President's Statement

An Invitation to Improve the Effectiveness of the Nonprofit Sector

This is an invitation to funders—both foundations and individual philanthropists—and to the nonprofit organizations they support to join together to improve the effectiveness of our work.

Some writers, myself included, talk of grants as "investments" in nonprofit organizations. The investment metaphor implies that a dollar spent to achieve our social, environmental, or other goals should go as far as possible toward advancing those goals. Pursuing the metaphor, I want to suggest that the sector would be better off if nonprofit capital markets—that is, the arenas in which the activities of funders and nonprofits are coordinated—functioned more effectively. This essay proposes that we work to overcome three different barriers to a more effective nonprofit sector: inadequate information about nonprofit organizations; inadequate information about the practices of funders; and insufficient coordination among funders trying to achieve similar goals.

Information that Funders Need About Nonprofit Organizations

In the business sector, capital markets provide information that facilitates transactions between investors and business organizations. In the nonprofit sector, funders trying to decide where to invest their grant dollars have no systematically reliable information about the quality and efficacy of nonprofits. They must rely on individualized, intuitive assessments of these organizations—not just with respect to startups, but even when considering investing in relatively mature organizations.

The fundamental problem is the lack of a "social" bottom-line equivalent of the financial returns of business organizations. Even if the nonprofit sector had counterparts to the Securities and Exchange Commission and the myriad analysts who assess the performance of business enterprises, nonprofit organizations simply do not produce much of the information about outcomes that savvy funders would want. In fields as diverse as education, the environment, and community development, it is often difficult to know whether grant-supported activities have any impact at all, let alone to measure the social return on investment.

It is relatively easy to track the outputs and costs of operations—for example, how many people were served at what cost per person. But the nonprofit sector needs more than this. We need to measure social outcomes, or at least the attainment of milestones necessary to produce those outcomes. Such metrics are as important for the nonprofit organizations themselves as they are for funders. While funders need the metrics to make intelligent investment decisions, the organizations need the same information to know what they are in fact delivering and to get the feedback necessary for continuous improvement.

The beginning of a solution lies at the sectoral level, among groups of organizations (e.g., elementary schools, workforce development programs) that aspire to similar outcomes. These organizations could articulate their core values and objectives and then work to develop common metrics. I don't mean to suggest that this is easy work. Even within a particular sector, many organizations have different, or differently weighted, objectives, and the development of common metrics may be complex and contentious. Moreover, data collection is often expensive and its analysis fraught with uncertainty. Nonetheless, it is only a slight exaggeration to say that, in the absence of this information, neither foundations nor the nonprofits they fund can know if they are effective or successful.

Information About Funders' Practices and Work

Information about outcomes must ultimately come from the organizations that do the real work of the nonprofit sector. However, the sector would also benefit enormously if funders captured and disseminated information about their own practices.

To be sure, organizations seeking information about potential funders have a valuable resource in The Foundation Center, which publishes a comprehensive database of foundation grant guidelines and procedures. But it is rare for foundations to go beyond this to make available information about the effectiveness of particular grantmaking strategies—information that would benefit other funders as well as the sector more broadly.

The problem is not just one of dissemination. The knowledge that exists within a foundation tends to be anecdotal and often resides only in the heads of staff members or in uncataloged documents in their files; for all practical purposes, this knowledge disappears when a program officer moves on. Imagine the value to the sector as a whole if foundations not only maintained such information for internal purposes but also made it publicly available. Relevant types of information include:

- Applied knowledge in the fields in which a foundation works (e.g., the lessons learned from comprehensive community initiatives);
- A foundation's experience with various grantmaking procedures and devices (e.g., approaches to due diligence and evaluation, "socially responsible" investment of their portfolios, and program-related investments); and
- The lessons learned from particular initiatives and grants.

Improving the nonprofit sector depends as much on learning from failures as on replicating successes. Barriers to the public acknowledgment of failure include the egos of foundation personnel and the potential harm to grantees and to funder-grantee relationships. If we can overcome the ego problems, however, we can probably figure out how to disseminate information without inappropriately casting aspersions on grantees.

Beyond Information, Toward Coordination

Let me turn to some matters that go beyond communication, to expanding the ways that funders could pool their resources to achieve common aims. A major function of capital markets in the private sector is to help coordinate and aggregate the investments of multiple investors—ranging from a handful in the case of venture capital to many thousands in publicly held companies. Equivalent philanthropic practices would include:

- Investing in funders' collaboratives;
- Investing in intermediary organizations that do regranting, fund social entrepreneurs, and manage portfolios of grants;
- Sharing the responsibilities of due diligence, so that potential investors in a common enterprise could accord a degree of deference to a lead funder with expertise in the subject; and
- Collaborating in developing management information systems and other methods of evaluation for similar grantee organizations.

Although there are real-world examples of each of these, their full potential is nowhere close to being realized. Barriers to collaboration include the desire for control or authorship—the "not invented here" syndrome—and an inflexible insistence that a grantee meet all of a funder's specific requirements when, inevitably, different funders will have somewhat different criteria. These barriers can be overcome over time through the mutual trust and give-and-take that result from collegial interaction.

Conclusion

For each of the problems described above, there are notable instances of effective solutions. For example, through its OASIS project, the Roberts Enterprise Development Fund is supporting the creation and dissemination of systems to track the outcomes of workforce development programs. The websites of the Annie E. Casey, Edna McConnell Clark, Robert Wood Johnson, and W. K. Kellogg foundations provide valuable information for others working in the same fields. There are also quite a few examples of collaboration among funders: just drawing on our own experience during the past year, The William and Flora Hewlett Foundation supported the OASIS project, engaged in joint ventures with the James Irvine, John D. and Catherine T. MacArthur, Andrew W. Mellon, and David and Lucile Packard foundations, and joined with other funders to create the Foundation Incubator in Silicon Valley.

Yet there is much more that could be done—with the potential for greatly increasing the nonprofit sector's impact on the social and environmental problems that confront this nation and the world beyond. We at the Hewlett Foundation are committed to improving our own practices and supporting others in each of the areas mentioned above. We welcome alliances with those who share our concerns and are undertaking similar efforts.*

Paul Brest
Summer 2001

*For an excellent, foundational discussion of the premises of this essay, see Jed Emerson, "The US Nonprofit Capital Market: An Introductory Overview of Investors, Instruments," in The REDF Box Set, Volume II: Investors' Perspectives, www.redf.org; Regina Herzlinger, "Can Public Trust in Nonprofits and Governments Be Restored?" *Harvard Business Review* 74 (1996): 97–107.