2001

Venture Philanthropy: The Changing Landscape

Morino Institute

venture philanthropy partners

investing in social change

Prepared by Community Wealth Ventures, Inc.

The Morino Institute, Venture Philanthropy Partners, Inc., and Community Wealth Ventures, Inc. have collaborated to produce a series of reports to explore and advance the emerging field of venture philanthropy.

The first report in this series, *Venture Philanthropy: Landscape and Expectations*, was produced in March 2000. This report, *Venture Philanthropy 2001: The Changing Landscape*, is the second in the series. Future reports will be published as the field of venture philanthropy continues to evolve and reveal additional lessons.

These reports have been produced to advance the understanding of venture philanthropy and to help in providing a strategic foundation for the work of Venture Philanthropy Partners. The mission of Venture Philanthropy Partners is to apply strategic investment management practices to build stronger, more effective, sustainable organizations serving children in the National Capital Region. Venture Philanthropy Partners will make its investments with two purposes in mind: first and foremost, to have a significant impact on the organizations in which it invests; and second, to learn how the venture philanthropy process can work most effectively so that knowledge can be shared with others nationally. Venture Philanthropy Partners was created by the Morino Institute, in partnership with Community Wealth Ventures, The Community Foundation for the National Capital Region, and in conjunction with a group of New Economy business leaders led by Raul Fernandez, Mario Morino and Mark Warner.

The Morino Institute, Venture Philanthropy Partners and Community Wealth Ventures would like to thank the organizations that have contributed to this report. Our hope is that the time they have spent sharing information and knowledge will benefit others involved in this field and increase the impact of venture philanthropy.

Please e-mail any comments, suggestions or thoughts on this report that would enrich the next version to: venturephilanthropy@communitywealth.com. Written suggestions may be sent to: Venture Philanthropy Report, Community Wealth Ventures, 733 15th Street, NW, Suite 600, Washington, D.C. 20005.

This report can be viewed online or downloaded at: www.venturephilanthropypartners.org.

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Introduction

After several years of robust intellectual ferment around the creation of venture philanthropy, its practice around the country has finally begun to move from design to execution. In so doing, the gap between the rhetoric surrounding venture philanthropy and its practice and performance on the ground has widened, calling into question whether venture philanthropy will be able to meet expectations of more effectively addressing social problems.

While such a gap does not diminish venture philanthropy's exciting promise, it does challenge those in the field to identify and understand it and to determine which capacities they must develop to close the gap. The responsibility of facing this task comes at a moment in time rich in learnings. The daunting challenge of this report is to capture and share at least some of those learnings, which we present in three main areas of focus:

1. *Venture Philanthropy Through a Wide Angle Lens.* This featured article sets the framework for the discussion highlighting the issues confronting the venture philanthropy movement in the United States.
2. Contributed Essays. This series of essays is written by individuals who have a wide range of experience in either venture philanthropy or high-end strategic investing, and who provide varied perspectives on the development and challenges facing the field.
3. Venture Philanthropy Organization Survey Results. This last section features an overview that highlights results of the survey as well as individual profiles of organizations surveyed for learning and comparative purposes.

The expression "venture philanthropy" entered the country's popular lexicon in 2000 with notable press coverage in *Time*, *Fortune*, and on web sites around the country. Articles proclaimed this new generosity might be the true legacy of the booming new American economy. While such coverage has raised awareness of venture philanthropy and created excitement about its potential, it has also muddied the popular understanding of what venture philanthropy is and what it hopes to achieve.

This approach to philanthropy borrows principles from the practice of venture capitalists in the business world. Venture philanthropy rests on the premise that the best investments require more than money: success requires talent, expertise, and strategic thinking. Moreover, like venture capitalists, venture philanthropists expect results and accountability from the organizations they support.

The research undertaken for this report and accompanying essays make clear that:

- Venture philanthropy funds have continued to proliferate across a wide spectrum, ranging from highly engaged grant-making to simple capital allocation without any additional strategic assistance. It is premature to claim proof of concept for venture philanthropy because relatively few investments have been made and the grant recipients simply do not have measurable results yet.
- Many of the funds are so new, and have so few staff, that they will be challenged to build the capacity of any other nonprofit organization until they build their own capacity.
- The majority of nonprofit organizations are inexperienced in and unprepared for absorbing the kinds of strategic management support that venture philanthropists are tying to their financial investments. As a result, most grant recipients underestimate what is expected of them, and their organizations risk significant strain in executing their end of the partnership.
- There is still very little agreement about or utilization of metrics for success. Most funds promise to develop these measures in the future.

The knowledge reported here from the various practitioners will offer those who are interested or engaged in the field a unique opportunity to learn from the experience of others. It is our hope that *Venture Philanthropy 2001: The Changing Landscape* brings some clarity to the discussion of venture philanthropy by providing a more lucid definition of the field and an exploration of its application, paving the way for future discussion and debate.

Venture Philanthropy Through A Wide Angle Lens

The view from the window of a fifth floor conference room on Columbus Avenue is of fog enveloping Boston's Hancock Tower, which seems to drift in and out of view. But the thinking inside the room is clear, sharp and focused. That's not surprising. Squeezed around a makeshift conference table are a handful of the smartest and most successful business leaders in America today. They are men and women who have fueled the engine of America's economic boom and lived at its warm, sweet center.

Jeff Swartz is the CEO of Timberland, which this day will announce its 16th straight quarter of record earnings, third quarter 2000 net income of $57.5 million and revenue growth from the same quarter in the previous year of 15.2 percent. He is joined by Ilene Jacobs, senior vice president of Fidelity Investments, Rosabeth Moss Kanter, the Harvard Business School professor and prolific author of books on world class business management, George Gendron, editor-in-chief of *Inc.* magazine which has documented the greatest decade of enterpreneurialism in American history, and Steve Woodsum of Summit Partners, a venture capital firm.

This group understands creating shareholder value, evaluating rates of return, building brand identity, and measuring results. Their collective expertise is in building the institutions that get successful products to market. In the new networked economy they are nothing if not well connected. Investment bankers are a phone call away. They e-mail from corporate jets. Presidential candidates visit their offices.

Today they collaborate on a venture backed by millions of dollars from technology titans like Cisco Systems, Compaq, Microsoft and AOL, as well as their own companies. But it's not a consumer product or fashion item for America's shopping malls. Nor is it a new software application or technology. It is neither business-to-business nor business-to-consumer. The challenge they are addressing is more formidable. It is the challenge of bringing a social program for America's youth to scale.

These are the trustees of the nonprofit organization City Year, whose mission is to build democracy through national service. The community service product City Year has developed is a powerful one, but it has reached only a few markets. Having raised and spent $200 million to expand youth service corps into 13 cities since being founded 10 years ago, they now grapple with the question of what capacity will be needed to go to scale. Implicit in their approach is the belief that adapting and applying the techniques of successful entrepreneurs can dramatically improve nonprofit service delivery.

They are not alone in their quest. Just a few blocks away, John Whitehead, former chairman of Goldman Sachs and former chair of the Federal Reserve Board in New York, advises the senior partners of Bain Consulting's Bridgespan Group about the kind of strategic assistance that will enable nonprofit organizations serving low-income youth and families to achieve "breakthrough" results. They are discussing a large New York foundation's decision not to engage in further system reform efforts, in favor of building capacity to create high-performing market leaders in the nonprofit sector. Venture capitalists take the same approach. Whitehead's experience on a dozen nonprofit boards led to admiration for their good intentions and a belief that they can do better. He has used his own resources and the talents of Harvard's faculty to build bridges from the old philanthropy to the new.

Similar scenes play out every week in hotels, conference centers and boardrooms across America. Whether the focus is charter schools, maternal and child health programs, workforce training, environmental protection, or other social issues, business leaders are paving a new path, and creating a new role for themselves in the process.

A few days before City Year's meeting in Boston, *Fortune* magazine convened a forum in Austin, Texas with Steve Kirsch, founder of Internet navigator Infoseek, Mort Meyerson, former CEO of EDS and Perot Systems, Ken Lay, CEO of Enron, Susan Dell of the Dell Foundation, and hundreds of others from Fortune 500 companies. They listened to Christine Letts, who wrote the seminal *Harvard Business Review* article on venture philanthropy, describe characteristics of successful venture philanthropy investments, emphasizing those in which the grant recipients were not weak organizations needing to be rescued, but strong organizations needing help to grow.

Letts advocated funding that was long-term, reliable, and not contingent on exact metrics. She described the relationships as distinct from "compliance relationships," in which the nonprofit partner feels it must jump through hoops to meet certain numbers, and instead is based on a venture funder's philosophy of "I will help you succeed." She recommended that funder and grant recipient work to establish metrics together in the course of their first year. Letts urged funders to recognize the distinction between scale and leverage and to focus on measuring whether an organization is leveraging more value, rather than trying to measure the degree to which it is growing to scale.

Just a few days after that, Sir James Lord, chairman of HSBC Bank, flew through the night from London to New York to address 200 people, each with a net worth of $45 million or more, on how venture capital practices can be applied to charitable giving for the purposes of making their philanthropy more effective.

Finally, that same month, Proxicom founder Raul Fernandez, philanthropist and civic leader Mario Morino, Jean Case of the Case Foundation, Virginia gubernatorial candidate Mark Warner, and nearly two dozen other investors held a series of meetings to review what may be the largest venture philanthropy fund yet launched, a $30-50 million fund to be spent exclusively in the greater Washington, D.C. region on behalf of youth. The Children's Learning Fund for the National Capital Region is Venture Philanthropy Partners' (VPP) first venture philanthropy fund and will make investments in organizations that seek to improve the lives of children through development, learning and education.

VPP's founders describe venture philanthropy as "the process of adapting strategic investment management practices to the nonprofit sector to build organizations able to generate high social rates of return on their investments. VPP provides strategic management assistance to leverage and augment its financial investments. In addition to gifts of equity—the investment—the givers also share their managerial and technological expertise, leverage their network of contacts, and help organizations empower themselves to achieve their missions instead of trying to redefine them."

PHILANTHROPY'S NEW ROLE

This report is not about City Year, Bain Consulting, Venture Philanthropy Partners or any one of the many exciting new initiatives being launched under the "venture philanthropy" rubric. But it is about the sea change they represent, the promise they hold, and the hurdles that must be overcome if their performance is to match that promise.

From Boston to Austin, from Northern Virginia to Northern California, entrepreneurs, philanthropists, technology millionaires and others are pulling philanthropy into the new millennium, holding it to higher standards and imbuing it with strategies, techniques and tools previously the private preserve of the venture capital world. In many cases, they are building upon the groundbreaking work of the field's earliest and most successful pioneers like the Roberts Enterprise Development Fund, Robin Hood Foundation, Ashoka, or Social Venture Partners. Old and new players alike bring value to the mix. Whether it is unique experience, relationships, or a new approach, philanthropy and our society are better for their efforts. Independent, but mutually supportive, like thousands of scientists who competed and collaborated to map the human genome, these business and philanthropic leaders contribute to an effort larger than themselves, seeking to crack philanthropy's code and create a new understanding of what's possible.

No longer content to be simply the philanthropic checkbooks that fund good works, they want to ensure effective design and skilled management as well. With a first-hand understanding of how capacity building strengthens an organization's ability to deliver service, these philanthropists know that money may be one way to build capacity, but strategic management assistance is another. Their approach responds to a specific diagnosis of a problem, perhaps best stated by Chris Letts, Alan Grossman and Bill Ryan in their book on high-performing nonprofits: "The biggest challenge many in the nonprofit sector face is sustaining or expanding successful programs…There is another way to look at sustained, large-scale impact — not as a function of program design alone, but of program design and organizational performance together. Behind every effective program, and especially every sustained effective program, is an organization that performs well. The challenge of large-scale impact can be reformulated as the challenge of helping more nonprofits perform better."[1]

[1] *High Performance Nonprofits: Managing Upstream for Greater Impact*, Letts, Christine M., William P. Ryan, Allen Grossman, © 1999 John Wiley & Sons, New York, NY

The authors also report, "Current attitudes about organizational capacity are far too narrow to support investment in organizational performance. Most frequently, nonprofit funders tend to see any investment in organizations as overhead, deadweight costs that take money away from program beneficiaries...We need support for the proposition that organizational capacity, especially the adaptive capacity needed to deliver on mission, is a much more vital resource for the nonprofit sector."

THE STAKES ARE HIGH

You could earn enough frequent flyer miles to see the pyramids by flying to all of the conferences that have been called in the name of venture philanthropy in the last year. There is a simple reason for this groundswell of activity: the stakes are enormous. Billions of dollars in philanthropic giving could be influenced by these early efforts. Against the backdrop of a decade of unprecedented prosperity, new foundations are being established at a rapid pace and their founders are young enough to be actively engaged. With a lot of money but little free time, many are looking for shortcuts and hoping to learn from those who have gone before them. Philanthropy may be on the cusp of the greatest revolution in the nonprofit sector since Congress granted tax-exempt status in 1954.

Only two things can be said for sure about venture philanthropy. First, it is still in its earliest stages. Notwithstanding the attention it is receiving, the concept remains essentially unproven. It's too soon to say whether it is better or worse than more traditional philanthropic approaches. Likely it is neither, but rather a new model getting ready to take its place alongside other existing models. Whether it deserves to gain prominence will depend upon whether those who espouse it practice what they preach—whether they allocate time and resources to build capacity in ways that go beyond traditional grant-making.

Second, this is more than a passing trend in philanthropic giving. It is a transformation wrought by forces as large as the planets. The changing role and expectations of government, the powerful and sustained growth of the new economy, the deepening divide between the wealthiest and the poorest, and the slow but inexorable maturation of the nonprofit sector have combined to bring philanthropy to this new place. As Peter Drucker writes: "Forty years ago when I first began to work with nonprofit institutions they were generally seen as marginal to an American society dominated by government and big business respectively. In fact, the nonprofits themselves by and large shared this view. We then believed that government could and should discharge all major social tasks, and that the role of the nonprofits, if any, was to supplement government programs or to add special flourishes to them. Today we know better. Today, we know that the nonprofit institutions are central to American society and are indeed its most distinguishing feature."[2]

THIS YEAR'S REPORT

Venture philanthropy is ubiquitous, spreading like kudzu, but with dozens of different species and varieties. It is a term loosely applied to almost every charitable effort begun during the last three years.

This report is organized around four questions.

1) What is venture philanthropy?
2) How is it being conducted?
3) What is its impact?
4) What have we learned?

Our extensive research, building on last year's report, enables us to answer these four questions more comprehensively than they have been answered to date. But comprehensive is not the same as complete. The rapidly evolving nature of the field makes complete and final answers impossible and unwise. There will surely be efforts too new to have included here or which limitations of space may have precluded this year. Candidly, some worthy philanthropic programs may be excluded because of judgment calls about whether they fit even the broadest definition of venture philanthropy. That doesn't diminish their worth or our admiration for them. It just means they are outside the scope of this particular report.

Finally, we want to be clear about the purpose of this report, which is to contribute to advancing the understanding of the field of venture philanthropy. That can best be done through honest appraisal of what works and what doesn't, what obstacles still

[2] *Managing the Non-Profit Organization,* Drucker, Peter F., © 1990 HarperCollins, New York, NY, page xiii

exist and what new issues have arisen that merit further attention. This report seeks neither to praise nor to blame, but rather to bring as much light as possible to bear on new developments so that readers can draw their own conclusions. Many of our most talented philanthropic and nonprofit leaders labor in a sector that does not have a field-building infrastructure to help move it forward; that will surely be part of all of our work in the future. We have also sought to make the report more fully three-dimensional by adding a diverse mix of voices and opinions through the contributed essays written by practitioners with expertise in this and related fields.

That said, let's switch to a zoom lens for a closer look.

What is Venture Philanthropy?

WIDE SPECTRUM – MANY MODELS — There is a wide difference of opinion about when and where the term "venture philanthropy" deserves to be applied. As the Edna McConnell Clark Foundation explained in replying to our survey, "The term (venture philanthropy) has lacked definition from the beginning, and it seems only to be getting more confusing. An overly precise sounding lexicon appears to be masking an enormous degree of ambiguity and need for learning. This has resulted in a great degree of uncertainty as to what comprises the field."

Rather than engaging in the unproductive task of judging competing claims, it might be more fruitful to acknowledge that venture philanthropy has developed across a wide spectrum with a variety of different models. These range from multi-donor funds that adhere closely to the philosophies and practices of venture capitalists, to the foundations of wealthy individuals that, while new, actually operate in a fashion more similar to traditional grant-makers. They range from hands-off grant-making to high levels of donor engagement that include, in a few instances, taking seats on the board of the nonprofit being funded. Essentially the models fall into three broad categories:

<u>Venture-generated philanthropic funds.</u> In this model, the resources being distributed from various funds or foundations were contributed from successful venture capital efforts. However, these philanthropic funds are not necessarily being disbursed or invested according to the principles that a venture capitalist would follow, which include a primary focus on strong leadership and commitment to providing strategic management assistance.

<u>Venture-influenced philanthropic funds.</u> This philanthropy is influenced by the success of venture capital practices and reflects at least some of the characteristics of venture capital. These include taking risk, measuring outcomes, and paying extra attention to organizational leadership. But these funds typically lack a significant strategic management assistance effort as well as the staff capacity to provide one.

<u>Venture-parallel philanthropic funds.</u> These are funds whose approach to philanthropy most closely parallels the behavior of venture capitalists, especially the high level of engagement reflected in matching financial investment with strategic management assistance. As in the case of Robin Hood Foundation, Entrepreneurs Fund, Roberts Enterprise Development Fund and Venture Philanthropy Partners, these funds anticipate making relatively fewer but larger investments and usually have larger staffs available to provide management assistance and capacity building.

This spectrum also suggests that there may be opportunities for more partnerships between venture philanthropy organizations, as well as between venture philanthropy organizations and foundations—partnerships in which the venture philanthropy organization works with nonprofits to build their capacity, but a foundation steps in to fund the expanded programs and works to maintain funding for the enhanced capacity.

FUNDS TO STRATEGIC MANAGEMENT RATIO — One clear metric likely to emerge for these funds is the ratio of dollars invested directly in a grant recipient to the total value invested in that grant recipient, including strategic management assistance. The smaller the invested funds to strategic management ratio, the closer the fund will be positioned to the venture-parallel end of the spectrum.

While all of these efforts are likely to have a positive impact on the communities they serve, the venture-parallel philanthropic funds that combine strategic management assistance with financial support are more specifically designed and structured to address the capacity issues that have been obstacles to successful programs getting to scale.

PROLIFERATION OF NEW FUNDS — Last year's venture philanthropy landscape report stated our definition of "a social venture fund" (a multi-donor fund specifically created to address social issues that utilizes venture capital practices—as delineated in Chris Letts' *Harvard Business Review* article—to maximize investor value and impact) while characterizing the venture philanthropy field as the "Wild West." This year the landscape is even wilder, with new funds proliferating and the term being ever more loosely applied to a diverse range of new and philanthropic activities.

Three-quarters of the nearly 40 funds we surveyed came into existence since January 1, 1999. Some are replications of the Entrepreneurs Foundation first created in Palo Alto. Many are affiliated with Social Venture Partners, originally established in Seattle and now taking root in nearly a dozen cities. Others range from The Glimmer of Hope Foundation created by Philip and Donna Berber when he sold his company, CyberCorps, to Charles Schwab and set aside $100 million to save lives in the Horn of Africa, to Japonica Intersectoral Investment Bank.

There is an undercurrent of tension between those funds that operate in strict adherence to and parallel to venture capital practices and those that don't, but still bask in the nomenclature. That tension is increasingly being given voice in "off-the-record" comments. In an on-the-record exception, the Flatiron Foundation stated in responding to our survey: "It appears that more people are using the language of the for-profit sector to make foundation activities seem sexy. Relatively few are truly questioning and exploring what it means to be differently engaged from conventional philanthropy and to reward organizations that demonstrate the best performance, not simply the most interesting people."

AWAKENED PRESS INTEREST — This proliferation of new funds is related to the awakening of the first popular press interest in venture philanthropy. Previous coverage was limited to philanthropic journals and trade publications. In July of 2000, *Time* magazine's cover story on the "new philanthropists" focused on the "multi-millionaires of the technology boom." It explained that "many of today's tech millionaires and billionaires are applying to philanthropy the lessons they have learned as entrepreneurs...One solution has been the founding of venture philanthropies which use the same aggressive methods as venture capital firms, whose money typically comes with technological expertise and experience at running lean, efficient organizations. This new breed of philanthropist scrutinizes each charitable cause like a potential business investment, seeking maximum return in terms of social impact — for example, by counting the number of children taught to read or the number inoculated against malaria."

Likewise, in May of 2000, *Forbes* magazine's cover story on Pierre Omidyar was headlined "The Radical Philanthropist" and described him "seeding a small number of causes in a style that has become known as venture philanthropy. The Omidyars will give more money to charities that follow solid business plans and meet the Omidyars' benchmarks..."

Both stories posit and perpetuate the implication, unfairly some would argue, that the new philanthropists are interested in results while the traditional philanthropists, often represented by the larger national foundations, are not. But even many leaders in the venture philanthropy field dispute this. Paul Shoemaker, who runs Social Venture Partners, explained, "I don't think venture philanthropy's focus on 'outcomes' is at all unique to venture philanthropy. Hell, that's the United Way in spades the last few years. The main thing that I think is truly unique is the level of engagement and the type of relationship between funder and fundee (and its focus on capacity building over a sustained period)." And, Shoemaker reminds, "By the way, arguing about what is 'unique' about venture philanthropy is no more useful or clarifying than arguing about old versus new. It says nothing about what is and isn't effective."

This increased press coverage, also including *New York Magazine*'s cover story on the Robin Hood Foundation, and numerous other articles, is a significant change that has succeeded in spreading awareness of the concept beyond a handful of early practitioners. Ironically the press coverage exacerbates the ill-defined nature of venture philanthropy and likely fosters further confusion.

How is Venture Philanthropy Being Conducted?

FOCUS — Many of the new funds recognize the need to focus their grants in a specific field. Nearly 50 percent of the funds surveyed invest almost exclusively in programs for youth or education. About one-quarter of the funds focus on job training or technology-oriented organizations. In many cases this may stem from the kind of belief expressed by Social Venture Partners that "venture funds must truly understand the business they are in and build people and infrastructure to support that business. Versus a traditional foundation, grant-making is a much smaller proportion of the fund's work and added-value."

Some venture philanthropists are contemplating what might be called "sector investments." As Gary Jonas, Managing Partner of Venture Philanthropy Partners, explains: "In many cities there are a variety of organizations working in the same substantive arena, with common needs that no one is large enough to fill and where consolidation does not make sense. For example, mentoring services: In the greater Washington, D.C. area, there are over 200 organizations that run mentoring programs for young children. All face the common challenge of doing due diligence on potential mentors and training the mentor to do mentoring. If a central service was funded that did the due diligence quickly and efficiently and then trained mentors as a service to the organizations, tremendous quality and quantity improvement could result."

STRATEGIC MANAGEMENT ASSISTANCE VARIES WIDELY — The scope and scale of strategic management assistance to grant recipients varies widely among venture philanthropy funds from intensive and highly engaged, to token and immaterial. There is no generally accepted standard, agreement or guidance on the most effective balance between financial investment and management support. Over half of the funds surveyed had two or fewer full-time employees, making it unlikely if not impossible that they would be able to provide material assistance beyond the financial. This is where the gap between rhetoric and practice is illuminated most sharply. If such assistance were considered a firm criterion, many so-called "venture philanthropy funds" would not fit the definition of venture philanthropy used by many of the funds in this report.

NO STANDARD SCREENING MODEL — Our research revealed that no standard model for screening potential grant recipients has emerged. Some funds have an open application process while others pick their investments based on their own landscaping of the field. Most funds, however, agree on certain criteria, such as the need for strong leadership (although invariably that term is undefined), the need for an entrepreneurial culture, and capacity to scale. It might be instructive to pay special attention to the suggestions that came from the Entrepreneurs' Foundation since it was created by veteran venture capitalists at the Mayfield Fund: "1. Look for nonprofits with staff that cross both sectors: nonprofit as well as for-profit. Venture philanthropy truly is the marriage of both worlds, and to be effective one must have had experience in each. 2. Select nonprofits that have both the capabilities to grow to scale (strong management/leadership) and understand and embrace this new working relationship with a funder. 3. Be prepared to address the dysfunctional capital market of the nonprofit sector."

VENTURE PHILANTHROPY FUNDS LACK THEIR OWN CAPACITY — Unlike venture capital firms, very few principals or experienced entrepreneurs are involved in providing the strategic management advice contemplated in venture philanthropy. Ironically, many venture philanthropy funds have not yet built their own capacity to provide the strategic management and technical assistance that is implied or promised. As noted above, 20 of the funds we surveyed had two or fewer staff. This often consists of an executive director and a part-time employee. Given the degree to which their time is consumed with the responsibilities of raising funds and managing their own operations, it's difficult to see how they would be able to provide quality management assistance to others. In many cases, those responsible for "applying venture capital practices to philanthropy" have not had experience applying venture capital principles in the private sector in the building of a successful business.

Many of the Social Venture Partners model organizations are upset with the lack of participation beyond money they are getting from their partners. As Austin Social Partners told us: "The disconnect between the needs of the organizations and the fact that some partners perceive the volunteer projects as hobbies is the toughest challenge for the successful engagement of these projects."

New Profit, Inc. confirmed that "venture philanthropy funds should not underestimate the demand and need for consulting services and portfolio management support needed by organizations. Venture philanthropy or high-engagement philanthropy requires deep intellectual capital resources and capabilities."

Finally, the Robin Hood Foundation explained: "Venture philanthropy, or engaged grant-making, requires significant investments of time and energy from the foundation staff or other service providers. For some foundations this will mean changing the staffing structure or making much larger grants to cover the cost of hiring people to provide services. Providing this kind of assistance requires patience and flexibility which must be built into the cost structure."

Venture Philanthropy Partners, working with McKinsey and Company, is preparing a review of 10 case studies in capacity building that will be shared with others in the field in 2001. That effort, among others, should help the field agree on a common definition of capacity building.

NONPROFITS ARE NOT PREPARED TO ABSORB STRATEGIC MANAGEMENT SUPPORT — Likewise, the majority of nonprofit organizations are inexperienced in and unprepared for absorbing the kinds of strategic management support that venture philanthropists are tying to their financial investments. As a result, most underestimate what is expected of them, and their organizations risk significant strain in executing their end of the partnership.

Capacity to grow was one of the most oft-stated impediments to the process. Along with this, a couple of the stronger venture philanthropy firms mentioned communication with the nonprofit grant recipient as the most important issue learned; both venture philanthropy firm and grant recipient must be in agreement. "Even with sufficient nonprofit management expertise, developing truly honest, open relationships between the fund and the organization's management has been extremely challenging," according to the Roberts Enterprise Development Fund.

CAPACITY BUILDING IS UNDEFINED — While much of the focus of venture philanthropy is on "capacity building," this term has not been defined by either the new venture philanthropists or the nonprofits who represent potential investment recipients, and may well mean something different to each of them.

What is Venture Philanthropy's Impact?

TOO EARLY FOR PROOF OF CONCEPT — Notwithstanding the promise held by the growth in venture philanthropy and the growing support it enjoys among donors, it remains too early to demonstrate that venture philanthropy results in more effective outcomes or more powerful social change in ways that distinguish it from traditional philanthropy. Many funds have not made any investments yet at all. Most of those that have made investments did so in only the past 12-18 months. Their grant recipients are still in the process of spending the money they received and building their capacity. Even if the venture philanthropy funds had tools for measuring impact, which most of them don't, there would be little in the way of results or impact to measure yet.

FEW METHODS FOR MEASURING OUTCOMES — Despite very strong expressions of interest in measuring outcomes and "return on investment," very few of the funds have established concrete methods for doing this. Because the desired social returns will often not accrue for several years, venture philanthropists are increasingly establishing benchmarks to measure interim progress. For many nonprofits this introduces a new challenge to their operations. Most venture philanthropy funds talk about predetermined benchmarks, rather than specific goals like financial return. A few mention strategy, capacity, program, and organizational development as goals. The Roberts Enterprise Development Fund and New Profit have led attempts to develop a process for evaluating performance (the Balanced Scorecard Measurement tool in the case of New Profit). Many hope this will come in time. As the Great Bay Foundation for Social Entrepreneurship put it, "progress will be made in developing straightforward models of metrics that will be tools that grantees and funders can use to assess the success of grant programs and individual grants."

What Else Have We Learned?

NONPROFITS ARE CONDITIONED TO INCREMENTAL GROWTH — There is a disconnect between the incremental growth that severe resource constraints have conditioned nonprofits to expect and accept, and the scalability that venture philanthropists are often seeking. This is symptomatic of the nonprofit field, as evidenced by a passive approach to growth rather than an ambitious and proactive approach. Either very little thought has been given to where the organizations could be headed, or anticipated growth was incremental with little expectation that it would ever be commensurate with the size and scope of the problems being addressed.

KNOWLEDGE CAPTURE IS SPORADIC — Efforts to capture and disseminate knowledge from venture philanthropy practices are sporadic. Besides this series of reports, only the major players, like Roberts Enterprise Development Fund, have made a concerted effort to communicate learnings. Nonetheless, most firms acknowledge the need. There are "too few precedents and too few learning partners," the Edna McConnell Clark Foundation told us.

The Robin Hood Foundation expressed hope that "more groups who have been practicing venture philanthropy or engaged grant-making will be able to share their experience with many other foundations that are starting to adopt this engaged model."

CONCLUSION

The response to our survey by the New Schools Venture Fund provides a good summary of what we found: "There is much more rhetoric and hype in the field of venture philanthropy. Many very different models for venture philanthropy exist without either a common definition or a clear differentiation between them. Hopefully in the coming year, venture philanthropy will begin to mature and the level of discourse will move into more substantive discussions of where it makes sense, what it really is, how it can be done well, what the risks are and where it doesn't work."

Venture philanthropy reflects an awesome ambition, one that is equal to the magnitude of the social problems it seeks to address. Reforming education, more effective job-training, and environmental protection are just a few of the formidable challenges venture philanthropy funds seek to undertake. Their success will depend in part upon the degree to which they adapt the venture capitalists' tools and strategies to the tasks at hand. Gandhi said, "You must become the change you seek in the world." Venture philanthropy funds that seek to build the capacity of other nonprofits must build their own first.

No matter how much philanthropy changes, one constant will remain: the dedication of extraordinary people in nonprofit organizations and foundations who put their careers and reputations on the line to solve problems that seem unpopular and often intractable. The future of philanthropy lies in neither a clean break with the past nor a stubborn reluctance to change. In philanthropy, as in most changes in society, the new and the established must work constructively, and respectfully, together.

Contributed Essays on Venture Philanthropy

Because venture philanthropy is an emerging discipline, its practitioners hold a wide variety of viewpoints on virtually every aspect of the practice: the application of engaged grant-making, grant recipient selection, the best means of providing strategic management assistance, and the definition of outcomes and measures. For some, venture philanthropy represents a challenge to a number of established funding institutions and practices, while for others it works best in augmenting existing funding mechanisms. To advance the dialogue on this topic, we asked a few of the field's leaders and foremost practitioners to write about venture philanthropy and the challenges that they have faced.

Each of these individuals is exceptionally busy working to create solutions that address some of society's most vexing problems, and we are grateful for their willingness to take time to share their insights to advance this dialogue.

These essays follow:

- *Institution and Field Building at The Edna McConnell Clark Foundation*, by Michael Bailin
- *SVP Seattle: Venture Philanthropy in Evolution*, by Paul Brainerd
- *A Commitment to Accountability: The Coming Challenge to Venture Philanthropy*, by Jed Emerson
- *Venture Capital's Lessons for Venture Philanthropy*, by David Hodgson
- *Lessons Learned at New Profit, Inc.*, by Vanessa Kirsch
- *Venture Philanthropy: Strategic Investments for Social Progress*, by Mario Morino

Institution and Field Building at The Edna McConnell Clark Foundation

Michael Bailin

Michael Bailin was appointed president of The Edna McConnell Clark Foundation in February 1996. Mr. Bailin was the president and chief executive officer of Public/Private Ventures (P/PV), a nationally recognized nonprofit organization dedicated to improving opportunities for young people in poor communities. Before founding P/PV in 1977, Mr. Bailin worked as a consultant in the Ford Foundation and was the deputy director and counsel of the South Street Seaport Museum in New York City. He also practiced law and taught at both Dartmouth and Franconia colleges in New Hampshire.

The Edna McConnell Clark Foundation has a three-decade history of grant-making intended to improve the lives of poor and disadvantaged people. Most of this work built upon a theory of change that focused on reforming public sector systems—including criminal justice, schools and child protective services.

As we have reviewed this work in recent years, we've drawn some uncomfortable conclusions. These include the view that large public systems are slow to reform, if not inherently intractable; that the resources available to the foundation to fund such reforms are disproportionately small in relation to the task of engendering fundamental and substantial changes; that whatever changes do happen are extremely difficult to measure; and that even if measurable and important changes are made in such systems, the likelihood that they will be sustained beyond the foundation's involvement is minimal due to the large number of forces (political, social, economic) that can overwhelm and wash them out at any moment.

This analysis has led us to the decision not to engage in further system reform efforts.

We have also reviewed the foundation's practice of organizing its work in up to five programs at any given time. While this has the virtue of allowing us to address a wider range of social issues, it has the drawback of reducing the resources that we can use to address any specific issue. And we have come to believe that spreading our limited resources over multiple program areas means that our effectiveness in any given area is too severely constrained.

With these thoughts in mind, we have reached some fundamental decisions—in effect, developed a new theory of change for our grant-making, which we currently refer to as Institution and Field Building. While each element in itself deserves extensive discussion, for present purposes they are outlined as bullets:

- The foundation will concentrate its future grant-making on a single, broad area: youth development. We will focus specifically on services to children and young adults between the ages of nine and 24 living in poor and underserved communities. Such services are intended to promote the successful transition of young people through their teenage years and into adulthood with prospects for self-sufficient, satisfying, and meaningful lives.
- We will devote the bulk of our resources toward investing in the organizational growth of nonprofit youth-serving institutions that have demonstrated their effectiveness and are at a stage of their organizational development suitable to undertake significant growth.
- We will make larger grants and longer grants than we used to, and will do so to support the growth plans of such youth-serving organizations. With each grantee organization we will negotiate a growth plan against which we will invest; and as part of this process we will work with each grantee to specify the outcomes for young people (and the indicators to assess them) for which the organization holds itself accountable.
- The foundation will define its success by virtue of the success of its grantees in meeting the milestones called for in their growth plans, and the achievement of the desired outcomes for young people that are the core work of each organization.

- We see our grantees as partners with us in this work, and in addition to making grants we will provide substantial and ongoing non-financial support to our partners in order to maximize the likelihood of success.
- From the very beginning, we will work to assure the sustainability of the organizations in which we invest beyond the date of our financial commitment to them.
- Finally, we will search for ways in which we can bring together organizations working in the field of youth development to exchange information, share experiences, and perhaps even pool resources. And we will be alert to opportunities for strategic grant-making in organizations other than those providing direct services that will further these possibilities, so as to promote conditions that enhance the constructive impact of the youth development field on the lives of young people.
- In the end, we will hold ourselves accountable for making a substantial contribution to the welfare of a large number of young people—and for documenting these efforts in measurable terms. Though less measurable, our goals will also include identifying investments and undertaking activities that will strengthen the field of youth development, and thereby indirectly contribute to good outcomes for young people far beyond those touched by the organizations in which we directly invest.

While to some people these elements can be construed as amounting to a "venture philanthropy" approach to grant-making, we don't find that term particularly well-suited to convey our intentions. The term "venture philanthropy" has not been defined in a widely shared way, and under any definition, it carries substantial "freight" from its origins in the commercial sector. We do not wish to burden our work with notions like "efficiency" as unquestioned virtue or "value creation" too narrowly construed.

We are about six months into the process of designing and implementing this new approach. We hope to engage in extended conversations with others who are attempting similar projects, including "venture philanthropists." We have learned a tremendous amount from our early efforts—but are daunted by how much more we have to learn.

For now, we have set ourselves five objectives:

- Improving outcomes for young people living in poor and underserved communities;
- Success in building and enhancing the effectiveness of the field of youth development;
- Achieving higher social return on the foundation's grants (i.e., better bang for the buck);
- Developing an alternative way of doing philanthropy that is resolutely focused on achieving demonstrable outcomes and strengthening the nonprofit sector; and
- Accountability and transparency in our own philanthropic practice.

We will share what we learn about this work as we learn it.

SVP Seattle: Venture Philanthropy in Evolution

Paul Brainerd

Paul Brainerd is the founding partner in Social Venture Partners and the founder and president of the Brainerd Foundation, which is dedicated to protecting the environmental quality of the Pacific Northwest. Prior to starting his foundation, Mr. Brainerd founded Aldus Corporation and served as its president until 1994 when Aldus merged with Adobe Systems, Inc. Mr. Brainerd also volunteers his time to a number of non-profit boards and community initiatives within the Pacific Northwest.

In June of 1997, several of us in Seattle had an idea for a more engaged form of "giving back" that was modeled after venture capital concepts. Like other entrepreneurs, we had an idea, a sense that there was a "market," and lots of energy to make it happen. As a result, Version 1.0 of Social Venture Partners was launched.

Four years later we can report the idea is working; there is indeed a "market" for new, more engaged ways to give, and we are making a positive difference in our community. We have attracted more than 280 partners who have learned a great deal about our community's needs, their passions, and how they might best give of their time, money, and expertise.

Version 1.0 (excuse us for being software folks!) became SVP v2.0 and then SVP v3.0 as we applied the model and grew the organization each year. Think of us as passing from infancy to pubescence, if you will. We are young enough to have lots more to learn, but we have learned a few lessons along the way that are worth sharing:

- The venture capital metaphor is a useful one. There is no IPO, equity or cash-out, but the rest—a closely-engaged relationship with investees, a focus on capacity building for the long-term, measurement of progress against goals, an integration of human as well as financial capital, and a focus on the success of a portfolio of investments—has proven to have concrete applicability.
- Quite unintentionally, the SVP model has spread across the United States. SVP groups have formed in nine additional cities with another three likely to start in 2001. The new SVPs sprouting up around the country are not a result of our initiative, but rather a result of the initiative of individuals from other cities who like the model and want to make it happen locally. Don't think of it as a McDonald's franchise but rather as a loose confederation of SVPs driven very much from within each community, bound together by some core principles.
- It seems that the common bond is about a desire to be engaged in and directly connected to one's philanthropy; a need to see not just one's financial resources, but business and life experiences brought into play; a connection to the venture capital metaphor; and most importantly, a sense of wanting to do this with peers. The last point responds to a very old human motive—the need to build and be part of a community, to learn from others, and to find a sense of connectedness in small groups working with others that have a common purpose. Perhaps that is "old philanthropy" updated for a new generation.
- Not all venture philanthropy models are multi-donor (nor should they be), but ours is. Not only does that enable us to have a wide range of partners' skills and talents to offer to our investees, it also creates a strong community of engaged, mutually-reinforcing philanthropists. That sense of community and connectedness was not as obvious in SVP v1.0 and v2.0 as it is today in v3.0. In fact, our emerging questions about SVP v4.0 center primarily on that "community" and what SVP should do to optimize its collective potential. In our case, SVP may not be just venture philanthropy and philanthropic education, but also an incubator or space for new social ventures. SVP may be a place where people can dream, find others to work with, and make change happen.
- In doing our SVP v3.0 planning, we realized that the founders of SVP and the partners who helped develop the organization had specific values that governed the early growth and success of the organization. These were largely unwritten and communicated informally. As the organization grew, we determined that these values and principles needed to be documented and shared. We hope that by sharing these values, all partners will be empowered to further the mission of SVP, a subtle, yet vital, step in our evolution that will ground us as we move into SVP v4.0 and beyond.

What are the implications of all this for other philanthropic organizations and the nonprofit sector? Time will tell, and as yet little can be said conclusively. What can be said is there remain many questions, concerns, and misconceptions regarding venture philanthropy.

As a result, we have a collective responsibility for creating dialogues with the rest of the philanthropic sector. We need to move the discussion away from "old" versus "new" philanthropy and toward what works, what is being learned, and what creates real value in the sector.

As Mario Morino put it, venture philanthropy is "a way, not the way." This advice helps us focus on the kinds of organizations and situations where the model is most applicable and creates incremental value. In much the same way that venture capitalists and banks coexist in the for-profit sector, so should venture philanthropists and traditional funding sources coexist and understand where each adds the most value to the nonprofit sector.

As for the nonprofits themselves, we think there are a few implications for them as well. Building these relationships takes considerable time and effort on the part of the nonprofit. As our experiences tell us so far (20 investees over the past three years), this model can work very effectively, exceeding our expectations, or fail quite clearly. Perhaps the biggest determining factor is finding the "fit" in the relationship with a nonprofit, recognizing that it will not always exist.

Our four years of experience with SVP Seattle has led us to believe that the venture philanthropy model is full of possibility, but we must be mindful of the perils. The venture philanthropy "movement," will soon come to a crossroads where it will pass from being "cool" into either having been a fad or having real substance and creating real, incremental value in our communities.

As one of our investees described our relationship so far, "The single most important thing SVP has done is to come into the venture with the right attitude, one of 'we're both going to learn. We're here to help, contribute and add strategic value, not to tell you what to do.'" This reminds us of the real possibility and potential in the venture philanthropy model when it is applied with rigor, humility, purpose and long-term perspective.

A Commitment to Accountability: The Coming Challenge to Venture Philanthropy

Jed Emerson

Jed Emerson is Bloomberg Senior Research Fellow in Philanthropy at Harvard Business School and president of The Roberts Enterprise Development Fund. Prior to REDF, from 1989 to 1996, Mr. Emerson served as director of The Homeless Economic Development Fund of The Roberts Foundation. Prior to joining The Roberts Foundation, Mr. Emerson served as the executive director of the Larkin Street Youth Center (working with homeless and runaway youth in San Francisco), as a national consultant to church-based nonprofits, and as young adult coordinator of a national volunteer program for the Presbyterian Church (USA). Mr. Emerson has a Masters in Social Work as well as an MBA.

Mr. Emerson has written extensively on both venture philanthropy and social enterprise. His latest paper, "The Nature of Returns," is available at www.hbs.edu/socialenterprise/download, and his past papers may be downloaded at www.redf.org.

As the report *Venture Philanthropy 2001: The Changing Landscape* so clearly documents, the past year has been an exciting one for those in this evolving field of practice. On the one hand, the launch of new funds pursuing a variety of "venture philanthropy" approaches holds real promise for innovation and the development of new strategies for investing in the creation of social value. On the other hand, those engaging in this practice have begun to attract the attention of critics who challenge venture philanthropists to truly "break the mold." We are at a crossroads, and it is increasingly clear that those involved in changing traditional philanthropy must rise to anticipate a new challenge—that of creating new forms of documentation and accountability to our investees, ourselves and the larger community.

Much of classical philanthropy is focused upon what may be called "transactive philanthropy," an approach to charitable giving that emphasizes the awarding of grants. Within transactive philanthropy, the value of the grant-maker is based upon the size, number and perceived "innovation" of grants awarded. While one may periodically fund an evaluation of a program, the primary definition of success is placed more on the act of giving than upon long-term impact. It is important to recognize that transactive philanthropy is a positive part of the nonprofit capital market. Some organizations with proven track records of success simply deserve additional financial support without the requirement of massive amounts of evaluation. Other causes should be supported simply because it is the right thing to do—this is charity in its purest sense and should not be underrated.

"Investment philanthropy," however, is different. Within an investment approach to philanthropy, the purpose of grant-making is not simply to make grants, but rather to invest in the enhanced capacity of organizations to execute their strategies with the greatest degree of effectiveness possible. Venture philanthropy, while not the only form of investment philanthropy, is an important development in that its primary focus and intent is the creation of greater organizational capacity and the maximization of social returns on investment. While a wide array of players is coming together under the banner of venture philanthropy, virtually all make claims of adding significantly greater value to both funded organizations and the strategies they pursue. We are not simply making grants—we are investing in the sustained improvement of strategy execution.

Within transactive philanthropy, the question of accountability could be said to have less importance to both funder and grant recipient alike. The documentation of accountability is simple: How many grants were made and to whom? Most annual reports or any foundation tax filing would serve to provide adequate information about whether and how the foundation's mission was being fulfilled.

For venture philanthropists, however, the issue of accountability is of paramount importance. Venture philanthropy claims to be significantly different from traditional grant-making in that it seeks to profoundly improve the capacity of organizations to execute their strategies: We make long-term investments in infrastructure, and we support meaningful innovation in the social sector. If this is true, then we must also commit to creating new and better ways of documenting the impact of our work. This applies not only to the performance of our investees—but also to our own funds. It is not enough to simply publish a list of investees and award amounts. We must hold ourselves, both individually and as a field, to practicing what we preach. We must document the degree to which our approach creates added-value, and we must openly and continually critique our strategies in order to raise our collective levels of performance.

As Peter Frumkin of Harvard University's John F. Kennedy School of Government has so rightly observed, "While all failed grants start with ineffective programs, constructive failures create value by helping us understand what went wrong. By contrast, unconstructive failures produce no new knowledge to inform future practice. The challenge for foundations in the future is to gain a greater understanding of constructive failures and to begin appreciating them as central to the diagnostic function of foundations."[3] Yet the present report observes that "efforts to capture and disseminate learnings from venture philanthropy practices are sporadic." Indeed, in discussing the need for early and accurate documentation of practice with the head of one venture philanthropy initiative, the statement was recently made that "we can't be too honest with our investors, since we still need to raise additional money in the future." It should be obvious to all of us that such a mindset speaks to the old school of practice and not the new.

It is not surprising at this early stage of the field's development to see a fear of premature evaluation. Yet it is exactly at this time when we should ensure that all venture philanthropy funds proactively document and analyze their learnings in whatever manner most appropriate to their own work. Since its launch several years ago, Social Venture Partners in Seattle has engaged in an annual self-assessment that is then used by both member partners and grantees to discuss how to best improve the organization. The Roberts Enterprise Development Fund has published not only critiques of its strategy, but also analyses of what happened with investees who were exited from the fund. Both of these efforts are early attempts to honestly identify problems in execution in order to gain the greatest possible value from those learnings by "failing forward." Each of us has the opportunity to change the terms of engagement by integrating our lessons into a continually improving approach to venture philanthropy practice—to the benefit of not simply our own funds, but the larger field as a whole.

If we are truly concerned with increasing the effectiveness of philanthropy, then we must embrace this coming challenge fully and with enthusiasm. In developing a culture of accountability we will all benefit from being open with our critics and modeling the very behavior we would hope all our investees would have—namely, honesty and the capacity to continually improve performance. After all, isn't that what venture philanthropy is all about?

3 "Failure in Philanthropy: Toward a New Appreciation," *Philanthropy*, July/August, 1998.

Venture Capital's Lessons for Venture Philanthropy

David Hodgson

David C. Hodgson is a managing member of General Atlantic Partners LLC, a private equity firm that invests globally in software, services and related information technology companies, and has been with General Atlantic Partners since 1982. Mr. Hodgson serves as a director of ProBusiness Services, a payroll and HR services outsourcing company; Proxicom, a provider of services and related software for developing Internet and intranet-based applications; S1 Corporation, a provider of information technology to financial institutions; and several other companies in the computer software and services industry. He is on the board of directors of echoing green, a national foundation that supports innovative social entrepreneurs, Boys & Girls Harbor, Inc., an East Harlem social service agency, and the Manhattan Theater Club, a thriving off-Broadway theater in New York.

Mr. Hodgson holds an AB Degree in Mathematics from Dartmouth College and an MBA Degree from Stanford University.

Much fanfare has greeted the arrival of venture capital (and venture capitalists) on the nonprofit scene. There is clearly an attractive association between risk-taking in the business sector and innovation in social services. The resurgence in the public sector's ability to engage bright minds as they consider lending name, career and capital to nonprofit pursuits is already improving things in our society. But is there more than fashion behind this trend? How will business principles hold up in close proximity to the many differences that characterize the nonprofit world?

One of the challenges facing business people who cross over to philanthropy and social services is the lack of familiar measurement systems. Social benefits, the output of nonprofits, are often difficult to quantify and value. Efficiency measures for charitable organizations are an enticing proxy, but the best social good often comes from work done with the most severely afflicted, and almost never makes a nonprofit look good on efficiency metrics. Size measures (money raised, people employed) become common success indicators, but offer no insight as to how success is to be achieved by new organizations.

Yet social entrepreneurs have the same characteristic unshakeable vision that their business counterparts exhibit. They are "fundable" in venture capital parlance because they know what they want to accomplish and have a clear view of how to meet a need. And they increasingly attract funding from a variety of traditional and new sources. Their success, measured by money raised, is clear. Their ability to sustain success is not.

Venture capital returns come from creating organizations of value. That value is a subject of constant debate, a debate that can be witnessed on any day in the stock market. But truly valuable companies have several common characteristics that can be spotted. These characteristics can, I believe, serve as models for building nonprofit organizations of value, provided their power and meaning is understood.

Predictability and longevity are beloved business attributes for investors. Since an economic value for a company can be determined by rolling up a long stream of profits into a current value, the easier it is to predict profits and the longer they last, the better. Being predictable and sustainable are hardly typical first principles for the nonprofit entrepreneur; boredom sets in when a board member even mentions them. To be predictable, an organization must have repeatable processes that don't depend on the brilliance of a founder to deliver the goods time after time. And to be sustainable, an organization must be built to outgrow its founder, to transcend its exciting beginnings.

In business, good ventures get to work immediately to define the processes they'll use to deliver a product or service. It becomes everyone's job to continuously critique those processes, suggest improvements, and implement better ones. Process measurement reinforces the company's intuition that things are getting better. The nice thing about measuring internal processes is that most people can agree on the things that make a process better. Shorter wait times for clients, services delivered in fewer visits, referrals or other handoffs made in real time, and more sure-handed treatment of exceptions are examples that cross the profit/nonprofit boundary. Most business people would be prepared to accept that organizations whose processes are constantly improving are probably becoming more efficient and effective as well, even if outcomes data is hard to come by.

A constantly improving organization is often a more exciting place to work, especially if employees have a direct responsibility for driving change. Attracting great people is usually the key to sustainability for an organization, and nonprofits are often challenged in recruiting by low salaries, long hours, and urban or rural locations. Venture capitalists have learned that people drive business value growth and that an exciting culture and big financial incentives help attract the best people. Nonprofits have been reluctant to accept the need for higher pay scales to attract talent (a situation that must change in my view), so most social entrepreneurs surround themselves with enthusiastic but inexpensive and inexperienced teams. A smaller number of better-paid, better-experienced staff may have less capacity to provide service in the short term, but are more likely to keep the agency in business for the long term.

Another critical determinant of sustainability is, inevitably, financial stability. No fledgling business can succeed and grow without significant capital, yet we continue to expect nonprofit start-ups to do so without any endowment, and often with only a year or two of committed funding. Social entrepreneurs take this as a fact of life and merrily walk down the gangplank, counting on their charisma and commitment to ensure that a new funder will always appear in time. It's little wonder that such organizations rarely survive the founder's retirement. Early attention to building a capital base would greatly improve the survival rate for nonprofit start-ups, while raising the stakes for funders and placing more emphasis on proven prior successes, all characteristics of the venture capital market today.

The question of how to best create and sustain innovative social service organizations has clearly captured the imagination of the business world, and with good reason. Business people are people first, and want an equitable, caring society. However, it is the nonprofit sector, not government, that is seen as the mechanism for achieving innovation in social service. Stock market wealth built over the last two decades has fueled a huge influx of social capital. With appropriate borrowing from business lessons about organizational success, it is possible this new era of social entrepreneurship will generate some extraordinary returns on that social capital.

Lessons Learned at New Profit, Inc.

Vanessa Kirsch

Vanessa Kirsch is president and founder of New Profit, Inc. NPI is a venture capital fund for the nonprofit sector focused on growing social entrepreneurial organizations to scale. Ms. Kirsch has 12 years experience in developing innovative solutions to social problems and is widely recognized as a leading social entrepreneur. Prior to launching NPI, Ms. Kirsch founded and led two nonprofit organizations, Public Allies, a national service program, and the Women's Information Network. She has received numerous public service awards and has been recognized by both *Newsweek* and *U.S. News & World Report* as a leader of her generation, by *Harper's Bazaar* as one of 30 young women to be leaders in the 21st century, by *Fast Company*'s "Who's Fast 2000," and by the *Boston Business Journal*'s top "40 Under 40" as one of the most promising leaders in Boston. Currently, Ms. Kirsch serves on the boards of Jumpstart, Dēmos, New Leaders for New Schools, GovWorks.com and the Tufts Advisory Board to the University College of Citizenship and Public Service.

We are in the midst of an incredibly exciting time in the evolution of venture philanthropy. Today, there are dozens of organizations using venture capital techniques to invest in social change, and the potential for this field is tremendous. The decisions we make now and the actions we take could determine whether venture philanthropy becomes a passing fad or fundamentally redirects how we make social change in America. At New Profit, Inc. (NPI), we begin with the following key principles:

- Invest in social entrepreneurs with pattern-breaking ideas;
- Make significant investments of both financial and intellectual capital that support the social entrepreneur's vision;
- Invest for the relatively long term, but plan for an exit strategy; and
- Agree on clear measures and allocate resources based on performance.

Venture capital for the nonprofit sector will only be realized if we all continue to experiment, learn and share our experience. With that in mind, we at NPI appreciate the chance to share some of our early learning and a few thoughts for the future with our colleagues.

Lessons Learned

Develop a clear strategy in order to generate relevant metrics.
With our initial investment, we attempted to define measures of success without first defining a clear strategy for growth. We quickly learned that this approach was the wrong way to go about performance-based funding. Without a clear strategy, it is difficult to gain consensus on the appropriate measures of success. With clear metrics, an organization is more likely to remain focused on its core strategy while pursuing additional resources and is less likely to be distracted by multiple funders' priorities. A recent cartoon shows Dilbert staring at a ringing telephone at a company *without* a strategy saying, "Uh-oh…what should I do?" In the next frame, he answers the phone at a company *with* a strategy saying, "We *don't* do that." Working with our partners at the Monitor Group, we have helped each of our portfolio organizations define not only what they *will* do, but also what they *won't* do. Once a detailed operational plan for growth is developed, each of our organizations develops a Balanced Scorecard (pioneered by Robert Kaplan and David Norton) to which they are held accountable on a quarterly basis.

Put the social entrepreneurs at the center.
Social entrepreneurs hold critical knowledge, and as practitioners, they are invaluable teachers and advisors to each other. Citizen Schools, one of NPI's portfolio organizations, incorporates an educational philosophy based on the apprenticeship model that promotes the idea that when students teach others they do their best learning. Likewise, NPI is an organization and a community run by social entrepreneurs for social entrepreneurs. Just as coaching organizations in our portfolio has increased our skills as leaders, we have found that one of the best ways to develop our entrepreneurs is to directly involve them in the work of NPI's portfolio. They help us in the selection of new organizations for the portfolio, they run strategy sessions for each other, and they join us for fundraising meetings. The dynamic learning community they create is a key part

of our model of venture philanthropy. At first glance, this important part of the NPI culture might not be apparent, but we believe it is critical to our success. Our social entrepreneurs do not sit in our office, but their presence is felt in everything we do and in every decision we make. As they earn their stripes, they take on more of a teaching role in relation to newer members of the portfolio. The culture of NPI becomes stronger the more our social entrepreneurs participate in and improve the activities of the fund.

Be "guests at the table."

In a shift from conventional philanthropy, venture philanthropy can be most powerful when it is centered on the agenda, needs, vision and knowledge of the social entrepreneurs. As in venture capital, better ideas come to scale when led by entrepreneurs and supported by investors who have valuable resources and advice to share. As funders, our job in this paradigm is to work together to support the entrepreneurs and to increase levels of support based on the achievement of mutually set performance goals. While we demand accountability, we have learned that we must also remember the limits of our role. One of our investors, an experienced venture capitalist, introduced us to the concept of being a "guest at the table." No one understands an issue at hand better than those closest to it. We have to remember what we *are* experts at: asking hard questions, presenting data, suggesting options, building a community and leveraging opportunities. At the end of the day, the decisions are made by the social entrepreneur. Engaged venture philanthropy assists social entrepreneurs in doing their jobs: refining their vision, goals and strategies, defining their plans and measures, and making hard choices. Venture philanthropy should be agenda-less philanthropy, where the money follows the entrepreneur's dream and performance.

Looking to the Future

We are all entering the next phase in the field of venture philanthropy. At NPI, we are learning by our experiences and evolving an understanding of what venture philanthropy is and how it works. A community of practitioners is emerging, and together we are sharing knowledge and building intellectual capital. Additionally, more and more financial capital is flowing into the field. Looking to the future, there are two areas we need to focus on. First, we must find opportunities to co-invest and leverage the significant resources in traditional philanthropy to support the organizations we identify as having great potential. Second, we must develop talent to operate these growing organizations. We must refine the skills of people within existing organizations, encourage business schools to prepare managers for careers in the social sector, and bring talent from all sectors to bear on these challenges. Today, America leads the global economy because of the entrepreneurial system we have developed. Working together, we can build a similarly dynamic entrepreneurial social sector and address our country's most pressing problems.

Venture Philanthropy: Strategic Investments for Social Progress

Mario Morino

Mario Morino is chairman of the Morino Institute and special partner to General Atlantic Partners, LLC, a private equity investment firm focused exclusively on Internet and information technology investments on a global basis. The Morino Institute is a nonprofit organization he founded in 1994 to help individuals, institutions and communities understand the opportunities and risks presented by the Internet and the New Economy to advance the social, educational and economic benefit of communities. Prior to establishing the Morino Institute in 1994, Mr. Morino enjoyed a 30-year stint in the information technology industry during its developing years. In 1973, he co-founded Morino Associates, a computer software firm that through a merger became LEGENT Corporation in 1989. LEGENT was acquired in 1995 in what was at the time one of the largest transactions in the computer software and services industry. He is a Trustee at Case Western Reserve University and sits on a number of boards including the Internet Policy Institute, the Council on Competitiveness, the National Commission on Entrepreneurship and Proxicom, Inc.

Venture Philanthropy 2001: The Changing Landscape highlights a number of issues that characterize the emerging field of venture philanthropy. One of the most compelling is that there is no commonly shared definition for what venture philanthropy is and how it is put into practice. This ambiguity of approach ironically can be found in the commercial world of venture capital—not so much in its definition but certainly in its practice. This ambiguity or grayness of the venture capital world carries over to blur venture philanthropy as well.

In the commercial world there is no one description that portrays how all venture capital firms function: a continuum defines those who call themselves venture capital investors. On one end of the continum are those who are simply capital allocators, adding little value to the investments they make. On the other end are the strategic investors, those who form true partnerships with the companies in which they invest and add substantial value. Between these two extremes are the majority of venture capital firms where this relationship between investing capital and providing a strategic value-add varies greatly. The investor's value-add comes from the strength of their investment team—the partners and staff that make up this team. It is their demonstrated experience in supporting leadership and helping build great organizations, their knowledge of the area of their investment focus, and their network of resources to which they have access, that collectively defines the value-add they bring to their investments, over and above the capital they provide. The strategic investor possesses in their investment team a blend of talent that is able to identify great potential, envision what is possible with that potential, and provide the strategic and operational management support to help develop the organization and its leadership to achieve this potential.

This investment continuum also exists in the field of venture philanthropy. At one extreme are those who will make investments (grants) in nonprofit organizations, yet will not be much more than an allocator of capital, bringing little or no real value-add for those in which they invest. On the other end will be those who, like their high-end strategic investor counterparts in the commercial world, will form strategic partnerships with those in whom they invest and will devote significant attention to nurture the growth and development of those organizations. Whether applied to venture capital or venture philanthropy, this continuum is essentially a means by which to classify investors with regard to the needs of a particular investment opportunity. Venture philanthropists can and will function across this venture philanthropy investment continuum. Just as the "best of breed" of the venture capitalist aligns to the high-end strategic investor, we believe the same will prove true for venture philanthropists.

What are the hallmarks of high-end strategic venture philanthropy investors?

- They seek to build great institutions.
- They are represented by an investment team comprised of experienced partners and advisors with a wide range of investment, operational and management expertise – people with the proven experience to add value and expertise to help build and develop the organizations in which they invest.

- They ensure a partner-to-investment ratio that limits the number of investments they make to ensure that sufficient time can be spent with each investment partner.
- They use an investment focus to leverage and build their partner expertise and external resource networks.
- They bring a long-term investment perspective on producing results that count.
- They are actively involved with their investments, becoming vested partners who share both the risks and rewards.
- They place great emphasis on a lasting partnership based on trust and mutual respect.
- They never lose sight that they are there to assist and support the leadership of the organization in which they invest, not to replace or assume the *de facto* leadership role, nor to have that leader assist the investor in his or her priorities or projects.
- And, they provide capital.

Strategic venture philanthropists should mirror their commercial counterparts. They must understand that their work starts, rather than ends, with the funding. They must develop relationships and build trust with the people of the organizations in which they invest. Instead of intruding and directing, they should support and consult. Instead of controlling, they must become partners who provide management advice and help executives deploy resources that enable organizations to deliver on their missions. They must make long-term commitments that enable organizations to invest in building themselves for the future rather than simply surviving to the next quarter. More than anything, they must help their partners do the right things and make the best decisions that will help build great organizations that, in turn, create great value.

Drawing on the experience and expertise of their investment team, venture philanthropy investors can provide strategic assistance in a number of ways:

- Addressing organizational issues;
- Helping to attract and retain key management and board members;
- Assisting in the development of product and distribution channels;
- Helping leverage partnerships through their strategic relationships with other organizations and with other organizations in which they've invested;
- Creating and executing development/expansion strategies;
- Developing financial plans, improving funds development, helping to establish new revenue sources, and creating syndicated funding by bringing together other venture philanthropy investors and foundations;
- Helping management leverage strategic benefit ranging from management development to the application of technology to strengthen the organization and magnify its effectiveness; and
- Providing access to industry and subject matter experts and knowledgeable advisors.

It is very clear that not all of what is done in the world of venture capital is transferable to venture philanthropy. The field of venture philanthropy needs to avoid those practices of shooting only for quick returns, twisting the mission of their investments to meet their own needs, and overly controlling the organizations—practices that caused entrepreneurs to shudder at the thought of having venture money in their firm. Venture philanthropy need not mimic these aspects of the venture capital world. Venture philanthropy should look to high-end, strategic investors as models, those who take pride in becoming partners with those in which they invest and help them build great, lasting institutions.

In 2050, let's hope that history critiques this period as the dawning years of venture philanthropy, which demonstrated its value and triggered a rethinking of philanthropy in America. Let's hope that the growing number of venture philanthropists help usher in a greater awareness of the importance of strategic investment for philanthropy and the nonprofit world—and even with regard to our government funding mechanisms. And most important, let's hope that significant social progress outcomes come from the stronger, highly effective, sustainable institutions that venture philanthropy helped build.

Overview

To compile the following profiles of venture philanthropy organizations, Community Wealth Ventures (CWV) surveyed a broad range of funds, foundations, and donors involved with social enterprise development to identify those that were funding non-profit organizations using the techniques and philosophy of venture philanthropy. The goals of this effort were threefold:

- To provide a comprehensive listing of organizations in the United States that are involved in venture philanthropy;
- To provide a detailed profile of each fund that will allow readers to discern the different approaches and techniques being used; and
- To create uniform and consistent data points for tracking and examining emerging trends in venture philanthropy.

CWV conducted extensive searches of Internet and literature resources and interviewed and surveyed a number of leaders in the field. CWV contacted all organizations cited in the previous report, *Venture Philanthropy: Landscape and Expectations*, to update and expand their listings for this report. Also, most funds cited in the literature search were contacted and received a list of the organizations that we intended to survey, with a request for recommendations of other funds that should be included. This year's list expanded to include 37 venture philanthropy organizations, with the survey results presented in both summary data and through individual venture philanthropy organization profiles.

All funds were surveyed using a questionnaire developed for this year's report (Appendix A). While this report profiles a wide range of funds and grant-making philosophies, to be included in this listing each fund expressed an expectation of high level engagement with grant recipients and a focus on building capacity in those organizations. Additionally, the primary objective of each fund was social return on investment rather than financial return.

Although we tried to create a broad questionnaire framework to allow a wide range of funds to accurately represent their differing philosophies and approaches, some of the funds profiled are structured such that certain questions were not applicable. Finally, we made our best efforts to be comprehensive, but as venture philanthropy is a rapidly expanding and changing field, certain funds may have escaped our research efforts, and new funds may have launched by the time this report is released.

Survey Results Summary

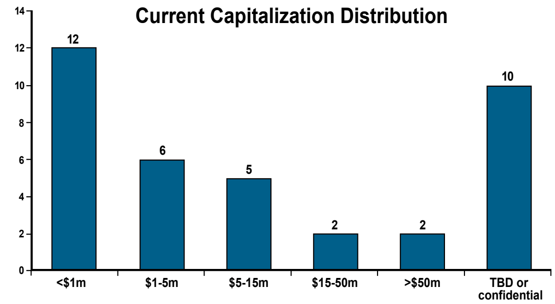
Age of Organizations and Fund Structure

Completed surveys were received from 37 venture philanthropy organizations. Of these, nearly 75 percent were founded since January 1, 1999, emphasizing that venture philanthropy is both still in its infancy and a growing phenomenon. In fact, many of the funds are still in formation, with 17 yet to make an investment as of the survey date (November 2000).

Thirteen of the profiled funds are founded on the donor-advised model, which gained popularity through the efforts of Social Venture Partners in Seattle. In these funds, the multiple investors are also responsible for selecting the appropriate investments and providing strategic management assistance to the grant recipients.

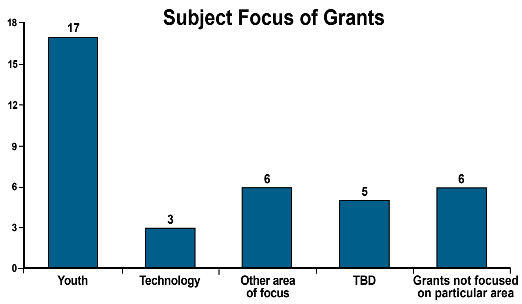
Capitalization

The profiled venture philanthropy funds vary greatly in terms of capitalization. Ten of the firms either had not been capitalized yet or indicated that their size was confidential. Of the remaining 27 funds, just under half (12) had less than $1 million in funds (or funds pledged). Only four funds had greater than $15 million in capital or capital pledged.



Mission Focus

Most funds have clearly defined a specific social focus for their investments, with nearly half of the profiled funds having a focus on youth-serving or education-based organizations. Another one quarter of the funds focus their efforts on either job training or technology-focused organizations. The remaining organizations either do not look for grant recipients within a particular area of focus or are too new to have decided on a focus.



Strategic Management Assistance

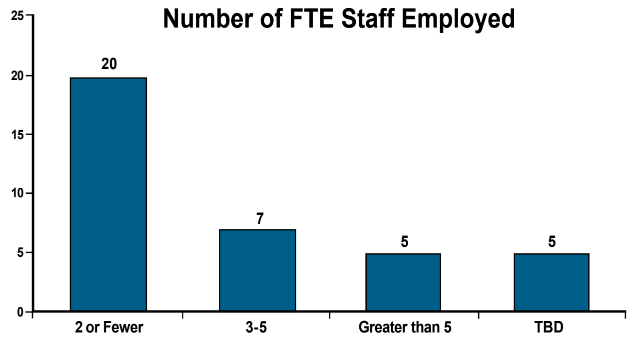
Staff involvement in the grant recipients varies greatly. Of the 37 funds profiled:

- 18 indicated that their staff would provide strategic management expertise;
- 13 indicated that the staff did not provide assistance directly; and
- 6 were undecided.

However, of the 13 organizations in which the fund staff does not provide assistance directly, 12 stated that the investors would fill that role as in the Social Venture Partners (SVP) model. While this means that almost every fund intends to provide some strategic and operating support to its grant recipients, there was little consensus on how this support would be provided, by whom, and in what quantity.

Only three funds said they had or would hire partners with significant cross-industry expertise to assist the grant recipients. Many (16) said they would rely on the expertise and efforts of the investors or of pre-assembled volunteer teams. About half of the funds also indicated that they would hire outside strategic and operating assistance for their grant recipients. Estimates for this assistance varied from a minimal amount to over 600 hours per year, suggesting that very few funds had enough experience to determine how much time they would actually spend working with each recipient. Most of the established funds that had monitored their time actually spent working with grant recipients fell within a range of 150-400 hours per year.

The number of staff at each organization reveals a key paradox being faced by funds with a stated objective of providing intensive strategic management assistance. Over half of the funds had two or fewer full-time equivalent employees. Recognizing that funds structured in the SVP model use the investors in the fund rather than staff to select grant recipients and provide strategic management expertise, only five of the 37 funds have (or anticipate having) more than five employees working full-time on the maintenance and success of their investment efforts.



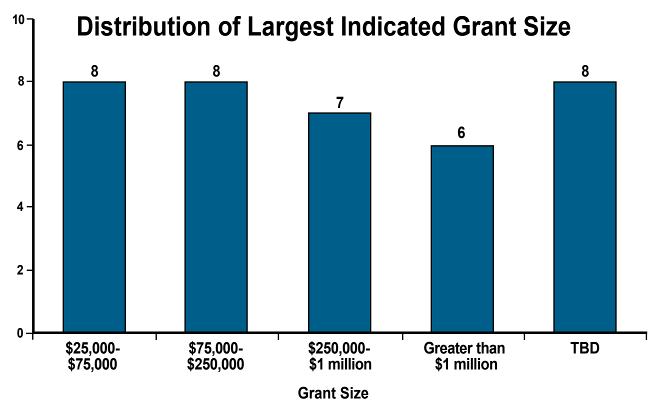
Identification of Grant Recipients

Most funds surveyed (22) utilize a hybrid process for identifying grant recipients, combining the traditional foundation process of accepting unsolicited applications with the traditional venture capital process of actively seeking out qualified nonprofits. Even though many organizations accept unsolicited applications, most prefer to support the nonprofit organizations that they themselves have identified. Only seven of the funds have chosen not to accept unsolicited applications at all. In almost all cases, interested nonprofit organizations submit to a thorough application and due-diligence process before a selection is made; most often the choices are made by an internal committee that uses specific selection criteria. Two funds have developed an incubator for nurturing promising candidates.

Grant Size and Duration

The anticipated size of venture philanthropy investments falls across a very broad range. Although six funds indicated they plan to make investments of over $1 million, this masks the great variance of investment size within many of the funds. Many of these funds award both large, engaged grants and smaller, discretionary grants. In one case, possible grant sizes range from $5,000 to $2 million. At least nine other funds also indicated large variances in grant size. Very few organizations appear to have the capacity and willingness to focus their investments in the range of $500,000 and above.

Among the venture philanthropy funds surveyed, eighteen (or two thirds of the organizations responding to the question) indicated that they would make investments with a timeframe of over three years, versus a traditional foundation grant of 1-3 years. However, only six of the 18 respondents plan to specify focusing their investments in the longer 4-7 year timeframe, and the remaining 12 expressed willingness to fund grants ranging from one year to five or more years. Five funds indicated that they awarded single-year investments with additional follow-up funding contingent on the grant recipients' success in reaching designated performance benchmarks.



Outcomes

There is very little agreement on common metrics for success among survey respondents. Almost all of the organizations indicated that they would work with a potential grant recipient to develop specific benchmarks for success, which in many cases may be used to determine future levels of funding. Five of the firms mentioned self-sustainability as a goal for the investment. Only one firm, New Profit, indicated that they had attempted to devise a measurement of social impact to be applied to all of its investments.