most nonprofit organizations had been able to reach, or come close to reaching, their pre-recession form.

LARGE THEATRES generally supported a higher percentage of their expenses through ticket and subscription sales, and a smaller portion of their expenses were covered by other forms of earned income (education tuition, royalties, special events). They offer a greater range of ticket packages, and rely heavily on income from the sale of subscriptions as it can provide a significant amount of initial operating income for the season. Subsequently, they fill a higher percentage of seats with subscribers rather than single ticket buyers. Earnings from endowments at larger theatres supported a greater percentage of operational and programmatic activities than

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[13] Voss, Zannie Giraud, Glenn B. Voss, Ilana B. Rose, and Laurie Baskin. *Theatre Facts 2012: A Report on the Fiscal State of the Professional Not-for-Profit American Theatre*. Page 18.New York: Theater Communications Group, 2012. Page 4, Web.

they did for mid-size theaters. Larger theatres also obtained a lesser percentage of their budgets than their smaller counterparts from foundations and fundraising events. More of their budget is spent on production payroll and they have higher realized levels of depreciation since they have far more fixed assets (property and equipment) than theatres of smaller sizes. Theatres in this category spent more on physical production, less on occupancy expenses, and in 2012 they tended to have a negative CUNA compared to the previous two TCG reports.

MIDSIZE THEATRES are much more reliant on contributed income with an emphasis on foundation and local government support. Proportionally, they received fewer in-kind and trustee contributions. While many mid-sized companies offer subscriptions, their ticket package options were not as varied as their larger counterparts, but they did report the highest subscriber renewal rates of the three categories. A higher percentage of their revenue derived from trustees, foundations, and government agencies, they earned less from co-productions and enhancement funds, and they spent less on production expenses. Mid-sized companies displayed the highest percentage of positive CUNA, but they tended to operate with a serious shortage of working capital.

SMALL THEATRES primarily rely on contributed income versus earned income. Those that offered subscriptions filled fewer seats with subscribers and retained fewer of those subscribers than the large and mid-sized theatres. Most of their resources went to artistic payroll, occupancy expenses, and general management costs such as office supplies and accounting fees. Less was spent on production payroll and royalties. Companies in this category place greater value on adding professional staff, and increasing the share of the budget allocated to administrative payroll. This comes from a clear desire to bolster operational infrastructure, which in turn will support the artistic endeavors of the theatre.

Some differences are obvious and expected. For example, board size increases with the size of the theater: small size theaters have an average of 10 board members whereas large size theaters averaged upwards of 40. Other notable, yet less obvious, differences among the three groups include earned income as a percentage of expenses. Small theaters covered an average of 41% of their expenses by earned income versus upwards of 50-55% for large and midsize theaters. In a snapshot of a year, large theaters had an average CUNA of -$315,000, midsize theaters had an average of +$159,273, and small theatres had an average CUNA of $1,036.50.[14] The numerous variances between these three classifications of non-profit theaters are significant as they demonstrate the unique priorities and challenges each size theater faces. While there is certainly some fundamental commonality among the three categories, the range and scope of issues faced by a small theater are vastly different than what a large non-profit theater faces.

A larger picture of 2012 shows us that income and expenses of non-profit theatres in America have mostly returned to pre-recession levels after a previously rough five-year period. The average theatre ended the year in the black in 2010 and 2011 after 2 years of prominent losses. Unfortunately, average CUNA fell slightly into the red in 2012. Single ticket income saw increases for a third year and subscription income for its second. Contributed income was relatively healthy as the country moved further from the heart of the recession years and individual contributions particularly increased. Expense growth closely mirrored inflation. However, the trend of negative working capital is a critical cause for concern and ultimately a threat to the future capability of many theatres in the field as a primary cause of Financial Stress.

[14] Voss, Zannie Giraud, Glenn B. Voss, Ilana B. Rose, and Laurie Baskin. *Theatre Facts 2012: A Report on the Fiscal State of the Professional Not-for-Profit American Theatre*. Page 18.New York: Theater Communications Group, 2012. Page 4, Web.

IX. THE PRIMARY CAUSES OF FINANCIAL STRESS

Financial Stress is the level of difficulty an organization may have in meeting basic financial and operational commitments due to a shortage of capital. Common causes include:

1. Operating with minimal or negative working capital
2. Poor Management and Governance
3. Limited Sources of Revenue
4. Outside X-factors

To acquire the best understanding of the enormity of these primary causes I will break each one down into a number of commonly experienced sub-causes. An organization that has a comprehensive understanding of these Primary Causes is an organization that will have an exponentially better chance of survival than of its counterparts.

Operating with Limited or Negative Working Capital

The first primary cause of Financial Stress can, in some cases, also be a result of Financial Stress, and that is working with limited or negative Working Capital. Not having enough money in one's working capital coffers can cause a great amount of Financial Stress as it makes the organization much more susceptible to sudden changes or shortfalls. Alternatively, an organization that does not adequately plan or budget for an upcoming fiscal year can find itself overusing the working capital it does have as a stopgap against their poor practices. Also, an organization can get in trouble if it is overusing working capital to cover repeated annual budget shortfalls and deficits. This goes more into the issue of poor management, which will be covered later in the paper, but it's important to understand how the lack of working capital can be both a primary cause as well as a result of significant Financial Stress.

An organization with an appropriate amount of working capital that is proportionate to its financial and programmatic size will be more stable than those with low or negative working capital. Working capital provides an organization with the opportunities to commit to large projects, lay groundwork for organizational growth, take artistic risks, and better meet its overall immediate artistic and financial needs without mortgaging its own future.

TCG found that the average amount of working capital for theatres in all three of the previously discussed categories (large, midsize, and small) was either negative or extremely low. This table charts the average working capital for 103 theatres surveyed by TCG, which clearly shows that working capital was in the negative for the five-year period between 2008 and 2012.

TABLE 12: AVERAGE WORKING CAPITAL (103 Theatres)

	2008	2009	2010	2011	2012	1-yr. %chg.	4-yr. %chg.	4-yr.%chg. CGR*
Total Unrestricted Net Assets	$7,906,013	$6,673,890	$ 6,817,503	$ 7,916,226	$ 7,892,983	0%	0%	-6%
Fixed Assets	$7,372,957	$8,220,972	$ 8,571,274	$ 9,129,511	$ 9,710,133	6%	32%	24%
Unrestricted Investments	$1,055,559	$510,061	$ 812,739	$ 798,696	$ 745,416	-7%	-29%	-33%
Working Capital**	**$(522,503)**	**$(2,057,144)**	**$(2,566,510)**	**$(2,011,980)**	**$(2,562,566)**	***27%***	***390%***	***363%***
Total Expenses	**$7,611,539**	**$7,387,329**	**$7,174,464**	**$7,673,125**	**$8,062,792**	**5%**	**6%**	**0%**
Working Capital Ratio	**-7%**	**-28%**	**-36%**	**-26%**	**-32%**	**-6%**	**-25%**	

* Compounded Growth Rate adjusted for inflation. ***Italicized positive percentages reflect an increasingly negative trend.***
**Trend skewed by 1 or 2 theatres' exceptional activity.

[15]

This gives great cause for concern as it means companies are operating, or rather trying to operate, under a significant amount of Financial Stress, which in turn ultimately means more time and energy is going to simply keeping the company solvent than serving the company's

[15] Voss, Zannie Giraud, Glenn B. Voss, Ilana B. Rose, and Laurie Baskin. *Theatre Facts 2012: A Report on the Fiscal State of the Professional Not-for-Profit American Theatre*. Page 18.New York: Theater Communications Group, 2012. Web.

mission. Thirty percent of theatres had negative working capital in 2008, which decreased significantly by 2012. 22% had negative working capital that improved over time, but still remained negative by 2012. Also more theatres reported negative working capital in 2012 than in any other year during the surveyed period. One large theatre accounted for 19% of negative working capital in 2009, 32% in 2010, and 29% in 2012. Another well-known theatre accounted for roughly 35% of positive working capital every year except 2010. When we eliminate these two theatres from the analysis we then have working capital levels of -$99 million in 2008 and -$187 million in 2012. That's an 82% deterioration of working capital for the remaining theatres after adjusting for inflation.

The working capital ratio, the portion of unrestricted resources available to meet the theatres operating expenses, is indicative of how long a theatre could sustain itself if it had to survive using only its current resources. Theatres with a negative working capital ratio are experiencing cash flow shortages and are therefore more susceptible to unexpected environmental or financial fluctuations. The theatres in this scenario are more than likely utilizing an open line of credit (OLC) or loans to cover the cash flow shortages they are experiencing. In the absolute worst-case scenarios, some companies have dipped into their endowment or restricted funds to cover cash flow shortages. This is an extremely unhealthy practice that is akin to putting a Band-Aid on a wound that needs stitches.

There are many recommendations as to how much working capital or how large of a reserve theatre companies should keep, but nearly all of them are based on a theatre's cyclical cash flow, which is either two or three months of operating expenses or a straight percentage of the theatre's operating budget. Determining the appropriate amount of working capital depends on each theatre's unique qualities and budget size. Of the 103 theatres TCG surveyed on the subject of working capital, only 8 theatres had met the ideal benchmark of either three months of operating funds or 25% of their annual operating budget. [16]

Earlier, we discussed how non-profit organizations must funnel any and all profits back into the organization, unlike a private company, which pays out portions of its profits to its shareholders or holds the money in its coffers as working capital. Like private companies, there is no rule against amassing working or change capital – money that is not necessarily dedicated to any one program, but can be used by the organization to pay for operating expenses, cover deficits, and or be used to facilitate growth. However, when I spoke with Mr. Robert Zukerman, formerly of the New York State Council on the Arts (NYSCA), he said that "in the earlier part of the non-profit arts movement, and particularly in the theater, there was a general aversion to amassing large amounts of working capital because it was thought that foundations wouldn't fund you because you didn't need the money."[17] Ben Cameron of Doris Duke Charitable Trust also affirmed this as a common non-profit business issue.[18] Only relatively recently are companies finally beginning to understand the importance of working capital, but very few have it and even fewer know how to raise it. At the beginning of the non-profit theater movement of the 1960's, companies simply were not trying to accumulate Working Capital the way organizations are now. Part of the reason being they did not want to deter donors or private foundations from giving to their organizations, and partially because the non-profit performing arts organization market was not nearly as saturated as it is today. Jumping ahead from 1996 to 2011, the number of non-profit theaters in the United States doubled while audiences and

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[16] Voss, Zannie Giraud, Glenn B. Voss, Ilana B. Rose, and Laurie Baskin. *Theatre Facts 2012: A Report on the Fiscal State of the Professional Not-for-Profit American Theatre*. Page 18.New York: Theater Communications Group, 2012. Web.

[17] Zuckerman, A. (2015, March 30) Personal interview.

[18] Cameron, Ben. (2015, May 28). Phone interview.

funding generally shrunk during that same time[19]. As an example, according to a NEA study published in 2015, the percentage of adults who attended at least one performance of a non-musical play dropped from 12.3% in 2002 to 8.3% in 2012. Attendance at musicals also dropped during that same 10 year span from 17.1% to 15.2%.[20] Consequently, with less competition and more money available from reliable foundational and government sources, leaders of non-profit performing arts organizations also did not feel the urgent need to amass significant amounts of working capital as they do today.

Organizations that lack Working Capital are far more susceptible to Financial Stress from cash flow shortages arising from unexpected shortcomings such as the loss of a major donor or unexpectedly poor box-office revenue figures, and/or unforeseen external factors that negatively impact the market place. Another drawback of having low amounts of Working Capital is that it prevents organizations from being able to take operational and artistic risks. Their overall flexibility is considerably diminished since they are already hovering very close to their bottom-line, and any deviation from the budget poses a true threat to their ultimate sustainability.

Non-profit performing arts organizations thrive on creativity. An organization's ability to provide artists and artistic staffs with the necessary support and resources to fulfill their creative ambitions in service of the mission is crucial, and having a deep well of Working Capital can be a true asset in these endeavors. Some organizations are now trying to address this issue by creating Artistic Risk Capital or Change Capital in order to regain some of that flexibility that they have lost. Of course, the size of the organization can also contribute to the loss of flexibility.

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[19] Novick, Rebecca. "Please, Don't Start a Theater Company! Next-Generation Arts Institutions and Alternative Career Paths." Grantmakers in Arts. 2011. Web.

[20] National Endowment for the Arts. *A Decade of Arts Engagement: Findings from the Survey of Public Participation in the Arts, 2002-2012*. Washington, DC: Arts.gov, 2015. Web.

While one might think a large organization with plenty of resources might be the most flexible, the alternative could be just as true. For example, smaller nomadic organizations with low overhead may actually enjoy certain opportunities that large organizations with permanent homes and large staffs might not. Putting together fundraising campaigns for "Artistic Risk Capital" is also a much easier sell than fundraising for "Working Capital," at least to the general public. This, however, does not fully solve the problem that many organizations are facing. While recognizing the issue at hand is a major step in the right direction, and certainly a fundraising campaign can help in the endeavor of righting the ship; it will really take a shift in the financial culture of the troubled non-profit performing arts organization to fully address this primary cause of Financial Stress.

A side effect of having limited or negative Working Capital that non-profit performing arts organizations face is severe susceptibility to cash flow shortages. Leadership in organizations facing cash-flow problems are then forced to make tough decisions about what can be paid and when. Trying to make payroll becomes a weekly struggle, laying down large amounts of capital for venue rentals or equity bonds becomes exceedingly difficult, meeting administrative obligations while in production becomes a stressful financial balancing act. Regular bills and payments to vendors are delayed to help cover other costs. These liabilities pile up, become past due incurring penalties, and in a relatively short amount of time a non-profit performing arts organization can find itself underwater as the compounded Financial Stress piles up. In this scenario many organizations turn to lenders, open lines of credit, and apply for bridge loans to fill gaps in cash flow. While this may solve one immediate problem, it opens the door for a new set of issues that comes with paying back creditors. There are some arts service organizations that offer low or no-interest bridge loans to non-profit performing arts organizations, such as the Alliance of Resident Theatres, New York, which provides $40,000 bridge loans to organizations that might be waiting for large payments to come in from foundations, or the return of a deposit from a venue, or a security bond from Actors' Equity Association. However, it is more likely that an organization may have to turn to its bank for a loan or to open up a large line of credit, which it can utilize to fulfill immediate financial obligations as well as expenses that are further down the road. Of course, there is a significant difference between the timing of a grant that an organization has been awarded and waiting to get a security deposit back versus not properly managing institutional cash flows. The second scenario indicates that something has gone wrong within the organization itself.

In a case where an accomplished theater company had to be resourceful to cover its annual shortfalls because of its lack of working capital, Theatre de la Jeune Lune manipulated its greatest asset to keep the theater running until it simply couldn't anymore.

A truly valued and revered cultural institution in Minneapolis, Minnesota, Theatre de La Jeune Lune was known the world over as an organization that was regarded for its lush – bold productions and reimaginings of classic plays and operas. Theatre de la Jeune Lune was founded in France in 1978 by theater artists Dominique Serrand, Vincent Gracieux and Barbra Berlovitz,, who were later joined by Robert Rosen, and all of whom were graduates of the École Internationale de Théâtre Jacques Lecoq School in Paris. Actor Steven Epp joined Jeune Lune in 1983. The company's name was inspired by the verses of a poem by Bertolt Brecht which reads, "As the people say, at the moon's change of phases / the new moon holds for one nightlong / the old moon in its arms." Serrand recalls starting the company as being "complete chaos, and that's what was great... We wanted to change theater but we didn't have a clue how to do it."[21]

For the first years of operation, Jeune Lune split its time performing between Paris and in Minneapolis. The company eventually made Minneapolis its permanent home in 1985 and, in 1992, moved into the renovated Allied Van Lines building in Minneapolis' Warehouse District. In 2001, the five original members officially took on duties as co-artistic directors. This collaborative style of direction made it possible for everyone to have an equal say in what goes on stage, as well as keep their creativity flowing. The artists behind the company would eventually become very well known for their theatrical trademark of incorporating what they learned under Jacques Lecoq into the classic works of Moliere, Shakespeare and D'Artagnan. They would also use a rather innovative style of mise en scene in shows, as well as comedic clown-style acting very similar to Charlie Chaplin, Marcel Marceau and Commedia dell'arte. Steven Epp explained their approach for producing shows saying, "We dissect the body in its movement, power and playfulness, and glean from that ways to apply that physicality to whatever material we're working with, to galvanize the role and find what's pertinent to a contemporary audience."[22] Jeune Lune was also highly notable for its productions of original works. Its most notable example was in 1992, when the company wrote and produced a Brecht stylized play titled *Children of Paradise: Shooting a Dream*. The show is a fictionalized portrayal of the making of the acclaimed French film, "Les Enfants du Paradis." The team used Brecht's trademark of episodic style in plays by doubling the actions from the film's setting in the 1830s and the shooting of the movie in the 1940s. The audience was also encouraged to

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21 Condon, Patrick. "What Caused the Acclaimed Theatre de la Jeune Lune's Demise." *Associated Press* July 13, 2008. Web.

22 Campbell, Karen. "It's a Mean, Mean, Mean, Mean World." *American Theatre*. New York: Theatre Communications Group, October 2004. Web.

participate in the show as they were seated directly on the stage for the prologue, serving as witnesses to the events portrayed in the movie. This was done to represent the mixed ambiguity of the film's meaning that the public felt upon release, leaving it to the spectators to decide its moral message. The production was met with critical praise, going on to win the American Theatre Critics Association's award for best new play.

In 2005, the Theatre de la Jeune Lune was awarded the Regional Theatre Tony Award. The company also received international praise when the French government knighted both Serrand and Gracieux for their contributions to the country's culture. However, despite critical acclaim, the company struggled in its later years to find an audience. According to past 990s, by 2007 the company had been running with significant annual operating deficits for the previous several years. These ultimately built up to an accumulated debt of $1,000,000, which was simply devastating for an organization that traditionally carried a $1.5 million operating budget. The company came close to closing many times before it finally did in 2008, but was able to stay afloat thanks to an occasional successful show and some minor retooling of basic overhead costs. However, it was primarily able to keep the doors open and cover its growing debts by borrowing against the equity in its famous home in the warehouse district of Minneapolis. According to Dominique Serrand, many people assumed that the $3 million building had been a "millstone" around the company's neck, but that that wasn't exactly true. The financial gifts the company received to purchase and renovate the property back in the 1990's made it into a true asset. He elaborated that "What happened after the theater opened was that the building, instead of being a burden, was actually an endowment"[23]. In a 2008 MPR News Article bluntly titled "Theatre de la Jeune Lune Closes," Serrand elaborated, "Since we couldn't build an endowment for the theater,

[23] Combs, Marianne. *Theatre de la Jeune Closes*. Minnesota Public Radio News. June 22, 2008. Online.

we borrowed against its equity. So the theater, the building, has actually helped us live and survive for many years." The theatre ended up borrowing money against its building for five years in increasing amounts prior to June 2008, when the Theatre de la Jeune Lune board of directors announced it would sell the theater building and "shut down the arts group as currently organized." Serrand said in a the same MPR article that the artists "are exploring ways to reinvent an agile, nomadic, entrepreneurial theatre with a new name" that will be "coming soon to a theatre near you." He mentioned his hopes for the closing to be viewed as a way of reflecting on what he sees as systemic problems with how art is funded in the United States. Unfortunately, that new entrepreneurial nomadic theater never manifested itself, and now Jeune Lune simply exists as a reminder to other organizations that even the most lauded and admired companies can succumb to the pressures of Financial Stress.

While there is no one single smoking bullet in the financial demise of Theatre de la Jeune Lune, it is clear that having an appropriate amount of Working Capital could have helped keep the company afloat while also making it a bit easier to restructure its producing model.

Poor Management & Lack of Fiduciary Oversight:

A significant catalyst for Financial Stress and the next primary cause we will discuss is that of poor management and governance. This is obviously a broad category as far as causes of Financial Stress goes, so we will break it down into the following sub-causes:

1. The relationship between the artistic and managerial leadership, and its potential strains.
2. The importance of a well-executed budgeting process.
3. Role of the board of directors.

ARTISTIC AND MANAGEMENT RELATIONSHIP: The importance of clear communication and understanding that needs to occur in order for a non-profit performing arts organization to succeed cannot be understated. These two components cannot exist on their own separate islands. Each affects the other. An imbalance on either side can result in poor allocation of resources, poor budgeting, and any other number of operational difficulties. While a complicated relationship to manage, the artistic and managing director must be able to present a united front to their staff and board, and they must be able to understand and appreciate one another's responsibilities and challenges.

While there are a few different organizational structures in the non-profit performing arts world, the most commonly used model has an artistic director and a managing or executive director as the organization's top leadership positions. Together, as partners, they guide the organization's operations and trajectory. As the titles suggest, the artistic director's primary responsibilities are devoted to the creative and artistic output of the company. They are also usually the public face of the organization. The managing or executive director also serves the art, but from the perspective of a business manager and strategist. Together, these two individuals and their respective departments must work in collaboration as the pilots of the organization because they, while not legally, are largely perceived by the public as the ones who are responsible for the overall successes and failures of the organization.

All companies takes their cues from their leadership, and all leaders of non-profit performing arts organizations must report their successes and shortfalls to boards of directors that are charged with the important task of providing fiduciary oversight as dictated by IRS non-profit tax laws. The relationships between the artistic and the managerial leaders and how it impacts the rest of the organization, as well as the clean flow of communication on all operational, programming, and financial matters, is vital to the overall success of that organization's ability to serve its mission. At the best organizations these facets work together seamlessly with open lines of communication and they institute a culture that inspires staff and artists to put forth their best possible work. In troubled organizations these various aspects operate in conflict with each other, rather than in collaboration towards a greater goal. A well-managed organization will ultimately experience fewer moments of great Financial Stress, and/or will be able to respond to unexpected financial challenges in a more competent fashion than that of an organization where these integral managerial and governing parts do not work together as they should.

Leaders who are at odds with each other, keep information from each other, or simply do not trust in one another's abilities in their respective job will make the difficult task of running a non-profit performing arts organization all the more difficult. Conflict at the leadership level can permeate the rest of the organization's staff, thus having an adverse effect on their abilities to do their jobs effectively. Goals are lost, directives are unclear, self-interests exceed the greater interests of the company, and the balance of power becomes shaky and confusing for all those working underneath the leaders. A poor dynamic between the artistic and managerial leaders was, in part, a contributing factor to the demise of the company for which I worked. The trickiest thing about it from an outside perspective though was that this conflict wasn't always easy to identify, as both parties insisted on hiding their internal struggles with a smile in an effort to show a united front. While an admirable effort, it was ultimately not genuine, which led to a buildup of tension that was released in the most negative of ways. Of the relationship between the artistic and managing directors Barry Grove (Managing Director of MTC.) and Billy Russo (Former Managing Director of New York Theatre Workshop) shared their insights:

"You can disagree with one another, but there has to be enough trust between the two of you that will help you come to the same conclusion." – Billy Russo.

"It's possible to disagree and argue behind closed doors, but at the end of the day you have to display a united front for your board and staff that is honest, inspiring, and calming." – Barry Grove.

Keeping dysfunctional leadership in place will hinder an organization's ability to fully support its mission, and the lack of clarity that comes from inept leadership will exacerbate any Financial Stress an organization may be experiencing. An artistic director who does not take into account the facts and figures presented by the managing director, or a managing director who does not provide accurate financial information to the artistic director, can poison an organization from within without much difficulty. Sometimes these partnerships never develop into what one wanted or expected them to. While it may be difficult to fully recognize and address this issue, it is important for the health of the organization to make change. In some cases highlighting this issue can fall to the board of directors as part of its fiduciary oversight responsibilities. Boards who suspect that the leaders of their organizations either do not get along or are hiding their complications must take steps to address the issue(s), which can be difficult. First and foremost is identifying whether or not there is an issue in the first place. To do this, they should watch for inconsistencies or contradictions between what the leaders say, put-downs or critical statements about one another behind closed doors, and/or a general lack of respect for the other's position or office. Once it is determined that there is a problem then the board must come together with the leaders to try and solve it.

POOR BUDGETING: It goes without saying that an integral part of running any company, not just a non-profit theatre, is being able to create and manage an accurate budget for the organization's activities. A budget is a financial estimate of future income and expenses. It is an important component in the plan of operation in projecting how much will be spent and how much will be earned. The practice of budgeting entails using past financial experiences and patterns and combining this with the understanding of current cost and circumstantial factors. Often falling on the shoulders of the general manager or managing director, the budget lays the financial foundation upon which all of an organization's activities will be based and measured.

Creating and implementing a budget takes a great deal of experience and expertise from the parties putting it together. It's a process that must be approached seriously, and in some cases even a bit conservatively. A poorly constructed budget can be dangerous any non-profit and especially disastrous for non-profit theatres with low amounts of working capital and or little to no reserve.

There are two primary ways in which a budget can go wrong – either the creation or implementation/management thereof. The most common issues that come up in a bad budgeting process are lofty income projections, production costs that go beyond the means of the theatre, forgetting to budget for certain line items, not factoring depreciation, incorrectly formulating payroll and benefits, forgetting to factor in occupancy cost increases (utilities, rent, etc.) and not accounting for debt retirement from previous years of accumulated deficits. Additionally, when creating a budget, one must carefully examine the cost of production relative to what the non-profit can and will charge for admission. If part of the mission of the non-profit is to make art easily accessible for patrons of all income levels, then that will have a direct impact on the organization's budget as it basically will establish a ceiling for earned income generated by ticket sales. As such, the parties that are responsible for creating and approving a budget must have a clear understanding of the ratio between production costs and its box office potential so as not to create an unrealistic projection or an insurmountable budgetary gap.

Once a budget has been built, it is still possible for it to be mismanaged. For one, certain line items could be ignored or not properly accounted for. Similarly, one could not properly update their actual expenditures and income, making it difficult to track their financial progress, which would subsequently make one more susceptible to the Financial Stress, associated with overspending and/or income shortfalls.

Again, the latter was the case for Theatre de la Jeune Lune, which failed to account for its growing deficit in its budget. Further complications arose when the company grew beyond its financial capabilities. The theatre simply could not raise or earn funds it needed to operate in a fiscally responsible manner, and did not do enough with regards to managing its expenses and overhead. This prompted the board of directors to finally close the theatre and sell its building to cover the accumulated debt, final payroll, and what was owed to creditors. "We have reached these decisions with great regret," stated board president Bruce Neary. "However, our fiduciary responsibilities to our artists, our staff, our donors and our creditors dictate this action. We are listing the building for sale in order to fully satisfy our creditors."[24] This is actually a prime example of how compounded stress from multiple sources can be devastating to an organization. Insufficient budgeting was not the sole cause of Jeune Lune's demise, but the Financial Stress from poor budgeting compounded with the company's serious lack of Working Capital was enough to push it over the edge to eventual closure.

The importance of a successful budgeting process cannot be overstated as it pertains to the fiscal welfare of non-profit performing arts organizations. Done well it can help prevent significant Financial Stress, or at the very least provide an organization with a solid foundation from which to better deal with complicated shifts in their financial existence.

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[24] Combs, Marianne. *Theatre de la Jeune Closes*. Minnesota Public Radio News. June 22, 2008. Online.

GOVERNANCE AND FIDUCIARY OVERSIGHT: Equally important to strong leadership and good budgeting for any non-profit performing arts organization is having a competent and engaged board of directors. Founding boards are often smaller and usually comprised of close friends or even family of the founding leaders. Working boards are comprised of experts in certain fields that a growing organization might need guidance in, and larger fundraising boards serve exactly that purpose among others. [25] No matter where a board or organization is in its life or development every board shares the following legal responsibilities:[26]

1. **Duty of Care**. Board members are expected to participate in the organizational planning and decision making of the organization. As such, they must make sound and informed judgments.
2. **Duty of Loyalty**. When acting on behalf of the organization, board members must put the interests of the non-profit ahead of their own personal or professional concerns and avoid potential conflicts of interest.
3. **Duty of obedience**. Board members must ensure that the organization complies with all applicable federal, state, and local laws and it remains committed to its established mission.

I want to highlight the last sentence of the first point, “they must make sound and informed judgments.” A board of directors, no matter how actively involved, does not experience the day-to-day operation of an organization nor see the finance picture as it happens in real time.

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[25] Roche, Nancy & Whitehead, Jaan. *The Art of Governance: Boards in the Performing Arts*. New York: Theatre Communications Group, 2005. Print.

[26] Bathurst, Jessica & Stein, Tobie S. “Performing Arts Management: A Handbook of Professional Practices.” New York: Allworth Press. 2008.

Therefore, the board members' decisions and judgments are based off of the information provided to them in regular reports from the organization's leadership at scheduled meetings. Each organization is different, but board meetings typically happen on a quarterly schedule, or they are required by law to at least meet once a year. If the board is not receiving honest and accurate reports on the state of the organization, or if board is not inquiring about the numbers, then it is far more difficult to make the sound decisions for the betterment of the organization. Additionally, it makes it incredibly hard for them to recognize when the organization might be experiencing Financial Stress.

Conversely, boards and board members who do not fully understand their role in the governance of an organization might not think to ask the tough or right questions when reports or provided to them. Richard Chait describes this as "the allure of philanthropy over governance" in his speech entitles *The Three Gremlins of Governance.*[27]. Scrutiny and constructive strategic thought on the part of the board will help maintain open lines of communication, which in turn will alleviate various financial pressures. It will also establish a solid foundation from which the organization's leadership and board can work together should they need to address challenges facing the organization.

One example of a good system is that of the Children's Theatre of Minneapolis. When I spoke with Tim Jennings, the company's managing director, he told me that they were able to weather a tumultuous time in the organization's life thanks in part to the systems that were put in place to help ensure a clear stream of communication between him, the artistic director, and their board of directors. "Turning around a company can't be the directive of just one individual," said Mr. Jennings. "Everyone has to be involved. The board, the artistic department, and management

[27] Chait, Richard. " The Gremlins of Governance." *Trusteeship Magazine*. July/August 2009. Web.

all have to be on the same page and work together to make it happen." This meant that he and CTC's artistic director Peter Brosius are joined at the hip and in constant communication with their board in order to come back from a $3.8 million shortfall in 2008, followed by a $2.2 million dollar deficit in 2010[28]. In response to this lingering Financial Stress, the organization's leadership, Board Chair Peter Carter, and Finance Chair Lynn Abbott, put together a plan of action that included numerous retreats with the board that were geared towards building trust as well as tackling the accumulated deficit and recent budgetary shortfalls. The retreats and meetings, which got heated at times, helped the artistic and managing directors lay out the major financial issues at hand in full view for the rest of the board to see. From there work began on a turnaround plan that involved major moves like cutting its workforce by 9% (20 people), suspending programming in its second stage, and reducing the budget. Some smaller yet just as important changes include establishing new financial reporting systems. They decided to establish bi-monthly financial reports that tracked the progress of the turnaround along with revised projections for the rest of the fiscal year. This was shared with the finance chair and finance committee, which would then be given the opportunity to ask Mr. Jennings and Mr. Brosius about anything that stood out. The rest of the board received a report every month that compiled financial trends, updated projections, and a narrative summary that described what the numbers were reflecting. Furthermore Mr. Jennings made it clear to the board that his door would always be open should they ever want to reach out and discuss certain matters with him regarding the organizations financial and operational health. These systems and the clean flow of communication helped engender trust and confidence in CTC's leaders, who knew the board of directors had their backs as they traversed this financially stressful time. "We asked a lot of

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[28] Preston, Rohan. "Children's Theatre Charts Financial Recovery." *Star Tribune* 17 Oct. 2013. Web.

questions that helped us to focus," said Abbott, who has been on the board for six years. "But this good news is a testament to the skill of the staff and management team at the theater. They are the ones who executed the vision and they are the ones who made sacrifices."

While their emphasis on good communication and new financial reporting systems did not turn the company around all on its own, it did play a key role in the revitalization of the organization. As of 2013, the company had recorded three years of surpluses of $270K+ while also paying down its debt at a rate of $145K a year. Additionally, in the past year the company followed through on a plan to make a balloon payment that would wipe away the rest of its accumulated debt once and for all. Another benefit of turning CTC around in such an organized and well thought out manner was that it earned the company recognition from major foundations such as the Pohlad Family Foundation, which gifted the company $750,000 in the form of a multi-year grant to help future growth. "They've come a very long way in a short period of time," said Marina Muñoz Lyon, vice president of the Pohlad foundation. "They're pursuing diversified income streams in order to weather future storms. The art is strong, with shows that respect the ability of children to think deeply. And Peter's theatrical savvy is matched by Tim's abilities. That's a truly winning combination."[29]

Limited and Diminishing Sources of Income:

It is a fundamental fact of life that no business, commercial or non-profit, can exist without generating revenue through one or more continuous and reliable sources. As we discussed earlier, income for non-profit organizations income are broken down into two basic categories, Earned Income or Contributed Income. When an organization is too heavily reliant

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[29] Preston, Rohan. "Children's Theatre Charts Financial Recovery." *Star Tribune* 17 Oct. 2013. Web.

on one form of income over the other, then it is potentially putting itself in a situation in which it is susceptible to Financial Stress should one of the streams dry up.

The primary example of an earned income revenue line for a non-profit performing arts organization is ticket sales for admission to the organization's public programming. Similarly, organizations that feature extensive seasons and programmatic series may offer subscription packages or memberships. Money earned from single tickets sales only becomes available after the performance for which the tickets were purchased has passed. This is also true of subscription or membership income as well, and a significant indicator that an organization is experiencing Financial Stress is the spending of the subscription income up front to cover immediate financial needs, which then greatly diminishes the company's ability to deliver the production or productions that money was earmarked for when the time comes.

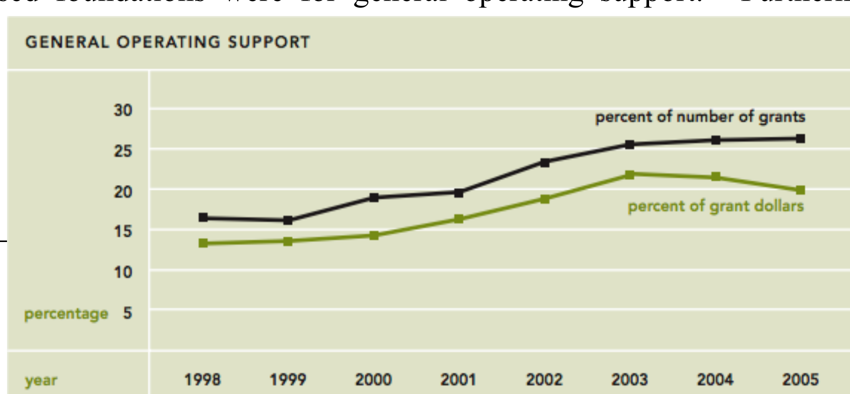
Beyond ticket and subscription sales there are many other kinds of Earned Income that non-profit performing arts organizations can take advantage of. These include guaranteed money from touring productions, tuition for workshops and/or classes, tickets to lectures or special programming, income from licensing, venue and rehearsal space rental, costume rental, shop rental, commissioned performances, concessions, and parking. The actuality of being able to call upon some of the aforementioned earned income revenue outlets depends entirely on the unique mission, scope, and nature of each non-profit performing arts organization. An organization without its own venue obviously cannot rent space or charge for parking the same way a multi venue regional company might. Alternatively, smaller nimble organizations can perhaps find more success with touring or holding workshops, all without having to deal with the overhead of owning and maintaining their own space. It is extremely important for non-profit organizations to take advantage of as many diverse income streams as is reasonably possible. While each non-profit performing arts organization's ratio of Earned to Unearned income differs, diversifying earned income streams is not something that can so easily be overlooked regardless of size, prestige, or artistic mission.

Just as it is with earned income, so is it essential for non-profit performing arts institutions to cultivate as many diverse and reliable contributed income sources as possible. Contributed income options include donations from private corporations, foundations, government agencies, and/or individual donors Funds raised in this manner help non-profit organizations performing arts organizations support various things such as capital campaigns, specific artistic programming, endowment funds, and of course general operating funds.

The organizations with the lowest amount of Financial Stress have, at the very least, a steady and reliable stream of contributed income that is diverse and well administered. An organization that is largely reliant on a handful of major contributors might actually be at more of a financial risk than say an organization that receives smaller donations from a large number of contributors. Should something happen to one of the first organization's major donors they will immediately find themselves in a situation with a major hole in their annual budget that needs to be filled, whereas an organization with a large contingency of smaller to medium donors can find comfort that it would take a mass exodus of donors to create a similar problem. Additionally, the latter organization will find that more donors allows for more agency within the fundraising and audience development markets than say an organization that relies on one or two major benefactors. With the proper cultivation, smaller and medium size donors can, over time, organically be developed into major donors.

Similarly, just as an organization can lose a major donor, so could the well of funds from government agencies and private foundations could run dry. These sudden shifts, loss of awarded funds, or diminished amounts are not uncommon and can have a profoundly negative impact on an organization's Financial Stress. In the earliest days of the non-profit performing arts movement, private foundations such as the Ford, Carnegie, and Rockefeller foundations were the go-to agencies for both new and established arts organizations that were looking to raise capital either for expansion, programming, general operating support, or to simply just get their mission off the ground. Today, these giants are no longer funding the performing arts in the way they once were, and other existing foundations have shifted their funding priorities from general operation support to specific project and artistic programming support.

A key factor in establishing and maintaining artistic and operational flexibility is to have access to funds that are not tied to specific projects or programs, but rather are for general operations. Today there are only a handful of private foundations that provide significant amounts of general operating support to non-profit performing arts organizations. A study by the Foundation Center in 2005 found that only 20% of grants from the 1,200 largest private and community-based foundations were for general operating support.[30] Furthermore, the below



[30] Foundation Center. *Key Facts on U.S. Foundations*. New York: Foundation Center, 2014. Web.

chart demonstrates that, while the number of general operating grants has actually increased over the last fifteen years, the percentage of dollars of these grants has dropped.[31]

As I discussed in the working capital section of this paper, the number of non-profit theaters doubled between 1996 and 2011. With this also comes the increase in demand for general operating support. The result is leaving many organizations with smaller grants that are either project focused or not enough to make a major impact on operational line items in their budgets. Today, the Shubert Foundation is known as one of the primary providers of general operating support for non-profits performing arts organizations. In 2015, The Shubert Foundation awarded $24 million in general operating to 72 dance companies, 368 theatre companies, 11 arts education organizations, and 37 arts service organizations.[32] Other grant giving organizations that provide general operating support include The Howard Gilman Foundation, The Scherman Foundation, and in some instances the Doris Duke Charitable Trust, but it tends to make larger contributions to a smaller group of organizations.

Government agencies also often see a fluctuation in their giving capabilities. Whether federal, state, or municipal, an agency's resources are dependent on a fiscal budget put together by the controlling administration and its representatives. One specific example of diminishing institutional funds comes from the New York State Council on the Arts. Former head of NYSCA's theater division, Robert Zukerman, informed me that the agency's financial resource shrunk by 37% between 1990 and 2015. While the state of New York actually gives out more money to arts organizations than many other states, NYSCA is still only able to spend $2.8 million across more than 300 organizations. In the theater and performing arts, the largest grant

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[31] Woodwell, William H. "General Operating Support." *Grantmakers for Effective Organizations*. 2007. Web.

[32] The Shubert Foundation. *Grants 2015*. New York: The Shubert Foundation, 2015. Web.

NYSCA provided in the last year was $70,000 to Lincoln Center Theater, which accounts for approximately .15% of LCT's $46 million in total revenue for that fiscal year,[33] Most organizations lucky enough to receive state funding rarely receive anything more than a couple of percentage points of their annual revenue. The money may actually go a little further for smaller organizations, but it is still a far cry from being a significant funding source. Arguably, the most significant benefit to receiving government funds from organizations like NYSCA or the NEA is that the grants are sometimes seen as a stamp of approval by the organizations constituents and other potential funders.

While no organization is immune to the negative effects of losing an institutional funder or major donor, the significance of the impact can be far less damaging to organizations that have are not entirely reliant on a small number of contributed income sources. Furthermore, we can see the importance of having an appropriate amount of working capital or a contingency fund, which can be used to cover shortfalls that might be related to a sudden and unexpected shift in contributed income.

A recent case in which an established organization was ultimately too reliant on one particular benefactor for a majority of its income is the Cedar Lake Contemporary Ballet Company in New York. A staple in New York's dance world, Cedar Lake has enjoyed 12 years of performing at its state of the art home on the west side of Manhattan in Chelsea, as well as touring around the world thanks primarily to a single benefactor. In 2015, the New York Times reported that Nancy Laurie, a Wal-Mart heiress and primary backer of Cedar Lake, would not continue to fund the company after the 2014-15 season. With a net worth of over $4.5 billion, as

[33] The Vivian Beaumont Theater, Inc. (d/b/a Lincoln Center Theater). *Financial Statements and Supplementary Information*. New York: The Vivian Beaumont Theater, 2013. Web.

reported by Forbes Magazine, Ms. Laurie and a foundation she ran provided more than 75% of Cedar Lake's annual $5.9 million operating budget as recent as 2013. This is in contrast to only 7.9% of revenue that was generated by ticket income and touring. Facility rentals to outside licensees for special events and performances generated around 15-16%.[34]

There is evidence to suggest that in recent years the company had made some efforts to broaden and diversify its donor base, the most notable clue being a job advertisement for a director of external affairs whose responsibilities were to have included developing "multiplatform sponsorship platform proposals for corporate partners, foundations, government and individuals."[35] Ultimately, the position was never filled and the company continued to remain reliant on Ms. Laurie's ability money until it ceased activity after its final performance in the summer of 2015 at the Brooklyn Academy of Music.

In the same NY Times article, the president of the major philanthropic consulting firm Philanthropology, Katharine DeShaw, said that while there are some nonprofit organizations that are established by single donors willing to endow their budgets in perpetuity, the strongest are created by single donors who then get like-minded supporters to join in the effort. "I guess the big message here is that whoever that founding donor is, unless they're willing to put enormous endowments behind their vision, their organizations won't survive if they don't invite other people in, and I would argue early in the game."

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[34] Cooper, Michael. *Cedar Lake's Ballet Closing Reveals Perils of Relying on a Single Donor*. The New York Times. March 27th, 2015. Web.

[35] Cooper, Michael. *Cedar Lake's Ballet Closing Reveals Perils of Relying on a Single Donor*. The New York Times. March 27th, 2015. Web.

The case of Cedar Lake demonstrates how Financial Stress can come in many forms. Here a seemingly healthy organization with a major benefactor failed to recognize the frailty of their financial situation, which ultimately led to its demise. To cultivate and secure a major benefactor who can commit to contributing large gift on an annual basis is a wonderful thing for any non-profit performing arts organization. However, there is danger in becoming overly reliant on major gifts as it can provide a false sense of financial security, and strip leader's motivation to build a diverse portfolio of donations from many different levels of donors.

Each non-profit performing arts organization must, within its scope of capabilities, identify and pursue the income outlets that are available to them. Furthermore organizations should game plan for the future as more and more revenue streams hypothetically become available to them as they grow and mature. To ignore new possibilities or to be overly reliant on a limited number of income sources can have the adverse effect of building up Financial Stress, which can ultimately lead to disastrous results as in the case of Cedar Lake Contemporary Dance Company.

X-Factors

Merriam Webster Dictionary defines an X-factor as, “a circumstance, quality, person, or environment that has a strong but unpredictable impact on a given subject.”[36] X-factors can be both positive and negative, but for our purposes of this thesis we will focus on the latter as these unexpected events can certainly lead to a significant increase in an organization’s Financial Stress depending on the circumstance. X-factors can be social, political, environmental, and or economical. They can be local, national, or global. X-factors are as diverse as they are unexpected, but they share a commonality in that they will do the greatest amount of harm to organizations that are already on shaky financial ground thanks to other primary causes of Financial Stress. Organizations with strong management, diverse income streams, sufficient working capital, and a responsible board, while not immune from the unforeseen, are for more likely of being able to weather new challenges in a way that will ultimately ensure their survival.

It’s not necessarily hard for one to imagine any number of worst-case-scenarios in which X-factors significantly impact an organization’s operation, but rather than rattle off a list of “could happen” scenarios I will examine some recent instances in which the unforeseen caused varying degrees of Financial Stress for one or more non-profit performing arts organizations. The first X-factor is the great recession of the late 2000’s. The Great Recession was a period of general economic decline that was observed by global markets. The nadir of the United State’s recession is agreed to have fallen between December 2007 and June 2009. As a result of this financial crisis, the U.S. lost 8.4 million jobs, the unemployment rate doubled to nearly 10%, the $8 trillion housing market bubble burst, there was a significant drop in consumer spending, and a severe collapse in business investing.[37] And while the economy stopped contracting in 2009, the recovery period would be long and arduous. For charitable organizations, this would mean three obvious things: 1) A significant drop in philanthropic giving; 2) fewer ticket buyers 3) significant loss in employment and creative opportunities within the community.

According to The Chronicle of Philanthropy charitable giving from individuals with annual incomes of more than $200K fell by $30 billion across the board.[38] Additionally, overall non-profit theatre attendance during the height of the recession fell by upwards of 14% from its healthiest pre-recession point five years earlier. With devastating hits to earned and contributed income sources, it's not hard to see why 45% of arts organizations reported having an operating deficit in 2009, which was up from 32% only two years prior. The non-profit arts community was also not immune to unemployment that had struck the nation. Companies downsized, wages were effectively frozen, and fewer inroads to employment were available to both young professionals trying to join the work force as well as veteran industry members who were laid off as a result of downsizing. Of course, this didn't just hurt administrative staff, but it also led to far fewer opportunities for artists across the board.

Since 2009, the arts community of the United States has been able to rebound with figures trending back to, and in some cases surpassing, their pre-recession levels. That being said, it has been a long and tough road that has left many casualties in its wake. The recession

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[37] "The Great Recession." *The State of Working America*. n.d. Web.

[38] Hall, Holly. "Giving by the Rich Dropped $30-Billion During Recession". *Philanthropy.com.* August 29, 2012. Web.

was a major contributor to the Financial Stress of performing arts organizations and, in many cases, exacerbated previously existing stresses that could be attributed with some of the previously mentioned primary causes. It is a fine example of how an outside force can be just as damaging as poor management, not exploring all possible revenue streams, and operating with low amounts of working capital.

Another recent prime example of an X-factor contributing to Financial Stress of organizations was the attacks of September 11th in 2001. In the wake of September 11th,New York City was left sifting through the ashes and a nation was stunned to find itself the victim of the most devastating attack on its soil since Pearl Harbor in December of 1941. The theater community felt the repercussions of the attacks just as they were throughout the rest of America. Performances were cancelled, shows in the production pipeline were put on hold or rethought altogether, venues remained silent, and the industry mourned along with the rest of the American public as the nation tried to make sense of what had happened. Non-profit arts organizations in New York, like all organizations, felt the impact of the tragedy in a variety of ways. Specifically, The Lower Manhattan Cultural Council, which supports many off and Off-Off Broadway theaters and artists lost its home in 5 World Traded Center and The Theatre Development Fund's downtown TKTS station was also destroyed. Slightly north of the Financial District, many theatres suffered during a period of quarantine in the days following the disaster. Rubble and recovery crews surrounded Tribeca Performing Arts Center and 3-Legged Dog had significant structural damage to its facility. As weeks passed and shows reopened the impact was immediately felt as New York audiences were running 20% below their average levels during that time of year.[39] While many theatres across the country responded to the call to help with the

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[39] S.D, Trav. "9/11: America's Theatres Respond." *American Theatre*. New York: Theatre Communications

recovery effort by hosting special events, disaster relief fundraisers, and opening their doors to emergency workers, the economic outlook was grim. In addition to the loss of earned income from ticket sales, these theatres also had to bear the brunt of a vastly diminished pool of resources that, before then, were normally available for arts organizations. The bleak picture that confronted the not-for-profit performing arts scene in the United States can be drawn from this bulletin from Marge Betley, literary director at Geva Theatre in Rochester, N.Y "We have several board members (also corporate funders) whose companies had offices at the World Trade Center–their world has turned to dust beneath their feet. How can we even conceive of asking them for support at a time when they need ours?" [40]For the performing arts, as for the rest of New York, the road was tough.

A drastic shift in the economic climate, havoc caused by a natural disaster, or the unease of a population in mourning following a national tragedy can suddenly turn all facets of life upside down in any number of ways. Like all other industries the non-profit performing arts are susceptible to the stress caused by unexpected X-factors. Those non-profits struggling in other areas are the most susceptible the negative impact and Financial Stress that results from a sudden environmental shift.

Group. 2001. Web.

X. CONCLUSION

Operating with low amounts of working capital, poor management, the absence of proper governance and fiduciary oversight, diminishing or limited income sources, and external X-factors together make up the fabric of the most common causes of Financial Stress for non-profit performing arts organizations, which are more susceptible to Financial Stress due to their basic business model of operating at a deficit. Artistic directors, managers, and boards can position themselves in a way to minimize their stress by paying close attention to each of these areas within their own operation.

The ebb and flow of the fiscal life of a non-profit performing arts organization can be a volatile one with many fluctuations that are in response to any number of factors over the course of its existence. However, by simply understanding the areas in which most Financial Stress can be found non-profit staffs, leaders, and boards can closely monitor its stress level and make sound and informed decisions on how and when to correct its organizational course before small stresses turn into fully fledged fiscal crisis. A three pronged approach of understanding the fundamental challenges of the non-profit performing arts business model, monitoring the primary causes of Financial Stress, and regularly checking one's organization against the Financial Stress spectrum will help empower organizations to have control over their own fiscal destiny.

Boards should pay close attention to the different levels on the Financial Stress Spectrum, and which of said levels (Minimal Stress, Normal Stress, Umbrella of Stress, Breaking Point, Closure) best describes their own organization's financial health. While each level has multiple points from which to measure and identify the severity of one's Financial Stress, it is critical for organizations to begin the process by calculating their Debt to Equity Ratio, their Working

Capital/Current Ratio, and their CUNA and then compare those results to its current operating and programming expense projections. From here, the boards can then factor in some of the less quantifiable components associated with each level to fully determine where their organization lies on the Financial Stress Spectrum.

While the discussion should always be led by the art and the mission, the conversation can only last so long and accomplish so much if the sound financial and administrative operation is not there to back it up. The balance of art and commerce is not an easy one to find, however it is also not impossible, and well-informed organizations that understand their strengths, weaknesses, and own potential Financial Stress pitfalls will have a greater chance of success and survival than those that operate with impunity.

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