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RE:FRAMING

Can Foundations Take the Long View Again?

By DENISE CARUSO

AS business leaders like Ted Turner, Bill Gates and George Soros have moved vast swaths of their private wealth into the philanthropic sector, market expertise has migrated there, too. As a result, foundation directors, trustees and advisers from corporate America have taken a stance that the return on charitable dollars should be tangible and measurable, and should drive capital flow in much the same way that earnings figures do in commerce.

But a small and increasingly vocal group of foundation leaders is challenging the benefits of this approach.

"In the 1980s and early 1990s, there was a huge push for private philanthropy to be more accountable and to spend more time being goal-driven," said Kathleen Enright, the executive director of Grantmakers for Effective Organizations, a Washington-based coalition of foundations that promotes ways to improve nonprofit results.

Advisers and trustees compelled foundations to redirect their unrestricted grants to more discrete, short-term projects — for example, distributing mosquito nets in malaria regions — that would deliver a measurable bang for the buck.

"The reason the nonprofit sector exists at all is because it can fund and invest in social issues that the for-profit market can't touch because they can't be measured," said Paul Shoemaker, a former Microsoft employee and entrepreneur who is now executive director of the Seattle affiliate of Social Venture Partners International, a philanthropic network. "The nonprofit 'market' is not designed to be efficient in that way. Yet we're applying the same efficiency metrics to both sectors."

As a consequence, when foundations switched to project-based accounting, they forced grantees to sacrifice long-term effectiveness for short-term efficiency, Ms. Enright said. Nonprofits could no longer afford to focus on important strategic activities like advocacy or working for social change, which require "deep resources and the ability to change tactics overnight if the situation demands it," she said.

In addition, critics say, project-based funding allows grantees to collect only a fraction of their real overhead costs. According to "In Search of Impact," a 2006 study of foundation grant-making practices from the Center for Effective Philanthropy, foundation chief executives will allow a nonprofit to add only 10 to 30 percent of direct project costs for overhead. Some refuse to provide any operational costs at all.

The financial strain knocks many promising nonprofits out of business.

"Everyone is managing against the perception that nonprofits are supposed to be low-cost and low-overhead," said Thomas Tierney, chairman and co-founder of the Bridgespan Group, a Boston-based consultancy and search firm for nonprofits that was founded at Bain & Company. The only way for nonprofits to increase their working capital is to take on more projects, which in turn keeps increasing the amount of capital they need — a "vicious cycle that perpetually starves them of capacity," Mr. Tierney said.

The issue is not a lack of charitable capital. In 2005, grant-making foundations distributed more than $36 billion on assets of $550 billion, up from grants of $1.94 billion on assets of just over $30 billion in 1975, according to the Foundation Center, an organization based in New York that maintains a comprehensive database on the philanthropic sector in the United States.

Based on its data, the Center for Effective Philanthropy concluded that the present situation was limiting the effectiveness of those charitable dollars. After surveying nearly 20,000 grantees of 163 foundations and interviewing 79 foundation chief executives and 26 leaders of nonprofits, it recommended that to maximize the impact on grant recipients, foundations "should make larger, longer-term operating grants" of unrestricted funds that can be used to support the organization and its overall mission, not just specific projects or programs.

Two other recent publications reached the same conclusion: the "General Operating Support Action Guide" for foundations, published by the Grantmakers group in July 2007; and "Daring to Lead 2006," a survey of nearly 2,000 nonprofit executives conducted by CompassPoint Nonprofit Services and the Eugene and Agnes E. Meyer Foundation.

Their findings echo the experiences of a handful of foundations at the vanguard of the movement to provide more operating support to charities over the last 10 years. They include the William and Flora Hewlett Foundation, the Edna McConnell Clark Foundation, the Philadelphia Foundation, the Whitman Institute and organizations like Social Venture Partners.

These grant makers have successfully shown that providing nonprofits with operating support "does not mean forking over tens of thousands of dollars and relinquishing expectations for results," the Grantmakers' report said.

Instead, they have built due diligence and accountability measures into their agreements that go much deeper than simple project budgets and reports.

The Edna McConnell Clark Foundation in New York, for example, has created a detailed system for evaluating results of general operating support grants to organizations that work to improve the lives of low-income youths.

David Hunter, the former director of assessment at the foundation, said in an interview published in the Grantmakers' report that agreements between the Clark foundation and its grantees include specific milestones that are clear indicators of progress. They include benefits for the youths who benefit from the nonprofit's charitable work, not just "process milestones for the organization."

Each of the three reports concluded that general operating support yielded better results for foundations and grantees alike, particularly as larger grants are offered over a longer period.

Yet in 2005, according to the Foundation Center, only 20 percent of grants from the largest private and community foundations were designated for general operating support. A majority of foundation leaders polled in the studies acknowledged that unrestricted operating funds were better and more effective for grantees. But they continue to focus their grant-making on project support, they said, because they prefer its clear-cut results and because their boards often mandate project support as a way to show a foundation's prominence in a specific funding area.

WHILE this may be good for a foundation's image, Ms. Enright said, it can turn nonprofits into glorified vendors that provide only the services the foundation requests, sapping the sector of both passion and innovation.

"The presumption is that the donor knows more about how to address a given problem than its grantees, and I think that's usually not a correct presumption," she said. "More operating support can shift the locus of action and ideas to the people who are closest to the problem."

Denise Caruso is executive director of the Hybrid Vigor Institute, which studies collaborative problem-solving. E-mail: dcaruso@nytimes.com.