

Breaking Down Walls to Build Up Nonprofits

R. Andrew Swinney 03 January 2011

Management consultant Peter F. Drucker famously taught us all to ask, “What business are you in?” The question was designed to prompt thinking beyond the simple surface answer (such as “book publishing”) to a deeper one (such as “providing information” or “creating entertainment” or “leading dialogue on important topics”). The deeper answers allowed corporations to break out of the confines of traditional thinking and to position themselves more broadly as their industries underwent technological or market changes.

We’re all redefining our roles these days. Billionaires now are tackling social change through “giving while living” philanthropy. Businesses know it is not enough to satisfy their customers and shareholders—they also need to be perceived as having a triple bottom line through which they actively contribute to the community in which they operate. Governments no longer can afford to be the sole providers of human service stability and social cohesion—they rely heavily on nonprofit partners to assist in that effort.

Rahul Bhardwaj, president and CEO of the Toronto Community Foundation, may have said it best in a recent

address in Brazil to the São Paulo Foundations Association. “We need to stop thinking of our sectors as walls, but rather as bridges,” Bhardwaj said. “If we can find ways to align our interests, to start by finding what we share rather than what we don’t, business will prosper all the more, the social sector will better serve more people, and government will improve the lives of its citizens.”

The Philadelphia Foundation straddles all three realms. As a community foundation, our purpose is to link those with financial resources with those who serve societal needs. That means we work both with the business world (companies, wealth managers and their clients) and the nonprofit sector. We invest the dollars provided to us, and from the resulting revenue we provide long-term funding for a wide range of programs—many of which government does not have the ability to support.

Given our cross-sector connections, it should come as no surprise that when we recently studied the nonprofit sector, we concluded that the financial fragility of nonprofits often is rooted in the business model under which they operate.

We found that too many nonprofits often make operational decisions based on insufficient financial data. This is fueled by a disproportionate focus on their missions, rather than focusing on their long-term market viability as organizations seeking to fulfill those missions. It’s the responsibility of nonprofits’ funders, board members and

the broader community to correct this imbalance if the nonprofits that they care about most—and that serve us all—are to survive.

The problem develops because the market forces that provide feedback in the business world generally don't do so for nonprofits. In economic downturns, businesses adjust production, pricing, marketing, and staffing based on demand for their products. They also use research and development to improve their efficiency, product quality, and competitiveness. Their shareholders have a financial interest in ensuring that necessary adjustments are made.

By contrast, a nonprofit's revenue, much of which is restricted, comes mainly from the voluntary contributions of individuals, foundations, and government, not from a customer buying a product or service. During economic downturns, demand for the "products" of nonprofits—especially in the case of social service organizations serving the most vulnerable—tends to increase even as funding diminishes.

Nonprofits' decisions about programs, staffing, and sustainability generally are not based on research about their comparative effectiveness or the viable alternatives because they cannot afford it, and funders rarely want to underwrite such evaluations. Given their tight budgets, nonprofits are unlikely to pay for research and development even in a good economy.

Moreover, the “shareholders” of nonprofits—the community at large as well as those who serve on nonprofit boards—are not necessarily direct investors and therefore may lack a direct financial stake in ensuring that necessary adjustments are made. And in a weak economy, nonprofits’ survival becomes even more dependent on their ability to appeal to a cadre of supporters who are committed to carrying out the mission. While these dedicated backers make valuable contributions with their dollars, when they restrict the use of those dollars, they limit the nonprofit’s ability to be flexible.

The business that nonprofits are in, though, is not just serving their specific immediate clientele or appealing to their donor base, but providing a needed service—arts programming, education, health care, food and shelter—to the wider community. To do that, they must continue to exist as entities. So as counterintuitive as it may seem, nonprofits must focus now—in the economically depressed short term—on their long-term fiscal health.

Specifically, nonprofits need to have frank discussions with donors about the crucial value of capitalization, and about avoiding slow starvation by investment in infrastructure and overhead. Nonprofits also must tell their supporters that they need unrestricted dollars as general operating support, funding day-to-day activities. Further, they need to get the word out that an established funding pipeline through planned giving programs is needed just as much as—if not more than—the

underwriting of new endeavors with naming rights.

Of course, those nonprofits whose revenue comes mostly through governmental contracts—in which the rates paid for their services are negotiated without regard for supply, demand and quality—face a much more complicated challenge. In such cases, data from “research and development” needs to be liberally shared with legislators, government executives and the public at large so that more realistic allocations are made. This process includes open dialogue about the actual costs of running vital nonprofits and, especially, the resulting societal savings through the essential services that these nonprofits provide.

Unpopular as it may be, taxpayers need to be educated that building reserves in the nonprofit sector also is a wise long-term financial investment. This sustains the very fabric of our community and the quality of life we enjoy. However you calculate it, for example, it is far more cost-effective to pay for successful programs that help at-risk youth than it is to pay for prisons and to compensate crime victims.

Whether we support nonprofits through stronger government support or donor and corporate dollars, we’re underwriting those organizations that teach our future workers, heal our illnesses, entertain and uplift us, support our natural areas, and especially those that care for the people who fall through the holes in our frequently

overburdened social services safety net.

The triple bottom line is a more viable region: one in which culture and recreation are enhanced, economic opportunities are advanced, healthy communities are built, and children, youth and families are strengthened.

And at the end of the day, isn't that the business we all are in?

R. Andrew Swinney is President of The Philadelphia Foundation. The Philadelphia Foundation's white paper *Nonprofit Fiscal Health and Sustainability* is available at its website, www.philafound.org.