



**The Hauser Center**  
for Nonprofit Organizations

**The Road Less Traveled<sup>1</sup>**  
**Funders' Advice on the Path to Nonprofit Sustainability**

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<sup>1</sup> With apologies to Robert Frost, *The Road Not Taken*, 1920.

## INTRODUCTION/PRECIIS

As part of the *Capital Ideas* symposium co-hosted by the Hauser Center for Nonprofit Organizations at Harvard University and the Nonprofit Finance Fund in March, 2007, an online survey was conducted about funder practices that support nonprofit sustainability. This article highlights the survey findings and the advice that funders offered from their own experiences as paths to greater nonprofit strength. Rather than a qualitative analysis of funding initiatives, this article presents guidance *to* the field *from* the field, as funders grappling with how best to strengthen the long term health of their grantees reflect on their works in progress. This article then goes a step further by annotating these lessons learned with the additional perspective offered from just four of the ten draft funding principles that have evolved from the *Capital Ideas* symposium with the hope of encouraging more funders to consider these principles and practices in their own work.

The *Capital Ideas* survey generated 48 profiles of funding approaches, practices and strategies that support nonprofit organizational capacity building, long term financial health and or programmatic improvement. The lessons funders learned from those initiatives informed ten funding principles that were introduced at the Capital Ideas symposium on March 15, 2007 at Harvard University. Four of those draft principles, outlined below, offered concepts that resonated throughout the profiles and are offered as key steps for funders to consider as they reflect upon their own giving practices. These principles include:

- 1. Understand when you're "building" or "buying," and fund accordingly.**
- 2. Actively pool resources when more funds are required to achieve results.**
- 3. Minimize the transaction costs for grantees and funders of applying for and reporting on grants.**
- 4. Fund at the organizational rather than the programmatic level, even when your primary interest is in one program.**

## BACKGROUND

Funders have long pondered how best to help nonprofits find their way and fulfill their missions to create greater social value and impact. The field has debated the value of general operating support, overhead rates, venture philanthropy and other engagement or investment models as pathways to build longer term ability within nonprofits. Yet, despite these debates and the funding methods they represent, the nonprofit sector suffers from the bumpy ride of unique and changing priorities, under funding and uneven access to the very types of capital it needs to thrive. These problems can be traced to many routes but they share a common root cause. Many of them involve the unintended and often impairing consequences of the ways funders structure and restrict the flow of capital into the sector.

Concerns about accountability and the quest to innovate new solutions rather than sustain working ones have led many funders to more narrowly target their support. With these restrictions come new burdens and additional costs without the resources required to meet them. The lack of standardization in everything from data and performance metrics to grant requests and reporting requirements has only added to the transaction costs nonprofits incur in funding their work. Funder reluctance to underwrite infrastructure or to help nonprofits build reserves or gain growth capital further impairs the sector. Working in the trenches, and sometimes just out of range of these debates, nonprofit leaders wonder why there is any deliberation at all when *they* know what they need. To thrive, or even to meet the demands of providing their rarely fully funded services, they want a new roadmap and need a different kind of funds flow and relationship with funders.

Now, based on the results of this small but influential sample of funders, these same nonprofit leaders can take heart. A new form of GPS – grantmaking positioning system – may be in play. These funders believe that they can and must do better collectively in their investing behavior. The key lies in improving how investors structure, steward and Sustainability must be viewed in that context – the desire to achieve greater impact -- rather than in this misplaced notion that sustainability means perpetuity for all, divorced from mission, business model or organizational lifecycle. Many funders have grasped this goal and are at work with their nonprofit partners to bring about needed change on how they fund the sector. They are traversing a road less traveled. In the *Capital Ideas* survey, these funders offer their own miles markers and guideposts along the way, hoping to make “all the difference. “

The *Capital Ideas* Symposium, and its Funding Principles and Funder profiles<sup>2</sup>, grew out of this conviction that funding practices must change if nonprofits are to have a better chance of fulfilling their missions. Three sector leaders with differing affiliations but significant experiences in the field, Kathleen Buechel and Elizabeth Keating of the Hauser Center and Clara Miller of the Nonprofit Finance Fund, agreed to collaborate in order to help reform how the nonprofit sector is funded. Together, the Hauser Center for

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<sup>2</sup> See Capital Ideas Proceedings, Funding Principles and Executive Summary at <http://www.isites.harvard.edu/k14620>, and at the NFF website, <http://www.nonprofitfinancefund.org>.

Nonprofit field leaders to help chart a new course. Called *Capital Ideas: Moving from Short Term Engagement to Long Term Sustainability*, this one-day symposium brought together thought leaders from research institutions, nonprofits, intermediaries, foundations, and government, people not frequently together to discuss funding norms. The groups considered promising practices, funding principles and additional policy or behavior changes required to encourage more investment in organizational capacity and financial health. Participants discussed barriers that funders faced in adopting these methods and emerged with the perspective that additional action is required if more funders –including foundations, significant individual contributors, intermediaries and government - are to adopt longer term and more effective practices.

### **Survey Structure and Highlights**

To frame the discussion, the symposium organizers circulated a brief survey of practices, programs or principles that supported organizational capacity building, financial health and programmatic improvement. The results yielded 48 profiles of initiatives, approaches or strategies designed to foster long-term sustainability in organizations, 20 of which were circulated to symposium participants with pre-reading materials. All of the profiles are available on the *Capital Ideas* Symposium website <http://www.isites.harvard.edu/k14620>.

The *Capital Ideas* survey was designed to collect giving practices and advice from funders actively engaged in supporting long-term sustainability. It is not a scientific or randomly selected sample, but rather represents a self-reported funder inventory of initiatives and experienced advice for colleagues. These practices involve three strands: building organizational capacity, addressing long-term financial health, and improving programs. The 75 responses received before the symposium included those from <sup>3</sup>symposium invitees and members of Grantmakers for Effective Organizations (GEO). Nearly 44 percent of the respondents were from private foundations, 15 percent from community foundations, and 12 percent from family foundations with the rest derived from public charities, intermediaries and operating and health conversion foundations.

This article presents their advice and annotates them from the perspective of just four of the 10 Funding Principles sparked by the *Capital Ideas* work and Symposium.

The survey first queried funders about their overall giving. Most foundations indicated they invest up to 25% of their giving in organizational capacity building, long-term financial health or program performance. Approximately 15% of those sampled indicated that 75-100% of their funding fell into each of those three categories. Most of the survey respondents award general operating support (only 17 percent of the sample said they did not provide such funding). The format of their general operating support investments vary: 32% of respondents provide general operating support as standalone

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<sup>3</sup> GEO represents more than 300 member foundations in a coalition dedicated to building more effective nonprofits. Its mission is to maximize philanthropic impact and the effectiveness of their grantees through research, applied learning, convenings and information exchange.

grants, 24% provide them alongside other program funding and 27% provide general operating support in both forms.<sup>4</sup>

### **What Funders Think Should Change**

Despite the diversity of their approaches, when asked about their views of potential behaviors and attitude changes that could improve nonprofit sustainability, four areas of strong agreement emerged. These convictions are echoed in the draft funding principles from the Symposium:

- Nearly 94 percent agreed that foundation relationships with grantees should change from oversight to partnership.
- Ninety percent agreed with the need to simplify grant applications and reporting, to make grantee effort commensurate with grant size and scope.
- More than 80 percent concurred that foundations should jointly decide with grantees on evaluation tools and metrics, that most grants should have fewer line items and other restrictions, and that foundations should increase the size and length of grants, even if that meant that fewer nonprofits were supported.
- Nearly 70 percent contended that standardization with other funders of grant applications and reporting is advisable.

Views differed on the potential challenges that may prevent funders from adopting sustainability initiatives and on how they could be overcome. The survey's suggested obstacles included the lack of recognition opportunities, the lack of support from Foundation Boards, and the long timelines involved. The discussion that occurred at the Symposium after the survey results were shared indicates that these challenges and others are formidable, and must be better understood for progress on sustainability to be achieved.

### **Funding Profiles and Key Findings**

The greatest value of the survey rests with the profiles, which are instructive both in the breadth of the models and the advice they offer. We asked funders to briefly profile, in their own words, at least one initiative, approach or strategy at their foundation that supports the long-term sustainability of their grantees. This could be a traditional funding program, a general approach to giving, or a giving strategy that crosses program boundaries. We indicated that we were particularly interested in initiatives, approaches or strategies that help grantees build organizational capacity, secure long-term financial health, or improve program performance.

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<sup>4</sup> These percentages are comparable to a recent study of general operating support from the University of San Francisco. The study found that a greater percentage of foundations prefer providing both stand-alone and program-related operating grants (48.9%) and equal percentages preferred either stand-alone or bundled (23.9%) support.

The average grant size reported varied considerably—not surprisingly, given the range of foundation assets covered, but somewhat in contrast to the Center for Effective Philanthropy (CEP) data on the median size of grants in general for the 30 largest U.S. foundations. The CEP data shows that the average grant size within their foundation sample is \$50,000. The median grant size of our Capital Ideas Symposium respondent initiatives was \$75,000, indicating an inclination toward slightly higher funding levels among the sample.

Overall, these initiatives range in grant size from \$5,000 to \$5,000,000 with the average grant size of \$550,000 skewed by the larger values in the survey sample. Any given foundation profiled awards between \$10,000 to \$35 million in these approaches. Combined, the profiles represent \$135 million invested annually in the nonprofit sector. Eight of the profiled initiatives had a median grant size of greater than \$1 million, suggesting they had reached a significant scale requiring substantial investment of time engagement and money. Others appear to be in pilot form, both in scale and in time and action.

Seventy-five percent of these initiatives represent less than 25% of a foundation's total annual giving and only 20% represent more than half of a foundation's annual giving. This compares to the University of San Francisco study on general operating support in which 50% of responding foundations (203 California foundations) indicate that general operating support represents less than 25% of overall giving.

Whatever their size, the results indicate that these initiatives rarely represent the foundation's main focus. This survey presents a small sample size, whose instructive value may be larger than the number of respondents, as their approaches offer an important mine of research and practical opportunity to explore what works better in supporting longer term nonprofit health. While additional research into the impact of these approaches is needed, this article suggests that if more positive funding activity were undertaken to correct the current mismatch of funding structures and sectoral needs, the sector and society would benefit.

When asked about the motivations behind these initiatives, most respondents said they sprang from foundation staff and leadership commitment and concern for the problems grantees were facing. Respondents also highlighted staff issues when reporting challenges, including the considerable staff time and expertise these initiatives require. Nearly half of survey takers reported having to create their own models because none existed for them to follow. This finding supports the rationale for generating the survey profiles in the first place— to share practices and advice. It also suggests that additional peer-to-peer exchange or joint learning could be an important tool that funders can use to encourage others to follow their lead, since—according to the survey—staff are the key champions of these approaches. Further outreach could provide even more sought after examples and funder encouragement to adopt these practices..

## **Issues Addressed**

The profiles present diverse foundation initiatives: everything from city-wide data collection projects, general operating support grant-making, technical assistance grants and contracting, sector wide learning circles and alliances, core-support programs, investment in intermediaries, venture philanthropy models, endowment development initiatives and community-wide capacity investments. They also cut across fields: affordable housing, the arts, human services, domestic violence, education, youth service, the environment. The initiatives come from all across the country: from Washington DC to Washington state. A compendium is attached in Appendix I.

### **Listening to the Profiles: Challenges and Advice from Funders**

We analyzed the initiatives we received in six ways: by foundation size, type and sector and by initiative size, duration or sector. The initiatives best clustered around three initiative types roughly characterized as Capacity Building Grants, Partnerships and

#### **Clusters of Funding Models Reported in the Survey**

**Capacity Building:** Initiatives that strengthen capacity of individual organizations by: investing in leadership training or development, strategic planning, fundraising development and/or providing technical assistance as well as initiatives that build the capacity of a sector. This includes initiatives that build the capacity of a group of service providers, generally categorized either by region or type of service provision. Also included are Capital Grant-making initiatives.

Total # of Initiatives Profiled: 31

Percentage of Initiatives Profiled: 65%

Range of Median Grant Size: \$5,000 - \$2.5 million

**General Operating Support:** Approaches that provide unrestricted support to organizations. Also included are two initiatives that provide long-term program support to a single large initiative.

Total # of Initiatives Profiled: 6

Percentage of Initiatives Profiled: 12%

Range of Median Grant Size: \$50,000 - \$220,000

**Partnerships:** Includes partnerships among funders that pool resources or data, initiatives that fund nonprofit partnerships across regions or service sectors and funding intermediaries.

Total # of Initiatives Profiled: 11

Percentage of Initiatives Profiled: 23%

Range of Median Grant Size: \$7,500 - \$350,000

General Operating Support.

In analyzing both the challenges and advice that funders provide, several trends and critical insights emerge.

### **General Operating Support**

Six general operating support initiatives were profiled with grant size ranging from \$50,000 - \$200,000, and total initiative giving between \$300,000 and \$17 million. These large operating support grants generally reflect foundation efforts to invest deeply in high performing organizations. The survey indicates that more funders give general operating support than chose to profile it in the initiatives they offered. Because funders selected only one or two of their own initiative to profile, we suspect those who chose to profile general operating support initiatives did so because their operating support efforts are prompted by the desire to strengthen the capacity or long term financial health of organizations.

FB Heron, who provides over two-thirds of its grant-making in the form of unrestricted grants, describes their core support as “akin to working capital for a business or a way for us to 'buy into' the organization's business plan.” Neighborworks America indicated that general operating grants encourage “more honest insight from grantees as to how funds are used.” Both funders indicated that through general operating support, they are able to move their relationship with grantees to a higher level. The Whitman Institute indicates grantees reporting that “ongoing, operating support helped provide them with the flexibility and freedom to build relationships with other organizations over time that resulted in collaborations that have strengthened and expanded their work.” Others, such as the Bank of America Charitable Foundation have found the greatest success pairing general operating support with executive leadership development opportunities. They have found this “strengthens the decision-making power of the grantees so that those receiving the funding will deploy these dollars effectively.”

### **Challenges of General Operating Support: Bringing your Board on Board & Measuring Impact**

Organizations also faced challenges implementing operating support initiatives. The two most common challenges were 1) convincing their boards of the value of general operating support and 2) struggling to measure the impact of their grants.

FB Heron notes that part of its success with core funding is that “the issue of discerning OUR impact vs. that of other funders has not been a primary driver for our board or staff.” Instead, the foundation uses a performance scorecard to evaluate the overall success of an organization and scales their investment into organizations demonstrating the greatest success. The Whitman Institute similarly attributes part of their success to the fact that “the direct role our funding has played is less important to use than the overall success of the organization.”

However, as organizations are encouraged to give larger operating grants over longer periods of time, a trend that nonprofits encourage, the McCune Foundation cautions that “with knowledge that one funder has a particular interest in ongoing support to the agency, other private foundations became ‘less interested.’” They indicate that “over reliance on a few funding streams makes an organization vulnerable to shifts in priorities and interests.” This suggests that as funders make larger general operating grants over

time, they must be aware not only of the benefits provided to an organization, but also of the possible unforeseen consequences. As Hank Beukema of the McCune Foundation notes “Among some funders the “C” word in public may be collaboration and cooperation, but the “C” word in private may be competition in the “ideas” arena as some want to be first to write and publish about it. We need to encourage these funders to share the stage with others and to take a longer term view.”

Funders may need to anticipate and counteract elements that discourage other funders from joining them, whether in the perception that additional funders are not necessary, or in the view that the work cannot be linked to specific outcomes, innovations or the credit that accrues to both. Convening other funders with the grantee to learn about its effectiveness, sharing metrics that relate to both organizational health and outcomes or identifying opportunities for funders who value it to get a specific type of visibility are possible ways to counteract this concern.

### **Partnerships**

We classified eleven of the forty-eight profiled initiatives as partnerships. Several were among foundations while other initiatives supported partnerships among nonprofit grantees across a region or service sector. Three initiatives are for pooled data projects, one of which, the Pennsylvania Cultural Data Project, was highlighted at the Symposium.

### **Challenges & Advice for Building Partnerships: Factor in Enough Time to Seed Relationships and See Impact**

The Pennsylvania Cultural Data Project, administered by the Pew Charitable Trusts, brought together seven funders from eastern and western Pennsylvania to streamline the data collection and evaluation process for arts and cultural organizations. Pew noted that everything requires time and clear communications: building partnerships with foundations, building trust with applicant organizations as well as creating a plan to effectively use the data. Other partnerships echoed Pew’s concern about time. The Ball Foundation, which is funding school systems to increase literacy, advises a funder to “Allow enough time for reflection and learning.” Likewise, the Nokomis Foundation, which has built the technology capacity of a consortium of 14 women’s organizations, encourages funders to “build in enough time to see the results!” Nokomis’ two-year initiative is now in its seventh year. Venture Philanthropy Partners’ (VPP) Fred Bollerer contends that his foundation’s relationship intensive interventions require more like seven to 10 years of support to be transformational, rather than the three to five years they initially envisioned.

Respondents admitted that forming partnerships can be challenging. One organization wrote about tensions between partners, another of partners who did not complete their commitment. Woods Charitable Trust notes that this work is heavily relational, and as such, advises organizations to be patient and design in a relationship-building component. Despite such challenges, the impact of initiatives like the Pennsylvania Cultural Data

Project have enormous potential, especially if all of the partners have the staying power to see the mutual advantage of collective action.

### **Using Partnerships to Pool Resources**

Another potential value of partnerships is the opportunity to pool expertise and resources among funders. Anecdotes abound about initiatives that languished because the funding from one investor and the information gained did not meet the aspirations of the initiative. Other projects are simply chronically under funded and cannot grow to sufficient scale or efficiencies. Pooling resources and effort can help overcome this obstacle. Diagramming which funders can intervene where and for what time period can build the range and length of funding required to make initiatives effective. Pooling funds through an already existing mechanism like a community foundation can achieve greater efficiency. This model surfaces in the Human Services Integration Fund model operating in Allegheny County, Pennsylvania. Multiple funders offered seed capital to a number of opportunities for the Department of Human Services to build data bases, infrastructure and other service enhances for the county that public dollars would not cover.

### **Capacity Building**

We received the greatest number of profiles (32) of initiatives self-described as targeting capacity building efforts. These programs ranged from organizational capacity building such as grants from the Edna McConnell Clark Foundation that invest deeply in youth-serving organizations to high engagement partnerships profiled by New Profit Inc. in Boston. Others, such as the Meyer Foundation's Exponent Award focus entirely on Executive Leadership development while still others concentrate primarily on capital projects. A group of small grants focuses specifically on providing technical assistance. Finally, seven initiatives were considered to be "sector-wide capacity building grants" which worked to not only strengthen the capacity of an individual nonprofit, but rather an entire city, community or sector. For example, the Boston Foundation's Nonprofit Program strives to "strengthen and reposition the nonprofit sector" and the Grand Victoria Foundation "seeks to increase philanthropy in Illinois by developing the capacity of community foundations."

### **Challenges: Executive Leadership and Measuring Impact**

Two of the greatest challenges faced by organizations implementing capacity building initiatives in this sample were sustaining progress during executive transitions or under weak executive leadership and measuring impact.

The Meyer Foundation indicated that the success of their Management Assistance Program was due in part to executive leadership and "if the executive leadership of the organization is weak or in transition, the Management Assistance Program interventions often fail." In response, the Meyer Foundation created the Exponent Award which

recognizes extraordinary executive directors and provides two-year \$100,000 grants for leadership development.

Organizations such as the Hawaii Community Foundation who were struggling to measure impact found that “you can learn as much from the stories that organizations share with you” and indicated that many of their metrics in fact emerge from stories. The Lumina Foundation for Education was one of many that recommended working alongside grantee partners to develop benchmarks and measurable outcomes. This contrasts to the practice of funders or consultants creating the metrics too early in the process or in isolation from their nonprofit partners.

### **Advice: Become a Partner, Utilize Experts & Engage the Board**

The most consistent piece of advice offered by these funders was to become a partner, not an auditor. Common Good Ventures indicates, “A foundation needs to be ready to become a convener, partner and consultant as well as use their own networks and resources to move the program forward.” One way that the Lumina Foundation recommends doing so is to “spend more time 'up front' engaging the principal grantee organizations (the intermediaries who will carry the lion's share of the load) in co-creating the plan. Grantees have a greater commitment when they are designers as well as implementers.”

Funders completing profiles also recommend utilizing outside experts and intermediaries when possible for a number of reasons. Some cited the heavy staff load created within their foundations by these initiatives while others lauded the value of adding additional perspective and experience. For example, the MacArthur Foundation recommends that a funder use experts during the design phase and “if possible, retain experts to assist with implementation if relevant expertise is not available in-house.” The Boston Foundation, after trying to build their initiative internally recommends, “Don’t try and do everything in-house and your self.” The Boston Foundation has since utilized its convening power to bring together nonprofit leaders to discuss initiative development, have made small contracts to academia to develop discreet portions and have used “strategic relationships with donors (like consulting firms who had relevant content expertise) for educational forums, workshops.”

Finally, funders of capacity building initiatives indicated that board engagement is critical to the success of these programs, at both the foundation and nonprofit levels. The Edna McConnell Clark Foundation indicates that “staff and board alignment behind the effort is essential – everyone must be focused on the same goals and objectives.” Rotary Charities of Traverse City, MI indicate that education of their own board education has been a success of their capacity building initiative and Pew Charitable Trusts recommends engaging the nonprofit boards by presenting results to both nonprofit staff and board members.

### **Our Advice -- Funding Principle Perspective**

The authors were struck by the consistency of advice funders offered others about their initiative types. As noted earlier, these profiles and their guidance helped to frame the *Capital Ideas* draft funding principles. Those principles provide additional food for thought for funders seeking better ways to support the nonprofit sector's longer term organizational needs. We annotate the advice funders offered with just four of the principles because they cut across the three funding types our survey respondents profiled, not because the others are less important. A full list of the draft funding principles that followed the Symposium is available in Appendix II. They equally apply to both collective and individual funder actions.

### **Principle #1 -- Be a Builder or Buyer and Fund Accordingly**

An important first step in making more effective grant is to identify what kind of funder you are and then to structure your investments and requirements accordingly. Clara Miller and George Overholser of the Nonprofit Finance Fund have characterized funders as either **Builders**—equity investors interested in sustaining, growing or altering an organization and expanding its work – or **Buyers** – those most likely to contribute to the day to day operations without imposing additional requirements or changes in what the NGO offers. Participants at the Capital Ideas Symposium drew on and expanded how these terms can contribute to sector sustainability and robustness.

Each type of funder – whether builder or buyer – is important to the sector's prospects. However, each must tailor its funding and its requirements according to its role and the size and scope of its investment. Equity investors – builders – can expect more engagement with the nonprofit partner. They may be called upon to offer the grantee a combination of operating revenue and capital investment. As is echoed in the profiles, funding from builders should be reliable, larger and longer investments. Our funding principle suggests that buyers, whose investments can also be substantial, should refrain from requests for special requirements or massive documentation in order to keep transactions costs commensurate with their funding role.

The Builder/ Buyer construct applies to each of the funding types categorized in the survey. It may offer some special insights about general operating support, which has generated a great deal of attention and ink in the field recently. Much significant work has appeared in recent years about the value and role of general operating support in the sector. These grants are important, often preferred by nonprofits and can be a tool for both builders and buyers. A buyer may wisely choose general operating support as a means of paying for services while minimizing transaction costs. The prevalence of this type of operating grant is captured in a University of San Francisco study of 203 California Foundations. Seventy-eight percent of this sample provided general operating support grants, with an average grant size of \$63,000 and median grant size of \$17,261.

This type of operating support is a necessary but not sufficient factor in guaranteeing nonprofit longer term health. While the study indicated that many, and increasingly more,

organizations provide unrestricted grants, it found that their reporting requirements are not dissimilar to that of program-specific grants. Though grants are legally unrestricted, foundations seek measurable impact from their investments and often require rigorous monitoring and report. Few funders believed that foundation grants should be the primary source of operating support for a foundation, and those who opt out of providing unrestricted support most often cited external pressures for accountability (mission-alignment is easier with a program grant) and a commitment to funding innovation (which is difficult when committed to large multi-year operating grants to several organizations). The study indicated that foundation staffs are more often in favor of operating support than foundation board members and that there continues to be discussion across the field of the role of general operating support from foundations.

A similar percentage (83%)<sup>5</sup> of foundations that completed the Capital Ideas Survey provides unrestricted grants. Yet, operating support alone will not correct the mismatch of mission and money that dominates the sector, especially if the nonprofits use these funds to provide more short term services without reinvesting in their own longer term organizational needs. If they do not invest in infrastructure, operating reserves or capital needs, they may not be further along the road to sustainability at all. This suggests that it may be important to encourage nonprofits to think about using these funds for infrastructure and organizational needs, rather than more service provision, if possible, while maintaining the integrity involved in giving leaders of nonprofits the latitude to make decisions about their own internal allocation of funds.

## **Principle #2 --Pool Resources**

The second principle calls for funders to pool resources when greater impact can be achieved. This is illustrated in the Human Services Integration Fund initiative in Allegheny County, the San Francisco Arts Education Funders Collaborative, profiled by the Fleishhacker Foundation and the Endowment for Health's development of a statewide nonprofit association.

A note of caution is in order on the role of partnerships. As we heard repeatedly in the survey, partnerships rely heavily on relationships. Much good grantmaking derives from investment partnerships where there is mutual trust, professional respect and confidence in the acumen and skill of both parties. As these partnerships deepen over time, they are nurtured through personal and on going communication and connection. The draft funding principles offer the underlying notion that all aspects of the funding transaction should be commensurate with the size, scope and complexity of the initiative. This notion applies to building and maintaining grantor and grantee relationships, which can be time consuming, complex and even costly. Funders must be conscious of the time and hidden costs involved in responding to their requests and in deepening these connections. They should be sure that their input and interactions add value in the relationship and in the product of the work that the partnership produces. NGOs report significant time involved in applying for grants in the CEP study. Including a calculation of the value of the time involved in fostering the partnership in its many facets could be factored into the

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<sup>5</sup> The University of San Francisco study indicates 78% of their sample offered unrestricted support.

in the grant size. This recognition and valuing it in the grant amount are part of the<sup>6</sup> imbedded in the principles.

### **Principle # 3 -- Minimize transaction costs**

There are many costs associated with grant requests, reporting and the adoption and tracking of metrics that are frequently not reflected in grants. These costs may be unknown, unrecognized or simply unfunded. Containing these costs or paying for those incurred is a concept that cuts across all three types of funding initiatives. The common data platform of the Pennsylvania Cultural Data Project seeks to minimize costs through shared data, metrics, reporting and even grant request formats that can be tailored to a funder's specific needs without extra work by the nonprofit. As stated earlier, there is great value in keeping the work involved in grant requesting, stewardship and performance tracking commensurate with the size, scope and complexity of the initiative. Requiring special reports or non standard applications or metrics adds costs. If funders actually need these additional requests, then they should be willing to adopt a net grants approach so that the size of the grant reflects the costs of these special requirements. Standardization on many levels can lead to greater transparency, especially if funders parse through trend information and use common applications, metrics and data together to analyze problems and celebrate results.

### **Principle # 4 -- Fund at the organizational rather than the programmatic level, even when your primary interest is in one program**

Programs or services do not exist outside their organizational context. They are supported by staff, systems and processes that span programs and budget categories. Yet many funders continue to fund as though the program could be dissected from its institutional underpinnings. Many funders specify the program they want to support, or seek specific metrics and reporting as though the initiative were cleanly separate and distinct from the organization carrying out the activity. Often, neither the organization nor the funder either recognizes the full cost of administering that program as such costs are bundled across program areas and are difficult to segregate through accounting or other system constraints. This under funding continues to compound across multiple program areas with many funding sources. The administrative burden of tracking and reporting for a single nonprofit with diversified funders and program areas can be significant and unnecessarily wasteful in its complexity. Shifting to support that acknowledges that the funder was drawn to the nonprofit for this specific program, but understands that it should invest at the overall organizational level offers an important pro-sustainability tenet.

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<sup>6</sup> The net grants theory was described by Clara Miller at the Capital Ideas symposium as the estimated value of the time involved in stewarding the grant (transaction costs) minus the actual award to determine the true value of the grant. Most often, the net grant does not provide the resources necessary to cover provision of the service or the project, because so many cost dimensions of stewardship and grant reporting are not calculated with such granularity.

Going a step further, to adopt metrics tied to achievement of programmatic *and* organizational goals can help insure that the organizational capacity will exist to continue to provide this desired service or program. Grantmakers and grant seekers should work together in crafting these metrics so that in fact, the organization does balance longer term organizational needs with shorter term demands. Some have gone so far as to suggest that the performance measures for funders themselves should be tied to their grantees' actual success. Insuring that the right and shared metrics are used can help to define a new type of productive and more transparent relationship between grantseekers and grantees. It can help alleviate funders' concerns that without direct oversight, and audit like relationships they are "not doing their jobs" to insure that value is being created.

The funding principles suggest that we should not confuse control with accountability. More numbers, especially those that are activity based or represent input ratios (overhead, fundraising costs) should be avoided in favor of output metrics like outcome quality, change accomplished and work or services improved over time. This new type of working relationship between grantees and their funders may well require new foundation policies and a different type of engagement with the foundation's board initially, as earlier findings indicate that foundation boards are often not early champions of such approaches.

Organizational or "enterprise friendly" support can allow a nonprofit to build cash reserves, gain growth capital and invest in the people and systems that will enable it to work well for the longer term that service provision demands today. This kind of supportive funding signifies trust that nonprofit managers, and not funders, are in the best position to deploy their internal resource, and parallels the equity investments that for-profit investors make. It is the rare funder who possesses the deep knowledge of a specific nonprofit that can make this kind of determination. This principle suggests that funders limit or eliminate grant restrictions. It also calls funders to understand what their money can and cannot accomplish, both in its size and intent.

## **Conclusion**

The profiles indicate that there are many ways that funders can support the long term vitality of the nonprofits in order to better serve society. The advice of peers is instructive, and suggests that policies, staff and board interaction and the structure of grants must be aligned to help achieve these goals. Restrictions carry costs, add complexity and may not add enough value to be justified, especially where standardization and streamlining offer advantage and clarity of purpose and outcome. Through sharing of data, performance metrics and funding partnerships, costs can be minimized saving precious resources to strengthen the organization doing the work.

When money is more flexible and less restricted or categorical, it can support enterprise growth, stabilization or improvement. This type of funding calls for a new approach in grantmaking, for new measurements tied to both organizational and programmatic outcomes, and a new relationship between grantmaker and grant seekers. It requires

leaving the special and unique behind, as Andrea Levere cautioned at the *Capital Ideas* symposium, in favor of the scaled and more effective. In time, more sharing about how the role of nonprofit leader and grantmaker changes under this rubric, how board's respond and how each organization measures and celebrates success will help to encourage others to adopt this less restrictive and important source of growth, working and ultimately social capital. It is a road worth traveling.

## APPENDICES

### Appendix I - Funding Profiles

This is currently in PDF format. It will be provided in hard copy.

### Appendix II - Draft Funding Principles

## Post-Symposium Funding Principles to Enhance the Effectiveness of the Sector

### **Collective Approaches**

*(NB: Collective approaches denote activities that rely on cooperative action among funders that removes barriers and supports field-wide practices that enable nonprofits to succeed.)*

1. Minimize the transaction costs for grantees and funders of applying for and reporting on grants.
  - Standardize grant request formats, reporting, and stewardship methods to avoid the taxing costs associated with “special” requirements or idiosyncratic processes.
  - Do not invent special performance metrics for grantees. Use your grantees’ or commonly accepted sector-specific performance metrics when possible.
  - Share data and data platforms (e.g., common electronic reporting and information or trend analysis) to avoid repetition in information collection and assessment.
  - Adopt a “net grants” approach that recognizes and limits the time and therefore cost that grantees spend applying for, securing, and reporting on a grant to a very small proportion of the grant itself. This is called the *net grant principle*, where the smaller the grant, the simpler and cheaper the process should be for the applicant, since the actual award realized is “net” the cost of getting it. Remember this principle when saying “no” as well—the net grant is always negative, and must be paid for from other sources within the organization.
2. Actively pool resources when more funds are required to achieve results.
  - Match amount, type, and duration of funding to the ambition and life cycle of solutions being undertaken. If a grant or contract is not going to be adequate to cover costs, reduce the scope or help find other funders.
  - Employ existing pooling mechanisms where possible, resisting ad-hoc creations.
  - Do not create new layers of administration.
3. Reform the field’s overly complex and expensive accounting, regulatory, and contracting requirements.

- Advocate revising Financial Accounting Standards Board (FASB) accounting rules to make nonprofit financial statements management-friendly and comprehensible to a wider range of users.
  - Develop a policy outreach agenda to improve IRS rules including Form 990, the public support test, and tax deduction standards.
  - Require that accounting and auditing firms use a standard, organizational-friendly format in audits for grantees (within existing FASB rules).
  - Use meaningful financial and program metrics rather than facile ratios such as overhead rate. Draw on existing standard, industry, or issue-specific measures.
  - Advocate for full-cost recovery or value based pricing in government and foundation contracts with nonprofits.
  - Press for parity between nonprofits and for profits in basic government contracting and compensation rules.
4. Create the culture, knowledge, and methods necessary to enable nonprofits to succeed.
- Make finance part of grantmaking; educate key internal and external constituents on realities, appropriate tools, and vocabulary of nonprofit financial principles, management, and accounting.
  - Fund experiments without punishments if results falter or corrections are required.
  - Find ways to support networked, “supply chain” and social ecosystems–type approaches that advance entire fields of service and social impact.

### **Funder-Based Approaches**

*(NB: Funder-based approaches denote activities that individual funders can undertake alone.)*

1. Fund at the organizational rather than the programmatic level, even when your primary interest is in one program.
  - Recognize that the nonprofit is an enterprise or system, not a set of hermetic programs and discrete line items.
  - Limit or eliminate grant restrictions.
  - Fund to enhance organizational capacity and financial health by building reserves as well as offering growth capital and unrestricted support.
  - Understand what the amount of money your foundation can invest can actually enable the grantee to accomplish.
  - Do not confuse control with accountability. Avoid reliance on input or activity-based ratios (fundraising costs, overhead) to assess grantees’ effectiveness. Instead, use output metrics (outcome quality, change accomplished) and work to improve effectiveness over time.
2. Fund to meet the organization’s business needs and operating realities.
  - Develop with the nonprofit a common understanding of its underlying business and its financial model and associated funding needs.
  - Understand the state of organizational development and build capacity (i.e., systems, skills, metrics, and reliable routines).
  - Understand the nonprofit’s community and “industry” context and role so that funding reflects this reality.
  - Use these factors to determine grant size, structure, and intent as well as auxiliary services such as technical assistance.
3. Avoid frequent changes in funding priorities; signal exits or changes well ahead of time for grantees.
  - Keep requirements simple, consistent over time, and commensurate with grant size and intended impact. Publish them.
  - Avoid repeated changes in funding priorities and application and reporting requirements. Avoid “unfunded mandates”—i.e., extra reporting or compliance for no more money.
  - Share standards of reporting with other funders to maximize grantee efforts on improvement rather than simply on compliance.
  - Fund from the premise of trust or not at all; avoid making accountability rubrics and due diligence a substitute for a basic belief in the organization or its idea.
  - Signal far enough in advance for the nonprofit to be able to respond if you need to change or review priorities.
4. Understand when you are “building” and when you are “buying,” and fund accordingly.
  - Make sure you and your grantee know the difference between “buyer” and “builder” funding roles.

**Buyers:**

- Are you funding the grantee to continue its current, excellent services again this year? You are a buyer. Either pay for a unit of service or give general support, and refrain from requests for massive documentation.

**Builders:**

- Are you asking a grantee to do anything new—serve more, provide better quality, etc.? You are a builder, expanding or improving the “factory.” Make sure you and others are providing for the full costs of growth (expanded skills, systems, mistakes, etc.) on top of continuing to fund regular operations at existing levels over the period it takes to arrive at a new “steady state” of effectiveness. The grantee will need a combination of operating revenue and capital and “equity” investment commensurate with the size and ambition of the change envisioned.
- Never premise funding on pushing the grantee to do more or do it differently unless you are willing to be a “build funder” and will help develop, organize ongoing funding for, and stay with a grantee through the several years needed for this growth.
- Fund pilots and smaller initial ventures as proving grounds for larger action; understand and honor incremental growth and ongoing need for reinvestment.
- Be reliable. If you want to support growth, provide larger and longer investments. Match the investment to the job at hand: Consider longer-term investments to help the grantee gain traction and experience.
- Acknowledge that funding start-ups and growth activities require even higher levels of funding and support than might be expected.
- Prepare your own organization for the financial, policy, and attitudinal fortitude and alignment required to fund for the long term.

5. Use evidence-based performance, learning, and organizational health metrics to measure and report effectiveness.

- Embrace commonly accepted industry-specific metrics rather than ad hoc measures.
- Encourage joint agreement on both a theory of change and how to capture and reward the non-numeric performance elements.
- Fund self evaluation, candid learnings, and course corrections.

6. Small can be beautiful: make appropriately sized investments, and do not encourage growth for growth’s sake.

- Fund recognizing that nonprofits have an appropriate scale and business model.
- Enable small, high-performing organizations to stay small and receive consistent funding.
- Support the use of “sharing mechanisms” (e.g., back office operations, group purchasing programs, etc.) to achieve efficiencies.