What Do Expenses Look Like Today?

Potential ramifications of a shift in expenses

ArtsFund has been analyzing data from arts and culture nonprofits across the state of Washington. These short pieces rely on data from 349 organizations, spanning 28 counties from 2019-2024, and dive into a series of reflections on specific trends, how the sector may have arrived at this place, and some speculation on what it means for the future.

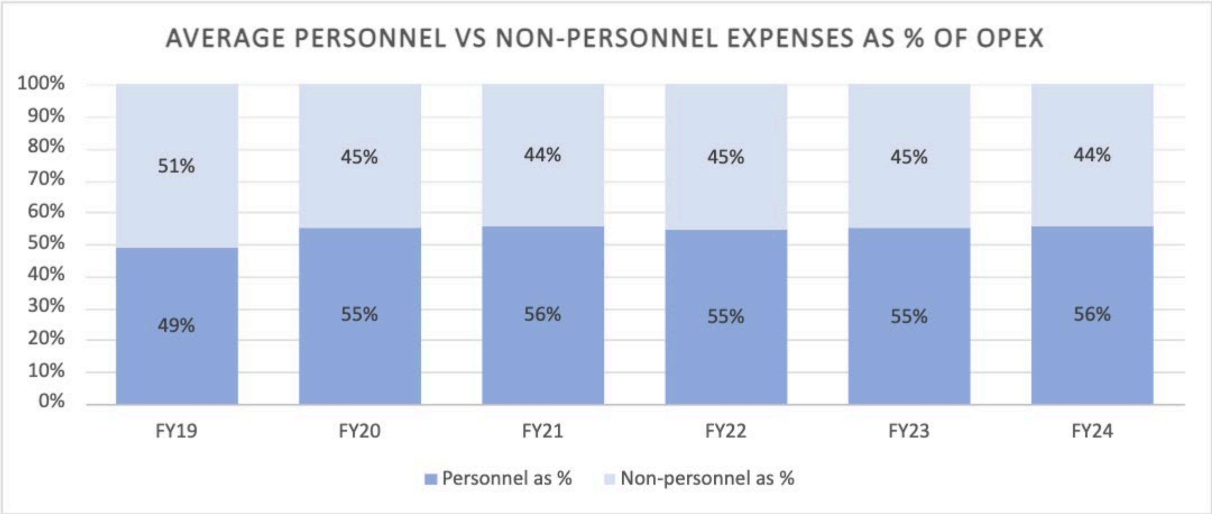

FIGURE 1- PERSONNEL VS NON-PERSONNEL EXPENSES AS % OF OPEX - FY19-24

On average, personnel accounts for 7% more of total operating expenses in 2024 than it did in 2019.[1]

[1] Data come from 349 organizations in 28 Washington state counties that participated in the Nonprofit Community Recovery (NCR) grant, and the Community Accelerator Grant (CAG) rounds one and two. These grant programs were funded by the Washington State Department of Commerce and the Paul G. Allen Family Foundation, respectively, and administered by ArtsFund. All numbers have been rounded to the nearest whole and data sources are provided in the footnotes when available. ArtsFund understands that there is significant variation in demographic data and how people identify. Demographic data are not definite and we understand that interpretation may vary. 2024 data is shown as budget expectations.

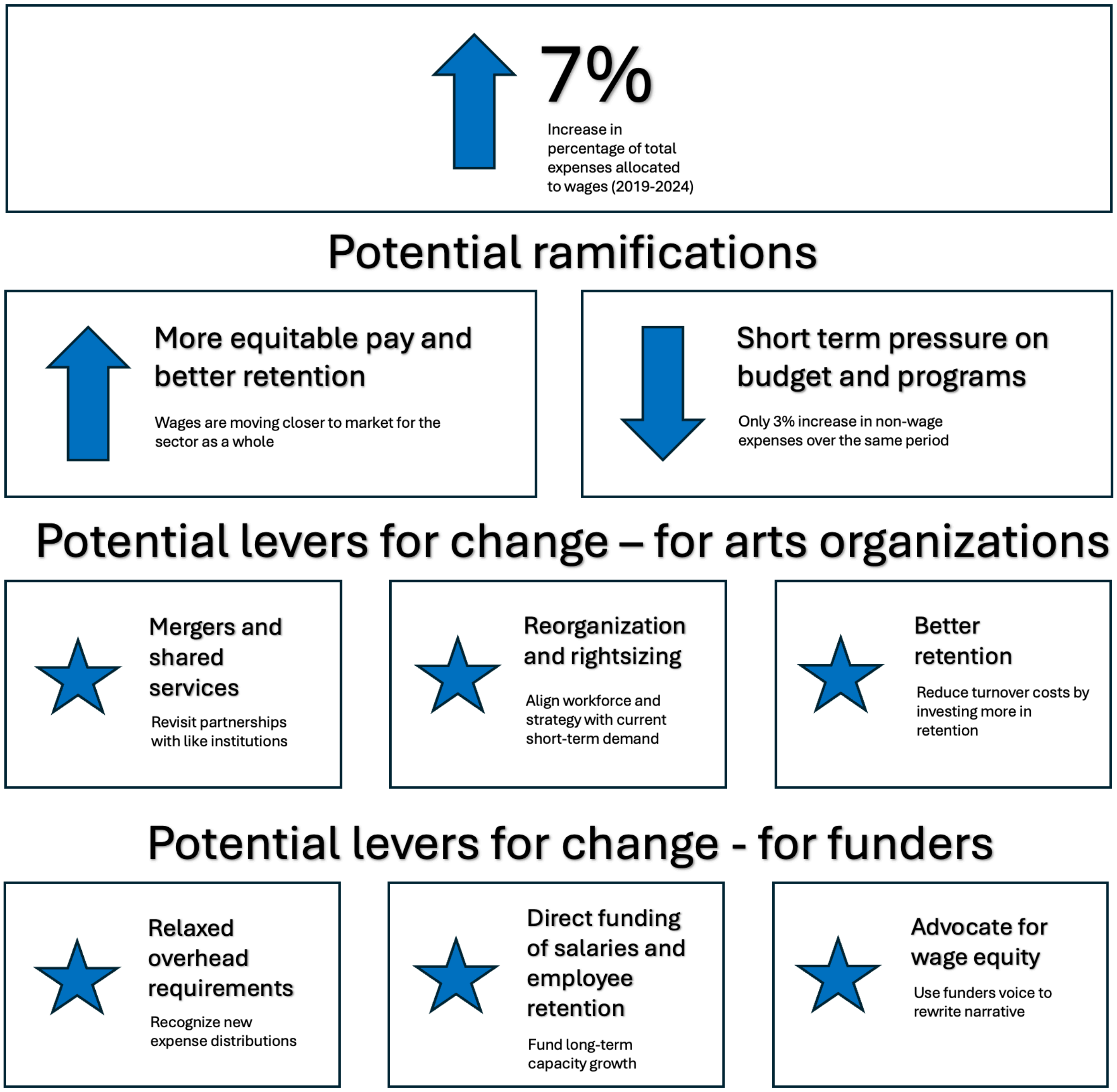

FIGURE 2 - SUMMARY

Organizations have seen an increase in both overall operating expenses and the percent of those expenses that are coming from personnel. Since 2019, average expenses for arts and cultural organizations in our dataset rose by 19%, while personnel costs rose by 35% over the same period. Another way to interpret the data would say that 92% of the increase in operating expenses from 2019 to 2024 have come from increases in personnel expenses. This dramatic increase in wages is already having significant impact on the way organizations structure their workforce and will require further shifts in the future in order to keep the sector's employees at competitive rates.

Comparing averages for arts and culture nonprofits and for-profit salaries is highly dependent on a number of different factors including geography, budget size, education, role, tenure, etc.[2] This makes blanket statements like *"nonprofit salaries are less than for-profit salaries"* difficult to support, but there are numerous reports that show the discrepancy between for-profit and nonprofit salaries grows as workers move up in title and responsibility.[3] Another measure of compensation and job satisfaction could be turnover rates by industry. For all companies in 2022, turnover rate was approximately 12%. For arts and culture nonprofits, it was estimated at 35%.[4] Compensation is only one component of job satisfaction and turnover rate, but we are making the argument that in general, even if for-profit and nonprofit salaries are similar, workload and expectations are often greater in the nonprofit world which leads to higher turnover. In addition, if it is true, generally, that the gap between for-profit and nonprofit salaries widen as title and responsibilities grow, this could also be a contributing factor to higher turnover as employees move up in the ranks.

The point we are making Is that this increase in personnel expense is not necessarily a negative for the long-term health of the sector. While double-digit percentage increases make budgeting more complicated in the short term, it is possible to assume that these increases are a correction for historical underpayment and future compensation levels that are more similar to the economy as a whole should help with greater job satisfaction, reduce turnover, and better allow organizations to plan long-term and retain institutional knowledge.

[2] https://nonprofitquarterly.org/its-complicated-nonprofit-organizations-and-wage-equity/
[3] https://www.artsy.net/article/artsy-editorial-survey-art-salaries-revealed-disparities-compensation-for-profit-non-profit-organizations
[4] https://socialimpactarchitects.com/nonprofit-turnover/

BUDGET SIZE[5]

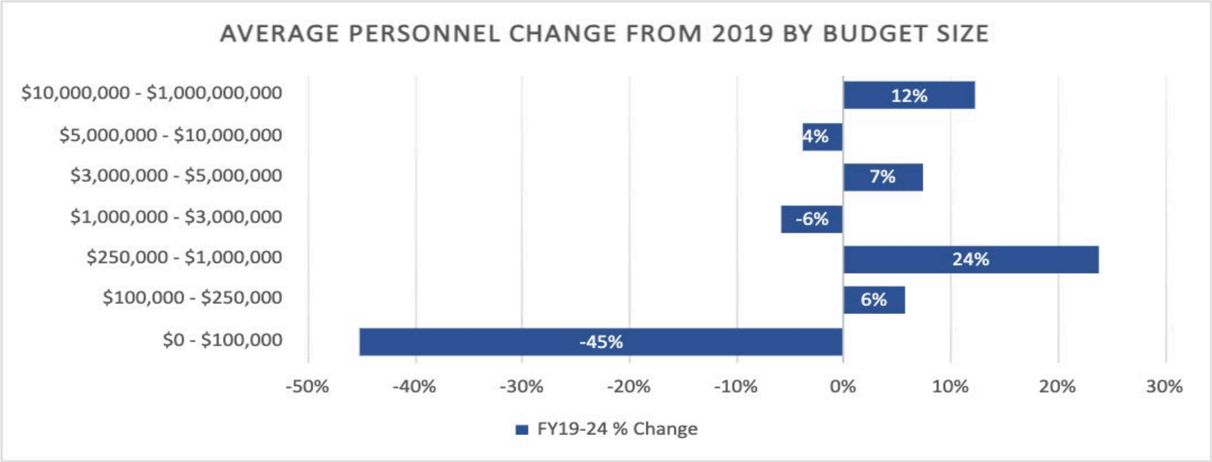

FIGURE 3 – PERSONNEL CHANGE FROM 2019

The correlation between budget size and change in personnel expenses presents some interesting takeaways. The chart above shows the percentage change in average personnel expense between 2019 and 2024 by budget size of organization. You can see that organizations with budgets of less than $100,000 had a significant reduction in personnel expenses. While we do not have exact data, anecdotally, we have heard of many smaller organizations that have shifted to more volunteer work as a way to combat higher wages. In addition, general inflation has moved many of the organizations from this category up to the $100,000-$250,000 bracket, leaving the remaining groups more towards the lower end of the zero to $100,000 range. Regardless, in terms of absolute dollars, it is organizations above $10 million budget size that have seen the largest increase. Those organizations, on average, have annual personnel expenses that are now $15.5 million. This is $1.7 million greater than they were in 2019. Again, without having the exact data, these larger organizations generally have a greater need for full-time employees and are often subject to multiple organized labor contracts. It is also worth highlighting the budget group between $250,000 and $1 million. Wage increases in this budget category can be particularly difficult to manage as this is often the bracket where organizations start to hire more full-time employees and find it more difficult to deliver on their missions with volunteers alone.

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[5] Budget size is defined as operating expenses.

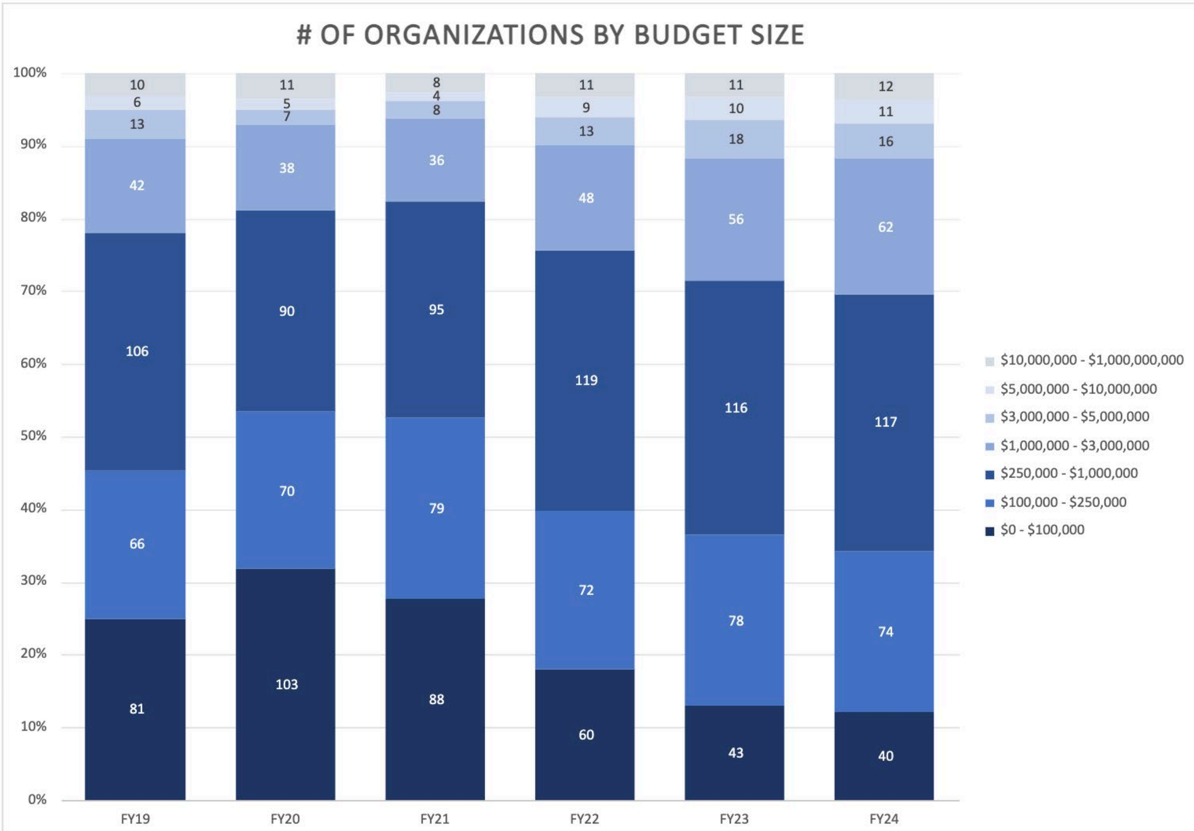

FIGURE 4 - NUMBER OF ORGANIZATIONS BY BUDGET SIZE

Figure 4 shows the number of organizations in each budget category from 2019 to 2024 budgeted. The takeaway from this chart is that inflationary pressures have pushed organizational budget sizes up in all categories. The significant reduction in the number of organizations with budgets under $100,000 could be seen as a statement that it is increasingly more difficult to run a smaller nonprofit and that the entry point for doing this type of work has risen since 2019.

What implications does this have for the sector?

The primary take away from this data are that the arts and culture nonprofit sector seems to be going through a correction when it comes to wages. We assume that this pace of growth will not continue indefinitely, but that these wage levels as a percent of total operating expense will remain the norm. This could lead to short-term reorganization, potential layoffs, and mergers or shared services. While short-term reorganization may cause disruption, the long-term benefits of more equitable pay have the ability to strengthen the sector as a whole. The ability to attract talent and maintain retention rates and institutional memory should allow for organizations to plan better and increase the strength of their infrastructure. It should also be noted that growth in non-personnel expenses, which can include direct programming costs, may slow relative to personnel expenses. In fact, in our data, non-personnel expenses have only grown by 3% since 2019. We know that inflation has been far greater than 3% over that time and so the assumption is that there has been a reduction in overall offerings funded by non-personnel expenses. This is not necessarily a bad thing and can be seen as a part of rightsizing the sector's offerings with a level of pay that is appropriate for retention and growth.

Short-Term

We have seen some of the short-term effects of higher wages already. Closures, mergers, and shared services have been front-page stories for the past several years. Even if organizations raise more funds, they are forced to allocate more of those dollars to payroll, potentially limiting the ability to grow staff. As demand continues to recover, organizations confront the reality that the overall cost of production has increased and efficiencies need to be found in other areas in order to compensate. Different organizations will have different approaches depending on geography, discipline, etc., but part of what we are seeing is an exploration of strategy that will allow for this wage structure. Mergers and shared services have long been seen as a potential remedy for nonprofit financial issues. Prior to this wage growth, ArtsFund participated in a study, conducted by Public Media Company, that suggested that merging backend services for a small subset of arts and culture nonprofit would actually not be financially beneficial because of how lean most organizations already were. What we are seeing now is organizations reassessing this assumption in the face of higher wages. It is good that organizations are revisiting these strategies, not necessarily to promote downsizing, but to provide additional capacity for growth without taking on additional payroll expenses.

Long-Term

The trope of the starving artist is one that is born out of a certain reality. This also applies to many art administrators. Financial incentives have never been a key driver for young people to enter the field and there has always been an assumed sacrifice in terms of salary that is balanced by and the ability to *"do what you love"*. These assumptions are less true today than ever and have potentially contributed to some of the harm we have been trying to work through over the past several years. Reduced salaries, lack of benefits, and insufficient job security have created environments that preference workers with existing wealth, or the willingness to suffer financially compared to other employment. The same set of circumstances has also reduced the ability of the sector to hire and train top talent. The reduced compensation structure has severely constrained the pipeline of who enters arts and culture as a career, and we are currently seeing the ramification of that in our attempts to diversify leadership. This is not to say that there are not diverse leaders ready to take on these roles, only that we have missed generations of potential leaders that could have been ready to step in had it not been for financial constraints. The long-term benefit of permanent salary adjustments is that we will be opening doors for a wider group of young people to enter the field, and this should translate into a more robust set of leadership candidates in the future. In addition, if we can continue to maintain wage levels at or near similar levels in other industries, we should be signaling to educational institutions from K-12 all the way to advanced degree granting institutions that training young people in the arts and arts management is a worthwhile investment for them as well. If we can maintain a healthier wage structure in the sector, those gains should multiply throughout the community and create a stronger infrastructure for arts and culture in general. Given the benefits of a healthy arts and culture sector to the entire community, this shift in wages could lead to better long-term outcomes for everyone.

Potential Levers

Both organizations, and those who fund those organizations will have several levers to pull when trying to adjust to this new reality. There are practical steps that can be taken along with shifts in mindset around what a healthy arts and culture nonprofit looks like. As the sector reorganizes itself and begins to test some of these strategies, there's no doubt that new opportunities will arise and lessons will be learned, but below are several potential ideas that both funders and grantees can consider for managing the change.

For Arts Organizations

Mergers and shared services

As mentioned above, mergers and shared services have always been a questionable approach for addressing nonprofit efficiencies. Part of the skepticism around its effectiveness for smaller nonprofits was that wages were so low, and workers were typically working so far beyond capacity that there were no gains to be had by consolidation. We are not suggesting that a potential solution is to pay people better and then double their workload, but if individuals in several different organizations have increased capacity and are doing similar roles, it could make sense to use that capacity to explore opportunities to scale together. We are already seeing demand eclipse 2019 in nominal dollars[6] and so mergers and shared services would not be an attempt to reduce the total workforce, but instead a way to prepare for further demand. If we assume that people will continue to come back to our theaters and our galleries in larger numbers, then developing physical and technical infrastructure that will allow workers to handle more volume without adding more people can be a way to reduce overall cost per transaction in an industry that often sees a loss on every ticket sold. Whether it's box office, finance, warehousing, or rehearsal space, we feel it is worth revisiting this strategy.

[6] Total revenue in our sample data is up 14% from 2019 unadjusted for inflation.

Reorganization and Rightsizing

Rightsizing workforces in the short term may be a reality for some organizations. We are calling out this reality not to make the recommendation as a first resort, but to recognize that it might be the correct move for some organizations. As mentioned above, you can make the argument that arts and culture nonprofit sector wages have been artificially depressed for years. This is rarely the fault of the organizations themselves and is often a result of funders' pressure to keep overhead low. As we enter into an environment where wages are more in line with livability and other sectors, it makes sense that budgets may not support the same level of staffing. People are an organization's most valuable resource, and any downsizing must be thought of strategically and often as a last resort, but as a funder, we also wanted to recognize that strategic workforce reorganization is something that many groups will consider. If done as part of a thoughtful strategy to align expenses with demand, it can make sense to see this as a tool to more long-term financial health.

Better retention

As mentioned above, in 2022, the turnover rate for arts and culture organizations was 35% compared to 12% for the entire economy. It is also estimated that the cost of turnover is approximately ½ to two times an employee salary.[7] As wages increase, the financial benefit of retention is even greater. To walk through an example, if your total payroll was $100,000 in 2019 and your turnover rate was 35% of that, then the cost of that turnover in 2019 was roughly between $17,500 and $70,000. If your wages are up 35% in 2024 then your payroll is now $135,000 and that same 35% turnover will cost you between $23,625 and $94,500. The difference ranges from $6,625 on the low end to $24,500 on the high-end. This is per every hundred thousand dollars of salary and so for an organization with $1 million payroll, that increase in turnover costs due to increased wages can be well over $150,000. Another way to think about it is to say that every one percent turnover can cost your organization up to $700 for every hundred thousand dollars of payroll. That may not seem like a lot, but the average payroll for organizations with budget sizes over $10 million is $15.5 million per year and using the above calculation and a 35% turnover rate, this increase in wages could cost up to an additional

[7] https://www.gallup.com/workplace/247391/fixable-problem-costs-businesses-trillion.aspx

$3.8 million per year in turnover cost. And that doesn't come close to capturing the full cost of turnover when you calculate in the loss of institutional knowledge and employee morale. The point is that focusing on retention has always been an important challenge for nonprofit leaders and that challenge is amplified in importance by these dramatic wage increases. Focusing on employee wellness will not only create a better culture, but also improve the bottom line.

For Funding Organizations

Relaxed overhead requirements

Different lenders will have different requirements when it comes to evaluating overhead as a percentage of total project, cost or organization cost. What number makes sense depends on the industry, the geography, the project, etc., but what we are recommending is that funders take the new wage reality into account when calculating what that overhead should be. Nonprofit arts organizations have a heavier reliance on labor than their for-profit counterparts that can often increase efficiency through capital/technology investments. Because of this, as wages increase relative to other costs, funders should be aware that overhead percentages will increase. In addition, funders should pay attention to livable wages in different cities and adjust their requirements accordingly. In summary, funders should be careful not to put pressure on organizations to depress wages below levels that allow grantees to hire the best people.

Direct funding of salaries and employee retention

ArtsFund still maintains that unrestricted funding is the most effective way to align philanthropic dollars with the need of the sector. That said, if granting organizations must find specific projects or initiatives, we recommend that they look at funding capacity, growth for salaries and other employee, retention programs, including benefits, sabbatical's, etc. Depending on the organization, there can be a gap between salary levels that are affordable to organizations and market levels that allow them to be competitive. Funders should investigate whether funding that gap leads to better medium and long-term strategies, and how they can direct funding specifically to improve organizations abilities to hire. This includes funding retention programs as well, given the cost of turnover highlighted above. While the intent of minimizing overhead is to create larger impact on community facing programming, supporting healthy salaries and retention can result in more dollars for organizations to use to fund their mission and programming.

Continued advocacy for better wages

Funders often play a critical role in unbiased advocacy for the sectors that they participate in. Whether you are an institutional funder or an individual funder, you can use your voice to advocate for a better wage structure for arts and culture nonprofits. This sends signals to organizations that they can invest in their people, and to corporate and public sector decision makers to pay attention to this situation as well. Part of our responsibility to the sector is to create positive narratives around those industries. The trope of the starving artist is one that is heavily ingrained in our society. Funders have the ability to help push back against this narrative by doing their part to bring wages closer to market, and to be vocal about why that is important for the long-term benefits to society.

Conclusion

From 2019 to 2024, there has been a significant shift in arts and culture nonprofits' expense structure, leading to a 7% increase in wages as a percent of total expenses. This is a result of a 35% increase in average wage expenses over the same period. We feel that this shift is permanent and reflects a positive move towards more equitable wages in the sector.

The long term benefits of more competitive wages in the arts and culture nonprofit sector have the potential of creating a more stable environment for organizations and their missions. In the short term, organizations will be challenged to adjust budgets in order to meet this new wage demand. In order to make these demands, organizations can continue to look at mergers and shared services, rightsizing workforce to demand, and prioritizing low turnover rates. Funders can continue to support more realistic overhead percentages, direct funding of wages and retention programs, and advocate for better wage equity in the sector. The short term result will be continued reorganization of how organizations balance wages and other expenses, potentially leading to further disruption, but the long-term outcomes are a more stable sector that attracts top talent and retains that talent for longer periods of time. This should create a sector that is better equipped for long-term planning, and better able to meet any future shocks that come their way.