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Clara Miller is president and CEO of the [Nonprofit Finance Fund](#), a national leader in helping nonprofits strengthen their financial health and improve their capacity to serve their communities. This column is the first in a series appearing over the coming months in which leaders from our community examine the current social finance system. Here Clara sheds light on some of the problems organizations currently face, particularly as a result of trying to follow "best practices."



### Examining the Social Finance System

We've read about it in *The Economist*, the *Chronicle of Philanthropy* and *Fast Company*... Ford, Hewlett, Surdna and MacArthur have experimented with it... Google, Omidyar and Skoll may abandon it altogether... and philanthropic giants from Bill Gates to Bono may succeed in redirecting it. But every day, people on the front lines of social change -- those who do the work -- simply shrug and use their precious time and energy to work around it. What is "it"?

"It" is our system of social finance, a confusing patchwork of traditions, regulations, and superstitions that regulates and restricts the supply and use of money in the nonprofit sector. How can we actually make progress to improve it? At "Capital Ideas" a symposium co-presented for an overflow crowd last month by Nonprofit Finance Fund and Harvard's Hauser Center, there was no lack of ideas, including from government funders, and they are promising. Earlier this year, a Grantmakers for Effective Organizations listserv on "overhead rate" drew a long series of thoughtful, even passionate e-mails from funders (astounding even to me!)

The time seems right to make progress toward a better system. But as a foundation program officer remarked, "I get it in the abstract...but what do I do on Monday morning back at work? I can't quite connect our procedures to the problem, our board doesn't get it and nobody thinks it's urgent..." Let's listen in to what could be a typical conversation -- to see up close and personal how "best practice" among funders (at all levels) can make life more difficult for the folks doing the work...

### Desperately Seeking Sanity: Little Steps to Fix Finance for the Front Lines

The program officer welcomed Sister Rose Sullivan to her office, thrilled to be meeting one of her heroes -- a true activist. Sister Rose, the CEO of a leading national anti-poverty organization, was inspiring. She spoke passionately about her work, outlining progress made over 25 years, highlighting the ironies and triumphs of fighting poverty in the midst of plenty.

The program officer was sold. "We'd love to help," she said, and turned the conversation to financial due diligence. "I know your annual revenue is \$30 million. How does that break down?"

Sister Rose intoned a practiced response: "We have a total of fifty government contracts, from four levels of government -- 40 entities in 12 states and 34 municipalities. Most are renegotiated annually, but it's unpredictable. Almost always contract rules are in conflict among government entities."

"And that makes up about 70 percent of your revenue?"

"Yes, along with some earned income from developer's fees and loans receivable."

“And 15 percent of your revenue is in foundation and corporate grants?”

“Yes, we get about 100 grants a year, mostly restricted, typically for a specific project or purpose. Some funders like bricks and mortar, some restrict the grants to a program or a project, some to a neighborhood or geography. Some want to pay for blankets or food. Nobody funds maintenance or depreciation on our shelters!”

“What about the other 15 percent of revenue?”

“Well, it’s from other charitable giving: the dinner dance, the golf outing, bingo receipts, the car wash and our bi-annual direct mail campaign.”

The program officer was delighted, “That’s great -- your revenue is very diverse -- we love to see that!”

But Sister Rose didn’t seem to share the program officer’s enthusiasm. Even on the brink of victory, she appeared to have been overcome by exhaustion, murmuring almost as if in prayer, “I don’t know if I can do diverse revenue anymore...please, no more negotiations about contract conflicts... no more truckloads of donated crew socks ...no more ramshackle “free” buildings...no more long conversations about small grants... no more tap dancing around use and overhead restrictions...and no more bingo...please, no more bingo...”

The program officer stared, astounded. The last thing she wanted was to drive Sister Rose over the brink...she wanted to help!

No wonder the program officer was taken aback. All of her training, from her MPA to her days in management consulting to her work at the foundation, had taught her that revenue diversification was an example of “best practice.” Was it possible that the drive for diverse revenue, combined with of a whole range of other “best practices,” could actually do more harm than good?

The answer is yes. In this case, the blanket enthusiasm was for revenue diversity -- and Sister Rose had accepted it as received wisdom. But revenue diversity is neither inherently good nor bad. Some attain revenue diversity through new programs, adding complexity and cost; others just diversify their “customers,” adding net revenue while keeping programs focused.

In Sister Rose’s case -- as others -- being pushed to diversify revenue wasn’t the only “best practice” she had had to deal with. Building ownership...good or bad? She had been gifted a building with maintenance and management needs that far outweighed the cost of leasing a comparable space. Innovation...good or bad? She had been asked to create new programs in order to get some of her funding, which then didn’t account for the staff costs necessary to run the new programs. Rather than helping the organization, these actions had stretched capacity and, ironically, financial resources, to their limit. Low overhead...good or bad? With funder restrictions and pressure from charity rating systems, she cut overhead while management complexity soared, reducing management efficiency and burning out several CFOs.

We can do better. Nonprofit Finance Fund and a lengthening list of government, foundation and individual funders are looking for ways to improve both the way revenue flows into nonprofit “enterprises,” and the way nonprofits access and deploy capital for growth and operating needs. In the course of this series we will explore ways the field can move -- and is moving forward with this important work.

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