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Trends in the Nonprofit Sector
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“Interim Executive Directors: The Power in the Middle” (2005)

Tim presents webinars and workshops on succession planning and transition management for audiences around the country. To schedule a session for your group, please contact Sheva Diagne at shevad@compasspoint.org.
Dear readers,

In an interview with NPR's Diane Rehm, Reef McIntosh, a surfer facing the big waves on Oahu said, "Conditions on or off, it doesn't matter. We're all still going to be out there. So it was pretty much how it looked: you know, big and ugly and hard and challenging and all that stuff that comes with big-wave riding." This seems like a good metaphor for what our readers have faced, hence the cover of this issue of the Nonprofit Quarterly.

As a part of our Nonprofits in the Age of Obama series, we have highlighted some of the knowledge that we aggregate in our daily online roundup, the Nonprofit Newswire (see "Trends: A Review of NPQ's Nonprofit Newswire" on page 8). This section contains summaries of recent events and their meaning, which you might not expect from this publication.

In assembling this package, we were "re-impressed" with nonprofits' ability to ride the big waves:

- Community-health centers positioned themselves perfectly to become much more central in the system of primary care in this country;
- Community-development loan funds stepped up to act as efficient and productive purveyors of loans to small business and nonprofits; and
- Community-development and housing organizations stepped up as primary players in the foreclosure crisis.

In each of these situations, these networks of community organizations mobilized quickly and efficiently to implement national strategies. For nonprofits during the recession, this is the really big news. These networks are powerful actors, especially when connected by their own communities and supported by national intermediaries.

The story of the power of networks is clear in "Unstill Waters: The Fluid Role of Networks in Social Movements" on page 52. Robin Katcher discusses what matters to network organizers and what influences social-movement effectiveness.

No doubt, this time has been incredibly uncomfortable, but if we wanted disruptive influence to spark a hard look at what works and what doesn’t, we got it. There are so many questions we must now answer:

- What is and should be the relationship of nonprofits and philanthropy to government?
- What is the most effective way to scale a response to a social problem?
- Do we need to think differently about our budgets and revenue sources?

We look forward to continuing to think about these issues with you. For your surf report, be sure to subscribe to the Nonprofit Newswire. And write to me at editorinchief@npqmag.org, and let us know what you think.
Dear nonprofit ethicist,

For nonprofit organizations and those affiliated with them, has anyone seen or developed principles, general guidelines, or “filter questions” that would help define an appropriate relationship between doing good and doing well? With the rapid growth of social entrepreneurship, the issue seems increasingly relevant.

Rarin’ to Go

Dear Rarin’ to Go,

Congratulations: your question is a stumper. For the first time since this column began, the Ethicist put out a call to his colleagues in the academic and practitioner communities. Although Tom Pollak at the National Center for Charitable Statistics and Pam Leland at the Leland Leadership Group had good insight, no one knew of a “decision template” for social entrepreneurship. Therefore, the Ethicist offers a few simple rules of his own devising:

1. The social in a social-entrepreneurship project comes first. Ask whether a money-making project advances the charitable mission—in some way—regardless of the amount of money it raises. Numerous scholarly articles caution that doing well may distract senior management from its real job of doing good.

2. The pecuniary benefits from the entrepreneurship in a social-entrepreneurship project should go primarily to the charitable class of persons for whose benefit the project is purportedly undertaken.

3. Entrepreneurs—not the charitable class—should bear any outsize risk associated with social-entrepreneurship projects. Part of entrepreneurs’ charitable contribution is bearing risk.

4. If a taxable organization undertakes a social-entrepreneurship project, it should voluntarily follow the rules applicable to tax-exempt organizations regarding conflicts of interest and private inurement. The last point deserves elaboration. While there are no federal rules and regulations regarding conflicts of interest, Appendix A to IRS Form 1023 has a model conflict-of-interest policy for tax-exempt entities. On the other hand, existing rules and regulations do limit private inurement: persons capable of exerting substantial influence on a tax-exempt organization’s business decisions are entitled to no more than reasonable compensation.

But regulations do not address return on an owner’s equity as a special form of inurement, because tax-exempt entities do not have private owners. When taxable entities undertake social-entrepreneurship projects, the policy against private inurement must be extended. The Ethicist suggests that the risk-adjusted rate of return on an entrepreneur’s equity should not exceed the most favorable rate at which the taxable entity can borrow.

These restrictions may prompt entrepreneurs to ask, “What is the economic incentive to undertake social projects?” True, there is no special incentive, but these rules are no disincentive either. The object of social entrepreneurship is not to do well but to do well enough. Doing good should be its own reward.

Dear Nonprofit Ethicist,

Should board members be permitted to purchase tickets for a raffle in which an organization participates or it sponsors?

Taking a Chance

Dear Taking a Chance,

Since board members cannot influence a raffle’s outcome, they seemingly should have the same opportunity to win as anyone else. Unfortunately for them, ethics requires avoiding the appearance
of impropriety. If board members were to win the raffle, others might assume the game was rigged.

Follow the example of for-profit companies that use games of chance to promote their products and prohibit employees and their families from participating. The same rule should apply to volunteer board members.

Dear Nonprofit Ethicist,

I’m the founder and president of a small, all-volunteer, nonprofit organization that was founded in 1994 to help stray animals. Last April an acquaintance was taken to the hospital. Because she left my name as her emergency contact, I was called immediately. I did not know this eccentric and reclusive person well; she had no close friends and was estranged from family. My connection with her preceded my charity’s founding (I helped her with a cat adoption several years prior), and she was a longtime, regular donor to my organization.

As a result of the call, I went to the hospital with a volunteer who is an attorney (I worried legal issues might arise). I was instructed by the woman—who died later that day—to take her cats and place them in a home.

Believing that the deceased had a will that might benefit the cause of animal rescue, I made a point to locate the document. She left her two cats, plus her residuary estate, to me. What initially looked like a considerable benefit turned out to be much more trouble than it was worth.

If you are a charity officer or director and are to receive a bequest as a result of charitable work, what are the considerations? In this case, the lawyer-volunteer determined that the bequest of items may have cost a good deal at one time, but was now worth little and had been made for the benefit of the organization, which she communicated to others. I asked the deceased woman’s attorney about whether the decedent’s intent was clear in the bequest, and she said, “She wanted you personally to benefit because of the good things you have done—even if you never were to rescue another animal.”

Do situations like this happen often? Are there rules to follow? This experience has been very odd and a real distraction from our mission, which is difficult enough all by itself.

Just My Luck

Dear Just My Luck,

The Ethicist cannot imagine situations like this happening often. You got lucky (that’s a joke). If the deceased intended her bequest to go to the organization, it would have been easy for her to name the organization as the beneficiary. This should be obvious to everyone except maybe a certain obtuse volunteer: If she named you in her will and her attorney (who is the legal representative of her estate) confirmed her intent, it appears to this nonlawyer ethicist that the gift is yours. What you choose to do with it is your business, but a donation to the charity would be a nice gesture.

Dear Nonprofit Ethicist,

Recently my organization decided to upgrade its Web site and needed budget figures from companies that could perform the work. Since our board president owns such a company, I asked her to provide one of the three proposals that we needed for the grant. I disclosed to the grantmaker that one of the proposals was from a company owned by the board president. We got the grant with the stipulation that the board president’s company not perform the Web site upgrade, citing conflict-of-interest concerns.

When I informed my board president that we received the grant but could not use her company for the work, she was upset and our relationship changed immediately. Over the past several months, I have felt strong animosity from her that has resulted in resistance to many of my initiatives and suggestions. She has been on our board for six years, and I know her well; her recent behavior toward me is clearly a result of this incident.

Our organization has a clear conflict-of-interest policy that requires only that conflict-of-interest transactions be disclosed openly and approved by the board, where the member with the potential conflict is excused from discussion and abstains from voting. This time the donor required it, but it makes me wonder whether the better method of conflict-of-interest management is never to entertain such a transaction. Certainly the organization can lose out on some sweetheart deals from altruistic board members, but this episode has made me see the potential for more risk than reward.

Distraught

Dear Distraught,

So the board president thought you should have withheld relevant information from the grantmaker? Or maybe she thought the conflict-of-interest policy did not apply to her? Bizarre. Do not blame yourself for her bad behavior. Sadly, the safest course is to ban such transactions flat out. It is sad, because when conducted properly, some transactions with insiders may benefit an organization.

This is a teachable moment, so let me add that transactions with insiders are acceptable provided that (1) the conflict is disclosed to the board, (2) the board investigates other alternatives and determines that the transaction is in the best interest of the organization, and (3) the board approves the transaction.
after both debate and voting take place in the absence of the conflicted party.

Dear Nonprofit Ethicist,
I am the executive director of a small nonprofit organization that takes in animals seized by county animal-control agencies because of neglect or abuse. For several months, I have worked with our board president to develop a proposal involving land acquisition that could significantly affect our future. Either the county acquires the land and we manage the shelter, or we acquire the land and contract with the county for services. Both ways have pros and cons.

Our president is unwilling to share the development of this proposal with our board while actively promoting its acceptance by the county. Should the county accept the proposal, it puts our organization at significant risk. The county is in no way obligated to contract with us for services, and should it choose another organization, that organization would be in direct competition with ours.

I have repeatedly asked for permission to share the proposal draft with outside funders for support, and each time the board president asks me to stand down.

Should I go against the wishes of the board president and follow my gut? The president has been with our organization for approximately two years and has moderate political clout. Nearly 10 years ago, I helped cofound our organization and am a significant financial contributor.

Dear Anxious,

Too bad your board president views the board as an impediment rather than a resource. One job of a board is to make sure all important questions are asked before major undertakings. It’s called due diligence. But boards are not good at keeping secrets. If neither the county nor your organization yet owns the land, there is a danger that leaks will drive up the price.

Try to interest your president in appointing a small committee of board members known for their discretion to review the deal. Stress the need for due diligence and try to get him to see that the board will be very angry if he presents it as a fait accompli.

If this approach does not work, give him a choice: either he tells the board (or a committee), or you will. He will not like an ultimatum, but as the executive director, you have a responsibility to the entire board. Being the founder and major donor may carry weight with him, but when the board is given a fait accompli to ratify, these things will not prevent the board from being angry with you as well.

By the way, do you know who owns the land? There may be something else going on beneath the surface.

Dear Nonprofit Ethicist,
An acquaintance took a job as head of IT at a foundation, where he promptly created a valuable piece of software on company time with the help of some consultants. Now he’s shopping around the product to for-profit companies, believing that he’ll figure out how to handle the details with the foundation later.

One of his ideas was to transfer ownership of the software to a nascent nonprofit he started. Then he could more easily take over the software license and sell it to the highest bidder or use it to garner an executive job somewhere.

Dear Appalled,
This is a common occurrence in universities. Your acquaintance, as the creator, and his employer, which provided necessary resources, both have a claim on the economic benefits of this product. Your friend should meet with the foundation’s CFO now and work out an agreement. After the dollars start flowing, it will be harder to negotiate.

But your acquaintance is kidding himself if he thinks transferring “ownership” to a shell nonprofit will allow him to keep all the goodies for himself.

The whole issue here is who, in fact, owns the product? If the product is successful, he can expect that the foundation will sue both him and his nonprofit. Moreover, a court might award the foundation more than he would be willing to give up through negotiation, and he would have litigation expenses on top of that.

Just for the fun of it, let’s look at his shell nonprofit scheme more closely. How does he get paid? If the nonprofit is merely a conduit for cash, he may have difficulty registering as a nonprofit and he will have a harder time getting the IRS to recognize it as tax exempt. If he clears these hurdles, he must still contend with the Intermediate Sanctions law, designed to prevent persons with substantial influence over an organization’s affairs from receiving excess benefits.

A negotiated solution is the simple and ethical solution.

Woods Bowman is a professor of public service management at DePaul University.

To comment on this article, write to us at feedback@npqmag.org. Order reprints from http://store.nonprofitquarterly.org, using code 170201.
This fifth installment of the *Nonprofit Quarterly’s Nonprofits in the Age of Obama* series focuses on the coverage of nonprofits in the media and analyzes more than a year’s worth of coverage of the nonprofit sector broken down into several areas:

- media coverage of nonprofits
- charitable giving in the downturn
- philanthropic contraction
- government funding (at the federal, state, and local level)
- nonprofit networks
- the mortgage and credit crises
- fraud and scandal
- IRS regulation
- nonprofit journalism
Trends: A Review of NPQ’s Nonprofit Newswire

by the editors

In June 2009, NPQ began publishing the Nonprofit Newswire, an online daily roundup of news on nonprofits and the context in which they make decisions. We knew that the combination of a new administration and the recession would cause critical elements of the nonprofit environment to change quickly and at many different levels. We also knew that these factors would further complicate the work of nonprofit leaders. We wanted to keep you abreast of relevant events and trends as they emerge.

The Nonprofit Newswire gathers news from around the country, sifts through it for its bearing on our readers’ work, and relays it—along with commentary on its implications and application to nonprofit practice. NPQ hopes this analysis enables you to make informed decisions about your strategies and to learn from innovation in other fields of work and other areas of the country.

I. MEDIA COVERAGE OF NONPROFITS

While NPQ has not done a formal study of the state of mainstream reporting on nonprofits, it has followed the news in the context of the Nonprofit Newswire. Five staff and volunteers scour the news with not only general keywords such as nonprofits, charity, and philanthropy but also words associated with fields of practice, such as child care, mental health, education and—even more specifically—charter schools. We then choose a mix of stories we believe is interesting and instructive (including some that are simply amusing) and add analysis.

In aggregating the news for the Nonprofit Newswire, we learned a few things quickly: (1) in some states and regions, nonprofit-related news is well covered by the press, whereas in others nonprofit-related news seems to be in a virtual blackout, and (2) by concentrating attention on local news...
have generally involved extending the term of the loan and reducing interest, but not the principal. This leaves many homeowners underwater and in a negative-equity situation.

HAMP is now making changes. “HAMP will now incorporate principal reduction into the refinancing process,” MinnPost reports. “Servicers will be required to consider the advantages of reducing principal to match the current value of the home. As an incentive, banks that reduce principal on loans will also get a fee based on how much debt was forgiven, and how deeply underwater the modified loan was beforehand.” While this effort is expectedly controversial, the farm crisis of the 1980s established the precedent of reducing loan principal.

The implementation of this, however, depends on too many factors to assume that much principal will be reduced. What’s the alternative? Boston-based nonprofit Boston Community Capital (BCC) has bought properties from struggling owners and sold them back at a lower price. The stipulation is that the owner must share with BCC any profits derived from the eventual selling of the home. In its first year of operating the program, BCC has bought 70 such properties (for more on BCC’s program, see page 25).

But even in local stories there are lessons to be learned.

School Asked to Return $900,000 Gift from Convicted Swindler
July 7, 2010; Philadelphia Inquirer
In July the Philadelphia Inquirer reported on a curious case of fraud. When someone steals something and then gives it to you, the rule is that you can’t keep it because it wasn’t the other person’s to give away. On the other hand, when you are the victim of the scam and suffer damages, shouldn’t you be entitled to compensation?

At the heart of a dispute is Malvern Preparatory School, an independent Catholic school outside Philadelphia for boys in grades 6 through 12, which received $900,000 from a former trustee. The trustee, Joseph F. Forte, is now serving a 15-year prison term for swindling investors out of millions of dollars. According to the Philadelphia Inquirer, the receiver—seeking to recover some of the $35 million stolen in a Ponzi scheme—wants Malvern Preparatory School to return the money it received from Forte. But because the school says it was a victim of the scam, it filed a counterclaim for $630,000. That’s how much Malvern Prep says it is owed because of debt incurred to build a new strength-and-conditioning center that Forte said he would contribute $1 million to help construct.
II. GIVING IN THE RECESSION

Giving USA and You: Cognitive Dissonance, Anyone?

by Ruth McCambridge

Over the past 20 months, one of the more well-covered stories in the news on nonprofits has been the impact of the recession on charitable gifts and nonprofit revenue. In short: the recession has left many nonprofits without funding for operational sustainability, let alone money for growth.

Even though the “story” has veered between the fairly dire and confusing, we followed all the revenue streams and permutations in the income of various kinds of nonprofits around the country. So we begin with our analysis of the 2010 Giving USA findings for an overview of the state of giving and then turn to substories in this category.

In early June, I participated in a panel at the Giving USA 2010 conference, where the 2009 charitable-giving numbers were explained by Indiana University Center on Philanthropy’s Patrick Rooney. He did an admirable job of explaining not only the numbers themselves—which indicated only a 3.6 percent drop in overall charitable giving—but also Giving USA’s excellent track record in producing giving estimates that are within a few percentage points of being right on the money.

He may have seen this extra step as necessary, because the day before the panel the Chronicle of Philanthropy ran an article challenging the accuracy of Giving USA’s numbers and, in fact, the numbers just felt wrong to many who had experienced and saw peers experience a much more precipitous drop in philanthropic support.

Adding to the sense of other-worldliness at the conference, the Urban Institute’s Tom Pollak gave a presentation, the gist of which was that, according to the organization’s surveys, the rest of the money flowing into the sector did not see much of a decline either.

Alrighty.

An Injection of Reality

The thing is, I don’t think that either of these gentlemen was far off in his assessment, but I do know that practitioners are accurate in their experience. So what happened?

To understand, we have to look more closely at the numbers. First, some of the philanthropic dollars given in 2009 were given to foundations, but the money is unavailable for immediate distribution. Panelist Wendy McGrady, who represented Giving USA, also noted that $1.6 billion was donated by five major donors and most of it went directly to a few foundations. If you do not count that $1.6 billion, the amount of total giving would have declined another 1 percent.

Also, many were surprised to see that corporate giving had gone up. No one much believed that, but the number includes in-kind donations in two sectors: pharmaceuticals and information technology.

Additionally, philanthropic dollars are hardly equitably distributed among fields or throughout the country.

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Additionally, philanthropic dollars are hardly equitably distributed among fields or throughout the country.
was an awkward fit.

First, the money for expanded services did not necessarily equal increased need, because the requests were made before it was clear how long the recession would last or how high the numbers of uninsured would soar.

Second, just at the moment when need grew the highest, capital projects needed to start, which required community-health centers to scramble to respond to health-care reform.

Third, the money was distributed in odd ways geographically: one wave missed the entire middle of the country, while another invested heavily in states like Massachusetts, arguably one of the better medically served areas in the country.

Fourth, in some states the investment of stimulus money resulted in the withdrawal of state money—a kind of shell game that left organizations reeling.

Not discussed much is clients’ inability to pay fees, which in some areas of the country has hit some subsectors hard. A good example of a sub-sector that has been hard hit in some geographic areas is child care. Many child-care facilities function on a combination of direct-pay fees and subsidies. In locations where joblessness was high, enrollment in child care declined and the budgets of those facilities were eviscerated, creating many closings. Over the course of 2009, 600 child-care facilities in Georgia alone closed.

The reason this particular story is so disturbing is that child care is obviously necessary infrastructure for communities to recover.

For me the thing that characterizes the past year is the way money was distributed in fits and starts. The budget impasse in Philadelphia, which extended 90 days, resulted in several closures of child-care centers. The money was subsequently freed up, but the damage had been done.

Stimulus money flowed into the sector in volume and in waves and ways that were sometimes a mismatch for the comprehensive work of a community organization. Just consider Community Health Centers, a network of community-health centers in California, where the money came in a few waves and was directed at expanded immediate services and capital improvements, including new facilities, development, and electronic records systems. But in several ways, this was an awkward fit.

From Bad to Worse?
Cognitive dissonance can make us angry or guilty or hopeless. In an effort to avoid such a sectoral state of mind, I would like to assure readers that you are not crazy or incompetent (which I am sure you already know). Long story short: if you feel like 2009 was a very bad year for giving, it was—and not just for you but for hundreds of thousands of your peer nonprofits, some of which were in critical support roles in the most financially troubled areas of the country.

But now let’s talk about this year and next, which promise to be as—or more—difficult for many state budgets. Things could get very, very bad, for instance, if the Senate does not pass an
extension of increased Medicaid. Many states have already written an expectation of this money into their budgets, and its loss would remove another $89 billion from 30 state budgets. In Kentucky this would amount to a $480 million loss. I think we can assume that some of those dollars will come out of absolutely critical services to communities provided by nonprofits. It is worth mentioning that Kentucky is ranked 49 in per-capita foundation giving, thus firmly falling in the realm of the philanthropically underserved.

Finally, while foundations are a small part of the giving pie, most agree that, strategically, foundations are very important. The Council on Foundations should take a much stronger leadership position in ensuring that areas that are underserved philanthropically get an infusion of money and the attention of this nation’s foundations. Additionally, I agree with Pablo Eisenberg—a fellow at Georgetown University’s Center for Public Policy & Nonprofit Leadership—who has frequently noted that the payout rate for foundations should be increased over the next few years to 6 percent. Eisenberg estimates that this would add an additional $10 billion to the money available to nonprofits working in one of the most difficult environments we have ever seen.


III. PHILANTHROPIC CONTRACTION
When a donor threatens to rescind a gift, what is an organization that planned on this gift—or, worse, spent the gift already—to do? Below we highlight some examples from our year in review of noteworthy and disastrous donor incidents.

Donor Take-Backs and Other Disasters
In the current economic environment, it’s not surprising that NPQ has identified numerous news reports on donors who refuse to honor their pledges or want to take back money that has been given to an institution.

Some incidents have involved universities and multimillion-dollar gifts. In and of themselves, these stories are interesting human profiles. The Yale Daily News reported that a donation of $1.7 million made to Yale by John Mazzuto (class of 1970), was not his to give. Industrial Enterprises of America, the company he headed at the time of the donation, is now in bankruptcy. The checks Mazzuto wrote to Yale were among $83.7 million he wrote from company funds and of which the current CEO is trying to recover as much as possible.

Over the past six months, Yale has had a bad run. In a similar case in March, another bankrupt company, Bearing Point, pledged $30 million to the university but made payments of only $8.1 million and now wants its money back. The position of the company is that the naming rights that came with the gift did not generate material benefit to it. The irony is that Bearing Point, which is $2.2 billion in debt, was in the business of management consulting and the money it wants back was to endow a management professorship.

Numerous donors have refused to honor their pledges or want to take back donated money.
the organization but confirming that starting in 2010 and continuing indefinitely, he would not make donations of the size of his previous gifts. In his statement, he wrote, “The shift in my financial circumstances is the cause of the reduction in giving, and not any disapproval or dissatisfaction with the programs.” Other nonprofits significantly affected by Gelbaum’s announcement are the Sierra Club Foundation, an environmental group, and the Iraq Afghanistan Deployment Impact Fund, a charity that provides services for American military personnel and their families.

In Boston, Carl Shapiro, a well-known philanthropist who has parked his name on many local buildings, pocketed a sweet $1 billion through Bernard Madoff and may have to return the money. If so, it may jeopardize his pledges to charity, and grantees may have little recourse.

What recourse might there be when pledges are not yet paid? The legal principle of *promissory estoppel*, or detrimental reliance. (*Promissory estoppel* holds that if a party changes his position substantially by acting on a gratuitous promise, the party can enforce the promise even absent a contract.)

**Delayed Donor Pledges**

May 9, 2010; *Palm Beach Post* | In May, in a move that is at least questionable in terms of long-term payback, a foundation in Palm Beach sued its donors for unpaid pledges. The Paragon Foundation, which is supposed to raise $5 million to attract minority businesses to the area, has opted to sue some of the companies that committed a total of $3 million to the foundation, according to the *Palm Beach Post*. The foundation has managed to collect only $1.7 million of the total.

The donor businesses, many of which are real estate firms, have felt the effects of the precipitous downturn in that market. But one of the principals suggests that it has withheld payment not because of business downturns but because it already got what it wanted from the deal—so why pay? On the other hand, some believe that the foundation has engaged in strong-arm tactics.

We do not know whether this trend has worsened during the downturn, but our sense is that many unpaid or delayed pledges out there today have resulted from the recession.

**Philanthropy Addresses Urban Blight**

And then there is organized philanthropy. In April, we shared a story on four foundations that pledged $65 million to the Washington, D.C., public schools, contingent on the chancellor’s maintaining her position.

In July we followed activity in Detroit that aims to keep the city from sinking further into disrepair. We asked our readers about their impressions of this trend, and here is a reader response:

I think you (and others) are raising some very important questions about the blurring of the “three sectors” and the imbalances and inequities that seem to be the result. I work for a public university, and I raise private dollars to support the university, its students, and its programs. Increasingly, the state of Illinois—and the same can be said about other states—has reduced general tax support to the public universities to the point where state or public tax

**More Philanthropic Money Flowing to Public Services**

In our fall 2010 issue, we will address this topic in greater depth, but one of the disturbing trends that *NPQ* has identified is the increasing use of charitable dollars to make public systems whole. Some donations to public systems are made at the individual level as well.

**Donor Gives to Local Sheriff’s Department to Maintain Services**

April 11, 2010; *Mansfield News Journal* | “In Mansfield, Ohio, an anonymous donor, purportedly a local businessman, gave $20,000 to the Mansfield, Ohio, sheriff’s department, the budget for which was literally cut in half from $3.2 million in 2009 to $1.6 million in 2010. The donation is meant to give the sheriff a few months to reorganize.” More familiar, of course, are the gifts that parents give and the fundraising that they do for the public schools in which their children are enrolled.

Some of this giving has occurred at a local institutional level. In March local reports indicate that the New England Laborers’ Cranston Public Schools Construction Career Academy charter school in Cranston, Rhode Island, donated $88,000 to two local public schools to ensure that they had some semblance of a sports program.

Activity in Detroit aims to keep the city from sinking further into disrepair.
dollars support only a small proportion of the operating costs and, in turn, force universities to raise tuition and seek funding from other sources, including private contributors.

Continually rising tuition puts public higher education out of reach for many capable and deserving citizens at a time when future economic well-being—for individuals and the country at large—is dependent on a highly educated citizenry. Viewing public education as a private good—whether at the pre-K or postgraduate level—is indicative of a shift in public policy that we, the public, have come to accept as an alternative to raising taxes and/or demanding more responsible expenditure of public monies. This shift in public policy contributes to increasing inequities, contradicting what I believe is really the role of government: to provide for the common good and to provide access for all to public resources such as excellence in education.

Our willingness to embrace “market forces”—even after the corporate irresponsibility that led to the Great Recession—as a “good thing” in the nonprofit sector contributes not only to a blurring of the three sectors but, more important, to the inequities mentioned above. Market forces work where there is a market—meaning where capital is available. A consequence is that no goods or services are provided to those without capital—or at least sufficient capital. Left to market forces alone, the rich get richer and the poor become poorer.

This trend is especially disturbing because it sets up the expectation that government can stand back from providing even the most essential services and that charitable dollars can possibly fill the gap. This is, of course, not always the case and in itself a dangerous proposition.

A Sign of the Times: The Wall Street Bonus Flap
In a cynical move that stands as an icon of the times, Goldman Sachs, the company that planned to increase top executives’ bonuses at the end of 2009, briefly considered requiring these executives to give some of their ill-gotten gains to charity. Apparently, the marketing wizard who thought up this strategy underestimated the intelligence of the American people, some of whom planned a protest outside the company’s hallowed halls. Goldman Sachs suddenly put $500 million into its charitable arm and reduced compensation from what it had been the year prior, which was well under the increased amount that had been planned.

Goldman Sachs’s Blankfein Doing “God’s Work”?
March 25, 2010; Bloomberg.com | Goldman Sachs CEO Lloyd Blankfein is not talking about it publicly, but from his foundation’s tax filings, a picture has emerged of his personal charitable giving. These findings are curious given that Blankfein once described investment banking as “doing God’s work.”

It’s a dangerous proposition that government can stand back from providing even the most essential services.

The Bloomberg news service reports that between 2000 and 2009, the Lloyd & Laura Blankfein Foundation—which the banking executive runs with his wife, Laura Jacobs—averaged gifts totaling $1.3 million a year. During the same period, including when the investment firm was publicly pilloried for what some described as reckless trading that contributed to the economic meltdown, Blankfein received $240 million in salary, bonus, and stock awards.

Tax records show Blankfein’s giving only through his foundation, which over the past decade adds up to $11.3 million, or about 5 percent of his compensation. Bloomberg said it was unable to determine whether Blankfein gave more and that the CEO had declined multiple requests for an interview.

Foundation recipients include the Robin Hood Foundation, the UJA Federation of New York, and several other schools, medical organizations, and cultural groups.

Regarding Blankfein’s previous comment on “doing God’s work,” it is ironic that the details about his giving appeared the same week as a Forbes story about a British entrepreneur who plans to donate more than half his $1.1 billion fortune to make good on a 50-year-old pact with God. At the start of his career, the entrepreneur told God if he’d help him become a business success, he’d give away at least half his fortune.
Corporate Branding
Over the past six months, news outlets frequently reported on the relationships between corporate sponsors and nonprofits. While most of these skirmishes and corporate-nonprofit divorces involved the incursions of fast-food and soda companies into children’s programs and anti-obesity campaigns, perhaps the most heartrending involved BP’s sponsorship of a sea otter exhibit in a Florida Aquarium. This story emerged in May, a month into the oil spill. At that time, the aquarium had not distanced itself from BP.

In some realms, Bill Gates’s foundation investment outstrips government investment.

Billionaire Philanthropy
For some time, the Nonprofit Newswire has covered the high-profile philanthropy of the Bill & Melinda Gates Foundation, Warren Buffet, and other billionaire philanthropists. While the Gates Foundation and Atlantic Philanthropies model good practices, several questions have been raised over the years about the relatively small number of final decision makers at the Gates Foundation, its overwhelming presence, and, therefore, its potential influence in some spheres of policy.

In some realms, Gates’s investment outstrips government investments. Some estimate that the foundation’s investment in the World Health Organization, for example, overshadows that of the United States.

Additionally, Gates and Buffet have made it their business to encourage other billionaires to get in the game. While NPQ would not turn up its nose at a six-figure investment, we worry that this, combined with reduced tax coffers, could spark a trend toward overdependence on the wallets and decisions of the very rich.

Philanthropic Prizes
We have also seen several American Idol–type philanthropic efforts, such as the Pepsi Refresh Project. Some have suggested that these kinds of initiatives indicate a “democratization” of philanthropy; others believe they are a diversion and a far cry from a leveling of the philanthropic playing field.

Pepsi Opt out of Super Bowl Ads in Favor of Charity ... and, Uh, Marketing
February 2, 2010; Netimperative | Instead of spending the $33 million it spent last year on Super Bowl ads, this year Pepsi launched a social-media campaign that gives $20 million to nonprofits. Each month, the Pepsi Refresh project accepts 1,000 nominations and allows entrants to nominate their ideas and to vote on which groups get the money. Winners were announced March 1, and by February, the process had already reached its 1,000-nomination limit.

As with any social-media campaign worth its weight, the Pepsi Refresh Project also has a heavy presence on Facebook; an application allows people to submit ideas and share ideas via their Facebook accounts. “We’re living in a new age with consumers,” Pepsi’s VP of marketing says. “They are looking for more of a two-way dialogue, storytelling, and word of mouth. Mediums like the digital space are more conducive to that.”

Some may counter, “How dare Pepsi? Super Bowl ads are sacred on Madison Avenue.” Is this the final blow to beleaguered traditional media? Maybe. But perhaps nonprofits can learn from the big guys. Lesson: take the money you would have used to purchase the 30-second spot during the first half of Sunday’s game and invest it in social-media marketing instead. The only problem is, without the commercials, there’s no reason to watch the game.

Big New Initiatives: Foundations
Some readers might scoff at the idea of a new trend in major programmatic initiatives in the foundation sector. Isn’t that what big national foundations do for a living? Big initiatives often seem to be the foundation-generated scripts for social change within which local nonprofits merely audition for roles.

Still, over the past few months the trend is, in some ways, bigger and bolder, and it indicates hope about engaging other philanthropic partners or links to government programs and concepts.

One example is the Kellogg Foundation’s $75 million anti-racism commitment. In May the Kellogg Foundation announced its five-year plan to reduce societal disparities that affect children of color. The Kellogg initiative attacks a long-entrenched societal problem with an array of interventions.
Announced a few years ago, Kellogg’s new strategic direction is child focused. The language of the foundation doesn’t concern change on the margins of the issue. A Kellogg VP told National Public Radio that the program focuses on structural racism and on changing people’s beliefs and biases. It obviously wants to make change sustainable, and to that end, it has posted descriptions of the programs of the 118 grant winners and the 807 groups that weren’t funded in hopes that other foundations will sign up to support the anti-racism projects in Kellogg’s America Healing program.

The Kresge and Skillman foundations have paid for a new city-planning team, headed by Toni Griffin of Newark, New Jersey, to implement Data Driven Detroit, a program to right-size and replan the sprawling, half-abandoned city. The Kresge Foundation has pledged $35 million in seed money for a 3.5-mile trolley line connecting downtown Detroit with an Amtrak station. Foundations have long been the lifeblood of many of Detroit’s services and support. Now, these foundations, along with the Kellogg Foundation and several others, will rethink the future of a city that many have written off as beyond salvation.

Getting Closer to Government

When five national foundations pledged $45 million to the Social Innovation Fund for additional program activity, the message was clear: foundations are increasingly attracted to big initiatives that put them closer to government (for more on the Social Innovation Fund, see “In Search of Breakthrough [or Incremental?] Social Innovation” on page 32). In this vein, NPQ has covered various government plans for foundations to function as re-grantmaking intermediaries and supplemental funding sources—as with the Social Innovation Fund—or as necessary sources of matching dollars, as with the Promise Neighborhoods’ replication of Harlem Children’s Zone.

But when compared with the $506 million pledge by a dozen national foundations to match the Department of Education’s $650 million commitment to its Investing in Innovation (i3) program, they are small potatoes. Department of Education Secretary Arne Duncan hopes that the federal and foundation dollars will help public-school systems scale up innovation and reform: a top priority of the Obama administration.

In March, the Nonprofit Newswire noted that foundations have underwritten the “reinvention” of the city of Detroit by subsidizing planning for the city’s radical downsizing (Detroit was built for a population of more than twice the level of current residents). The Eli Broad Foundation in Los Angeles has paid the majority of the salary of Robert Bobb, brought in from Washington, D.C., as the emergency financial planner to resurrect the city’s public schools.

The message is clear: foundations are increasingly attracted to big initiatives that put them closer to government.

Unlike the old Ford-Rockefeller-Carnegie model—as exemplified by Ford’s Gray Areas program, which evolved into the War on Poverty and Model Cities programs—these foundation initiatives aren’t intended as prototypes for future government replication. While they may involve and leverage government dollars, they are foundation initiatives that stand—or fall—on their own merits, tackling social problems of a scale and intractability that have stymied past public-sector interventions.

Finally, some philanthropic initiatives involve funders that have struck out in new directions and generated programs that neither the funder nor the grantee could have imagined only a couple of years prior.

At Schwab Charitable, the commercial-gift-fund affiliate of the mutual fund behemoth, the monies that sit in donor-advised fund accounts until they are used for grants will help guarantee microfinance loans in the developing world. They remain invested and continue to earn money in donors’ accounts, but they do double duty as guarantees for the loans of the Grameen Foundation, which helps 100,000 borrowers in Egypt, Indonesia, and the Philippines. The Double Give Program allows Schwab donors to see their dollars used in multiple ways to advance the charitable objectives that prompted them to invest in Schwab in the first place.

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**IV. GOVERNMENT FUNDING**

**IV. (a) Federal Funding**

*Despite all the talk—and perhaps hype—about tiny programs, such as the $50 million Social Innovation Fund and the $10 million in planning funds for the Promise Neighborhoods program, the real story in recent federal funding for nonprofits is the American Recovery and Reinvestment Act (ARRA) of 2009. A large portion of the $787 billion stimulus legislation flows to and through nonprofits. Maybe the community-health centers, community-action agencies, and community-development corporations that play crucial roles in the stimulus simply don’t tout themselves with the alacrity of the self-styled social entrepreneurs and social innovators, but they have important stories to tell about the role of the nonprofit sector in making the stimulus work and overcoming impediments built into stimulus programs.*

**Stimulus Funds: ARRA**

In the first half of 2010, the stimulus stories have been distinguished by the nonprofit sector’s demonstration of the innovative behavior built into its DNA.

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**At the time of this writing, the bulk of the stimulus funds has not been spent.**

At the time of this writing, the bulk of the stimulus funds has not been spent: As of June 30, 2010, only $122 billion of $275 billion slated to go out in federal grants, contracts, and loans (as opposed to the $288 billion in tax relief and the $224 billion in entitlements) had been paid out. Our spotting of past trends may ultimately be predictions of future directions in stimulus funding; these trends highlight the challenges that the nonprofit sector will have to confront and overcome.

**Critics Out in Force**

Stimulus funding has, of course, received its share of criticism, a healthy portion of which has been directed at nonprofits. Republican senators John McCain and Tom Coburn issued a report deriding much of the stimulus as no more than politically motivated pork, and Coburn’s pet target has been spending for nonprofit cultural activities, such as theater programs. His notion is that funding for the arts doesn’t generate as many jobs as, say, funding for shovel-ready highway projects.

The senators also took aim at youth-employment programs by selectively identifying individual grants and contracts that did not seem to meet their targets or purposes. In one of the oddest critiques we might have imagined, they were joined by the new governor of New Jersey, whose staff came out against youth-employment programs run by nonprofits, suggesting that the benefit to young people working as recreation counselors, for example, was demonstrably inferior to summer employment in the private sector, such as working as stock clerks in drugstore chains. We didn’t say any of this made demonstrable sense.

**Reservoirs of Distrust**

The bulk of the weatherization funding in the stimulus was intended to go to and through community-action agencies because they have delivered weatherization services (i.e., services to promote home energy efficiency) throughout the nation for years. But many states that have received weatherization funds have been slow to distribute funds to nonprofits. In North Carolina, weatherization crews were supposed to start working in July 2009 but didn’t hit the streets until November. Explanations for the laggard expenditures include Davis-Bacon Wage Determinations for weatherization contractors and multiple layers of certification mandated to ensure accountability. State officials in North Carolina took the extraordinary step of warning the 30 nonprofits designated for weatherization money “not to use the funds to finance regular operations . . . [and] not to use the money to pay employee bonuses.”

In this state, as in others—such as Texas and Georgia, where the funding flows seemed glacial—the program sparked state distrust of nonprofits (in this case, community-action agencies), but in this area of stimulus funding, responsibility for delays should be shared at every level.
The Approaching Funding Cliff
Several articles in the Nonprofit Newswire highlighted the dangers inherent in expanding programs with time-limited funding, such as the one- and two-year stimulus grants. For cities and counties that anticipated a post-recession flow of local tax revenue after the expiration of stimulus funds, some have scrambled to pay the salaries of stimulus-hired policemen and teachers, prompting Congress to contemplate new funding to help cities and counties preserve jobs.

There are dangers inherent in expanding programs with time-limited funding.

It’s more difficult to find salary money for nonprofit jobs that don’t fall into the police-fireman-teacher bucket of government jobs. In western North Carolina, nonprofit jobs that will be at risk when the stimulus funding ends include staff at Head Start and Early Head Start programs, expanded medical teams at a community-health center, and three positions at a Boys & Girls Clubs of America. As difficult as it is to make the case for Congress to preserve government jobs, it is harder to see the path for a major extension or infusion of stimulus capital for nonprofits that face a stimulus funding cliff.

Stimulus Strategy Assessed
December 27, 2009; Telegram & Gazette | Here are the two faces of the stimulus package. On the one hand, there is a problem in putting onetime stimulus funding into organizational operations, according to the December 2009 Telegram & Gazette. As Roberta Schaefer of the Research Bureau asks, “What are you going to do when you don’t have stimulus money? If [the stimulus] is just going to prop up existing institutions without making any changes in how they operate, it can’t be sustained. That’s a really big problem.” On the Worcester public schools, Schaefer says, “The school department got stimulus money that stemmed the tide for them, [but] [n]ext year, because there will be no stimulus money, they’re facing a $26 million deficit without any way of funding it. The stimulus money, in effect, just delayed the inevitable.”

And on the other hand, stimulus funds have gone to longer-term uses, such as the two grants given to the Great Brook Valley Health Center. They’ll use one for hiring new doctors and support staff, who eventually will generate enough revenue from patient visits to sustain the salary costs. The other grant will fund facility improvements to create space for new providers and more patient visits. Similarly, at the Worcester Housing Authority, stimulus money went to roof repairs and other physical rehabilitation costs, which will stave off future costs.

This tale of two stimulus stories highlights the contrast between grant funds that lead to an abrupt funding cliff and stimulus funds that stimulate long-term growth. Of course, problems persist. The Community Builders, a nonprofit housing developer and manager, added 23 new positions as a result of its two stimulus funds but counted 46 jobs created: that is, 23 jobs created twice. Stimulus is good, but for many organizations, the looming funding precipice will create a serious problem in the all-too-near future.

Nonprofit Bulwarks for the Stimulus
Criticism of stimulus priorities was to be expected. But criticism of the role of nonprofits in the stimulus makes little sense. Notwithstanding occasional problems, nonprofits have been wildly successful in stimulus implementation. The $1.85 billion in stimulus funds that has been invested in health centers translates into $3.2 billion in new economic activity in communities via new services and jobs.

In the area of broadband initiatives, nonprofits have taken major roles in developing programs to accelerate broadband deployment in un- and underserved rural areas, such as Connect Minnesota’s collaboration with that state’s Department of Commerce. Though delayed, even the weatherization program will finally be implemented.

To make the stimulus work, nonprofits have become problem solvers and, yes, even social innovators making inadequately formed programs that are implemented by overwhelmed government agencies work nonetheless. Despite the fru fru of the social innovation hyperbole, the discernible trend in the stimulus stories of the first half of 2010 is the tried-and-true nonprofit sector demonstrating its innovativeness in solving problems.
that would reduce or eliminate delays in contracting and reimbursements, suggesting not only centralized contract monitoring but also the elimination of redundant programs with conflicting, useless rules and regulations. In a March Utica Observer-Dispatch article, the comptroller explained that state agencies that can’t issue contracts and make payments in a timely manner worsen the problems of nonprofit-service delivery. This conclusion was not a sudden lightning bolt of awareness by local officials, of course. The state associations and management-service organizations grabbed ahold of the issue and refused to unlock their jaws.

Elsewhere, the nonprofit stance had to be what nonprofits typically do: organize, lobby, and sue.

**Mississippi Mental-Health Providers Face Off with State**

*June 14, 2010; Sun Herald*

A story from the Sun Herald in June was familiar but had an interesting twist. Nonprofits have long found themselves in untenable negotiating positions with government and are often unpaid for the full cost of contracted services. Further, this situation is unlikely to be imposed on a profit-making contractor.

In 2001 in Mississippi, for example, the state decided that it would offload a portion of the cost of the match to federal Medicaid funds flowing to mental-health centers by requiring them to pay it.

But this year, the six strongest of the 15 mental-health centers in Mississippi played hardball with the state and have refused to pay their portion. Their intention is to make the state resume its matching responsibility. Edwin LeGrand, the director of the Mississippi Department of Mental Health, dug in, saying, “They’ll no longer be considered state providers if the share isn’t paid by July 1. If that happens, the program is set up in such a way that funding for all 15 community-mental-health centers could be jeopardized.” The executive director of Region III Mental Health Center, Robert Smith responded, “We cannot continue to operate paying back 25 cents on every dollar that we earn. We’re all just struggling trying to figure out the best way to resolve [the issue].”
centers are located in low-income areas and, because of regulation, are still largely community based in terms of governance. But they are also networked through intermediaries, and the federally qualified are connected through a common funding source. Because they work in areas with large numbers of uninsured, they are a natural network for the implementation of health-care reform.

Although Obama’s historic Patient Protection and Affordable Care Act was not signed into law until March, the federal government tried much earlier to expand and strengthen the network of community-health centers around the country, apparently to prepare them for an expanded role in primary care through the use of stimulus money. Stimulus money was released for at least three goals: the expansion of patient load during an anticipated period of increased unemployment, the expansion and improvement of facilities, and a conversion to electronic records. Again, this money was not distributed evenly. One competitive wave of it missed much of middle America, and in other locations, the stimulus money suffered state cutbacks in a kind of shell game.

V. NONPROFIT NETWORKS IN THE NEWS
During these hard times, nonprofits have proved nimble and adaptable. In considering the networks that have mobilized around national crises, nonprofit robustness becomes particularly evident. The networks discussed here are distinctive because their members are explicitly community based but knit together by intermediaries that know what they are doing. Below we provide a snapshot of some networks’ resourcefulness even in the wake of fewer resources.

Health Reform: Community-Health and Mental-Health Centers and Hospitals
The nation’s 1,200 community-health centers working out of 8,000 sites have their roots in the civil-rights movement and Lyndon Johnson’s War on Poverty. During the 1960s, their inception and the enactment of Medicaid and Medicare occurred within a year of one another and attempted to address inequities in health care. Community-health centers are located in low-income areas and, because of regulation, are still largely community based in terms of governance. But they are also networked through intermediaries, and the federally qualified are connected through a common funding source. Because they work in areas with large numbers of uninsured, they are a natural network for the implementation of health-care reform.

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The end of access to federal dollars could create a post-stimulus hangover.

Where are these events headed? Various local governments have tried to tax otherwise tax-exempt nonprofits through payments in lieu of taxes, fees on students at universities, taxes on hospital beds, and other creative, desperate government strategies to eke out a few nickels from nonprofits to plug budget holes.

Will it get worse? As we watch the end of access to federal stimulus dollars, it could create a post-stimulus “hangover” in which community-action agencies, youth programs, environmental groups, and health clinics try to manage programs with stimulus funds that will run out after 2010.
This kind of sector research should be funded more frequently at the network level. It offers timely and meaningful data that can have major impact.

The health-care reform bill calls for $11 billion to be distributed over the next five years for community-health centers, which are viewed as central future providers of primary care. Representative Bernie Sanders of Vermont can be thanked for shepherding through the centrality of health centers in the reform act as well as the funding, despite accusations that the health centers would bypass laws preventing the federal funding of abortion.

While community-health centers received investments, nonprofit hospitals and free health clinics did not. Even as this debate raged, free clinics reported being overstretched, and nonprofit hospitals were judged a poor credit risk. All the while, some predatory activity by larger hospitals targeted community hospitals that struggled.

**Free Health Clinics**

Outside recent funding streams—and reflecting how much health-care reform and current appropriations fail to meet the needs of poor people—are the networks of free health clinics. In June the Nonprofit Newswire reported on the results of a survey of 1,007 free clinics (with a response rate of three-quarters), indicating that free clinics serve an average of 1.8 million people who make 3.5 million medical and dental visits in the United States every year. Each free clinic served an average of 747 new patients each year and 1,796 unduplicated patients. Their budgets are small, averaging $287,810, and more than half receive no government funding.

During the debate on health care, nonprofit hospitals were judged a poor credit risk.

Many of these clinics are associated with the National Association of Free Clinics, which represents 1,200 free clinics in the United States. In March, the Nonprofit Newswire noted free-health-clinic events in Atlanta, Georgia, Roanoke, Virginia, and Belmar, New Jersey, with the Roanoke and Belmar clinics heavily focused on dental care. More free-clinic days were planned for Houston,
New Orleans, and Little Rock. In each clinic, hundreds waited in line and thousands were served.

Still, our suspicion is that health-care reform will leave many without coverage, such as undocumented immigrants specifically excluded from coverage by the legislation, others unable to qualify for Medicaid or Medicare, and those unable to afford repeated co-pays. Because health-insurance reform will be phased in over several years, these nonprofit or volunteer-organized free clinics will have a continuing function for many years to come, with a crucial role for the networks that support them.

**Nonprofit Hospitals**

But not all nonprofit hospitals have struggled, and the Senate Finance Committee continues to raise questions about how to justify the “nonprofitness” of hospitals. During this period, the states have provided much of the regulatory oomph, particularly where attorneys general have decided to question the nonprofit credentials of tax-exempt entities that don’t behave much like nonprofits.

The Senate Finance Committee continues to raise questions about how to justify the “nonprofitness” of hospitals.

The headline example was the case of Provena Covenant Medical Center in Illinois. The state attorney general, Lisa Madigan, suggested that Provena’s activities didn’t distinguish it from a for-profit hospital, contending that the hospital “concealed the availability of charity care,” had debt collectors chase poor patients for uncompensated health-care services, and gave the poor little information on how to apply for charity care. As you might guess, Provena disagreed.

In what is expected to be a precedent-setting case, the courts ruled against Provena, and the state supreme court approved the attorney general’s decision to yank the Catholic hospital’s tax exemption because of insufficient charity care. The appellate courts found that Provena devoted less than 1 percent of its revenue to charity care, an amount that simply doesn’t qualify as a nonprofit level of service to the community.

With a relatively quiet IRS, there has been more activity among attorneys general—especially since attorney generals often run for higher office—and more focus on fraud and self-dealing as well as on the nonprofit status of large tax-exempt entities such as hospitals.

Meanwhile, the Mental Health Parity and Addictions Equity Act went into effect on January 1, 2010, but without any investment to build out existing systems of care. Last year, in the report *Grading the States*, the National Alliance on Mental Illness evaluated these systems of care state by state, and the nation as a whole received a D.

Theoretically, the parity act frees up money from insurance companies that are now required to cover mental illness at parity with physical illness, but implementation of this requirement will take many steps and iterations that may include legal challenges to insurance companies looking for a way out. Advocates also worry that many chronically mentally ill people are uninsured.

When the Patient Protection and Affordable Care Act was signed, however, the parity requirement was extended to the uninsured, but the systems of care are still inadequate and in many areas provide a poor foundation on which to build. In fact, on the eve of Mental Health Month (in May), several states were busy eviscerating their existing programs. Some of the conversation suggests that advocates may not even try to rebuild a standalone system for mental-health programs but instead, through cross-training, build out the capacity of physical health facilities to address mental illness.

Meanwhile the United States has historically high numbers of chronically mentally ill people in prisons and jails and more lost on our streets. The report *More Mentally Ill Are in Jails and Prisons Than in Hospitals* by the Treatment Advocacy Center and the National Sherriff’s Association revealed “America’s shameful 50-year trend of exiling severely mentally ill persons out of hospitals and into the oblivion of the criminal justice system.”

VI. THE MORTGAGE AND CREDIT CRises AND NONPROFIT INTERVENTION

The historic spate of mortgage foreclosures throughout the nation may be the primary culprit behind the economy’s dissolution into
The Great Recession. But the involvement of nonprofit community-development organizations and the national and regional networks that support them may be the pivotal element in reversing the foreclosure tsunami. The work of these organizations in digging the nation out of the housing crisis hole demonstrates a model of nonprofit networking and resourcefulness from which other organizations can take cues.

This past year, the Department of Housing and Urban Development (HUD) made available new funding for its Neighborhood Stabilization Program (NSP) to fund states, municipalities, and nonprofits to acquire, rehabilitate, and return foreclosed properties to the market. The scope of the problem is enormous, taxing the financial and organizational capacities of even the largest community-development corporations (CDCs). But community-development networks have come to the table to rebuild swaths of foreclosed properties—often the dregs that private purchasers have passed on.

The tellingly successful response in these nonprofit approaches to foreclosures has been facilitated by the existing organization of CDCs and others into consortia or networks. As covered in the Nonprofit Newswire, the Neighborhood Stabilization Program (NSP2) grants announced early this year rely heavily on nonprofit consortia, for example, $137.6 million to Habitat for Humanity International for work in five states and $137 million to Chicanos por la Causa for work in eight states. One third of NSP2 grants went to nonprofits that are members of the NeighborWorks network (the Neighborhood Reinvestment Corporation). In addition, three cities’ applications have placed local offices of the national Local Initiatives Support Corporation in key roles.

Locally crafted consortia evolved in Milwaukee, which received $25 million in NSP2 funds to be used in collaboration with the Milwaukee Foreclosure Partnership Initiative (MFPI), with steering committee members from the Local Initiatives Support Corporation, the Greater Milwaukee Foundation, and others for targeted neighborhood marketing and a code enforcement “strike force.” The city of Newark put in an application as the lead for a $20.8 million NSP2 grant covering much of Essex County in partnership with nonprofit developers such as Brand New Day, Episcopal Community Development Corporation, and others.

Other local networks tackled the foreclosure problem as well. They include the various community-development loan funds and community-development financial institutions that link various groups to restore vacant foreclosed properties and return original residents to their homes.

In March the New York Times described Boston Community Capital’s “brainchild” program, which works with local nonprofits to purchase homes that have been foreclosed—before residents have been evicted—and then rent homes back to occupants. The process works well for banks and residents, occupants don’t lose their homes, and banks can offload properties with plummeting market value.

Perhaps the most significant of these networks is the effort of funders such as the Ford Foundation and the John D. and Catherine T. MacArthur Foundation to create a $1 billion real estate owned (or REO) capital fund under the aegis of the National Community Stabilization Trust to acquire foreclosed properties in bulk on behalf of nonprofits and municipalities.

The challenge of negotiating for large groups of foreclosed properties from recalcitrant lenders and servicers requires the creativity and experience of the nation’s top community-development financial intermediaries: the Local Initiatives Support Corporation, Enterprise Community Partners, the Housing Partnership Network, NeighborWorks America, the National Urban League, and the National Council of La Raza. But without Ford’s $50 million in program-related investment to the trust, plus MacArthur’s working capital loan of $3 million, the trust couldn’t play anything but a marginal role in acquiring discounted properties from banks and servicers, according to the Wall Street Journal.

Nonetheless, the existence and effectiveness of these networks and consortia in addressing the

**Boston Community Capital’s program helps local nonprofits purchase foreclosed homes and then rent homes back to occupants.**
foreclosure problem appear to help put grassroots groups onto municipal and state government radar screens—and on the Department of Housing and Urban Development’s as well.

But large parts of the nation might not be linked into national housing and community development. That puts the onus on HUD to ensure that

Nonprofit CDFIs rose to the challenge and maintained capital inflows in low-income neighborhoods.

local and state governments join with grassroots groups to ensure that the strategies for redeveloping foreclosed properties benefit the communities and families that the stimulus was designed to assist. It also puts an onus on national networks to identify the gaps where foreclosure is an issue, but un-networked nonprofits find themselves unable to secure the capital and technical assistance to function effectively.

The Credit Crisis and CDFIs

Community Finance Institutions Successful but Poor

April 21, 2010; The Daily Record

Across the nation, nonprofit community-development financial institutions (CDFIs) have done much better than Troubled Asset Relief Program (TARP)–subsidized commercial banks, particularly when you realize that CDFIs work in low-income neighborhoods and take on projects that conventional lenders typically wouldn’t consider.

In Maryland, CDFIs have financed day-care centers, affordable apartments, senior-citizen complexes, and new businesses. Among the notable are the Enterprise Community Loan Fund in Silver Spring (which helped finance senior housing developed by a church-based community-development corporation in Northwest Baltimore) as well as Baltimore Community Lending, Maryland Capital Enterprises (in Salisbury, doing business microloans), and Baltimore’s Neighborhood Housing Services.

CDFIs have a lot going for them—except capital. Between 2006 and 2009, the number of CDFIs in Maryland dropped from 22 to 16. Nationally, CDFIs report the inability to keep pace with loan demand because they simply don’t have enough capital for lending. The Obama administration has increased federal support for the CDFI Fund at the Department of Treasury, which is the nation’s primary source of CDFI funding (through grants and tax credits). Between 2007 and 2008, the fund increased from $54 million to $94 million; between 2008 and 2009, it increased to $107 million; and then, through the stimulus bill, it received another $100 million.

The increased appropriations have been accompanied by greater competition among CDFI applicants. Maryland has developed programs to support CDFIs, including those in the Department of Business and Economic Development and the Department of Housing and Community Development.

But these programs can’t provide nearly enough capital to meet the housing, facility, and business development demands in lower-income neighborhoods.

How unusual! This successful program is almost entirely dependent on nonprofits, yet there’s not enough money available for these nonprofits to function, as the common parlance says, “at scale.”

The Great Recession began and persisted largely because of the implosion of banks and mortgage companies that backed—or promoted—subprime loans and other risky adjustable-rate mortgages. In response to their self-inflicted damage, the banks turned off the credit spigot to lower-income communities, affordable-housing development, and inner-city economic ventures—just what the nation didn’t need from the financial industry.

As they have always done, nonprofit community-development financial institutions—including community-loan funds, community-development credit unions, and community-development financial intermediaries—rose to the challenge to maintain capital flows in low-income urban and rural neighborhoods, often outperforming their larger and better-capitalized for-profit counterparts.

On several occasions, the Nonprofit Newswire has noted the stellar performance of CDFIs in providing loan capital to community-based housing and economic development projects.

Although CDFIs received a substantial appropriation through the stimulus program, they can hardly be characterized as well subsidized compared with the billions in TARP funds that commercial-bank counterparts received. But as we noted in April 2009, nonprofit CDFIs have done much better than TARP-subsidized commercial
banks, particularly when you consider that CDFIs work in low-income neighborhoods and on projects that conventional lenders won’t consider.

According to Neil Barofsky, TARP’s inspector general, the Wall Street bailout failed “in many ways,” not the least of which because TARP-subsidized banks failed to restart their frozen lending pipelines. With only pennies of comparable loan resources, CDFIs lent as fast as possible, with loss rates that were proportionally tiny compared with those of banks.

Despite their successes, CDFIs reported that they were unable to keep pace with loan demand because they don’t have enough capital for lending. This problem occurred despite the Obama administration’s increased federal support for the CDFI Fund at the Department of Treasury.

We believe that TARP funds would have been better used if at least half had been set aside for nonprofit users such as CDFIs. These standout organizations have gotten increased attention, including a commitment by Treasury Secretary Timothy Geithner to invest repaid TARP funds in CDFIs at an initial dividend rate of 2 percent, as opposed to the 5 percent rate of Treasury’s Capital Purchase Purchase Program (CPP).

After eight years, the dividend rate of these investments will be 9 percent, compared with five percent under CPP.

We suspect that other nonprofit fields merit attention and profile comparable to the recession-era performance of CDFIs. Nonprofit Newswires mention them regularly in part because of their connection to national networks that promote and publicize their work and advocate federal funding programs, including the creative use of repaid TARP funds. CDFIs are a model not just of nonprofits performing admirably but of a nonprofit field that has demonstrated how to organize and advance despite plenty of financial and competitive hurdles.

**VII. SCAMS, SCHEMES AND THE SCURRILOUS IN NONPROFITLAND**

*With the nonprofit sector still reeling from the economic downturn, it hardly needed more to strike a blow. But over the past year, fraud and scandal have played a significant role in the fortunes of the third sector. We provide a roundup of some of the standout offenses below.*

**Internet Scam Bears Watching by Charities**

May 17, 2010; NorthJersey.com | A recently uncovered online work-at-home scam has used the Habitat for Humanity name to involve people in raising funds that are forwarded to accounts that—you guessed it—have nothing to do with Habitat. Targeted individuals are offered a “job” to fundraise for the well-known charity and instructed that they are allowed to keep 10 percent of the take and must send the rest to a specified bank account.

An FBI representative says that these scammers are increasingly hard to track because of mobile technology and new accepted ways of conducting business. They “clear out bank accounts quickly or use wire transfers that are difficult to trace. And they move on to new scams rapidly, closing down e-mail accounts and opening new ones with different Internet providers.” Habitat is doing all it can to keep up with the moving target of this con, but as the FBI rep says, “Each technological advance poses another impediment to catching them.”

**Scams: Chasing After Disaster**

Earthquakes, oil spills, economic destitution . . . bad times bring scam artists out of the woodwork to prey on others’ hope and despair. During this period of high unemployment, we have seen several variations of work-at-home scams for the unemployed. These kinds of scams are much harder to trace because of the increasing use of mobile-communication devices.

**TARP funds would have been better used if at least half the funds had been set aside for nonprofits.**

In June we noted that so many charity scams have popped up in the wake of disaster that the FBI created the National Center for Disaster Fraud after Hurricane Katrina. The BP oil spill has engendered yet another wave of such exploitation and, to counter it, the Oil Spill Fraud Task Force, which includes the aforementioned FBI unit and representatives from local law enforcement bodies. There are so many levels at which such scams are destructive, it is difficult to list them all.
Everyday Fraud: Fleecing Children, Nuns, and War Veterans

For the nonprofit sector, fraud stories are the equivalent of murder stories for the local news. If it bleeds, it leads, and over the past year the Nonprofit Newswire has followed some appalling cases, complete with sympathetic victims.

What characterizes many of these cases is the choice of the kind of charity targeted. Veterans, children, and others to whom we as a society rightfully believe we owe something have been the objects of such scams. Thankfully, state attorneys general have moved to punish evildoers, but such scam makes donors more wary.

In March, BusinessWeek reported that the Federal Trade Commission levied a record-setting $18.8 million fine against the New Jersey-based telemarketing firm Civic Development Group LLC, which raised funds for charities associated with service people: military veterans, firefighters, and police.

The charity claimed that 100 percent of donors' gifts would go to charity. In reality, however, the charities in question received only 10 percent to 15 percent. In this case, the firm's owners will be forced to relinquish at least a portion of their ill-gotten gains. As BusinessWeek reports, “Pasch will surrender a $2 million home, paintings by Van Gogh and Picasso with a combined worth of $1.4 million, an $800,000 guitar collection, $270,000 from the sale of his wine collection, $117,000 in jewelry, three Mercedes and a Bentley. Keezer will lose his $2 million home and vehicles.”

Over the past year, the Nonprofit Newswire has followed some appalling fraud cases complete with sympathetic victims.

A few days later, in Worcester, Massachusetts, so-called professional fundraiser Michael Hilady was charged with bilking nuns of $370,000 based on allegations that he lined up a fictitious donor named “Arthur” to contribute between $3 million and $14 million. School representatives had even accompanied Hilady to Florida a few times to dine with the donor, but these in-person meetings were always canceled at the last moment.

Based on Hilady’s promises, the nuns began their work and racked up $3 million in construction costs before it became clear that there was no money and, evidently, no Arthur. Investigators located Hilady at a Comfort Inn in Rhode Island with a woman who is not his wife. Massachusetts Attorney General Martha Coakley said investigators concluded that Mr. Hilady spent some of the money paid him from Venerini Academy on adult entertainment, personal expenses, and travel.

The most offensive but also most confounding story over the past year is the strange saga of the U.S. Navy Veterans Association. This story came from the hardworking St. Petersburg Times in March 2009, and you have to read the series to believe the events. Long story short: the organization runs a national fundraising operation that brought in $22 million in 2008, but attempts to track down organizational leadership, auditors, and documentation of spending have proven fruitless. The pursuit of these characters has extended to other localities.

Schemes: Politicians and Nonprofits

For a publication dedicated to covering trends in the sector, certain stories are all-too common, including the number of politicians, lawmakers, and policy makers that have been cited in news accounts for misdeeds—from stealing to misappropriating funds to actions that, if not illegal, are morally wrong.

Take the case of three California officials responsible for prescription-drug spending for low-income patients. These officials had no qualms accepting money from a nonprofit funded by pharmaceutical companies that do business with the state to pay for their travel to drug industry conventions and conferences. Should these three public employees have known better? Absolutely. As the San Francisco Chronicle reported, Medi-Cal prohibits employees from accepting gifts that exceed $320 from any firm, subsidiary, or person that “has financial dealings with the department.”

In some cases, politicians know better, but it doesn’t stop them from behaving badly. For instance, in something that could only be considered sheer political grandstanding, Republicans in the U.S. House and Senate this past spring...
pushed for a moratorium on all earmarks, including those to nonprofits and municipalities. As we noted at the time, the mere status difference does not ensure that federal dollars will be well or badly expended. Instead, as John Cranford noted in CQ Politics:

There seems to be an impression that nonprofits are by definition small, public service-oriented organizations, when they sometimes can hardly be distinguished from ordinary companies. Three of the largest defense contractors—Aerospace Corp., Battelle Memorial Institute, and Mitre Corp.—are organized as nonprofit enterprises. Battelle had almost $3.5 billion in federal contracts in fiscal 2008, including shared responsibility for managing the Oak Ridge National Laboratory. Not coincidentally, Battelle also benefits from a few million dollars in earmarks in fiscal 2010 appropriations, according to Taxpayers for Common Sense.

Even when their acts of philanthropy suggest ulterior motive, politicians that seem to do good can come under a cloud of suspicion. After New York City Mayor Michael Bloomberg gave some $200 million to arts and cultural groups from his personal wealth, the New York Times noted, “The gifts reflect the often blurred roles Mr. Bloomberg plays in the city as mayor, tycoon and philanthropist. And while the donations earned him praise from grateful recipients, who regard him as an enlightened billionaire, they also drew rebukes from elected leaders, who argued that he bought political acquiescence with his checkbook.”

Of course, some stories cause any reasonable person to wonder, “Will this ever stop?” The most egregious of such incidents was a suit filed by New York Attorney General Andrew Cuomo against state senate majority leader Pedro Espada charging the lawmaker with stealing $14 million over five years from nonprofits he and his family operated. As Talking Points Memo reported at the time, the suit alleges that Espada used Soundview Health Center, the nonprofit clinic he founded, to pay for $80,000 in restaurant bills and $450,000 worth of credit-card charges. The suit also alleged that Soundview gave Espada a contract for a $9 million severance package and $75,000 in credit for unused leave time, of which he had 14 weeks every year.

VIII. IRS: ENFORCEMENT

Over the past year, the IRS has been relatively quiet in its dealings with the nonprofit sector. As noted previously, that has made state attorneys general more assertive in their efforts to root out fraud and other nonprofit misdeeds. But even in a calm year, the IRS made its presence known in a few areas of nonprofit activity. Below we detail the highlights.

Over the past six months, the big news in IRS regulation of nonprofits is the push to determine who is alive and kicking and who has expired among the smaller nonprofits in the sector.

This past year, the IRS has not been a ball of fire in getting nonprofits on a straight-and-narrow path.

As background, the IRS and others have assumed that nonprofits have inflated sector head counts because they have never declared themselves dead. The IRS requested that nonprofits that hadn’t yet submitted a 990 complete a simple electronic form by May 16, 2010. As of April 2010, the total number of nonprofit organizations of all sizes registered with the IRS was 1.5 million,196,000 of which had not responded by the deadline. The IRS stated its intent to pull the status of all nonresponders, but late requests should be open to mercy.

IRS Shuts Down Credit Counselors

Over the past few years, the Internal Revenue Service has not been a ball of fire on regulations meant to help (or push) nonprofits along a straight-and-narrow path. Maybe the IRS’s new 990 requirements occupied too much of the agency’s charity bandwidth.

But the IRS did show nonprofit regulatory gumption in the nonprofit-credit-counseling arena, and it should better review the behavior of nonprofit mortgage-down-payment groups. In 2006 the IRS stated that it could rescind the
status of groups that provide buyers with mortgage-down-payment “gifts” that are in fact payments from developers to induce purchasers to buy homes with inflated prices. Soon after, HUD weighed in, saying that if the sources of gifts were questionable (i.e., seller provided), it wouldn’t approve down-payment gifts on Federal Housing Administration (FHA) loans.

You would think that that’s the end of the story. But the Nonprofit Newswire continued to encounter problems suggesting that nonprofits linked to private real estate developers had found ways of reinventing themselves to shimmy past IRS and HUD restrictions. In Sacramento, the bibli-cally named Nehemiah Corporation of America, a pioneer of the gift-down-payment-assistance idea, now works through a for-profit affiliate to recycle its accumulated down payments into an affordable-housing investment fund. Its CEO (whose salary is $480,000) said that the organization’s income contributed to down payments ($55 million, according to a January 2010 Sacramento Bee article) to be used by Nehemiah’s for-profit arm for direct real estate investment on its own and for grants to nonprofit housing developers.

To Nehemiah, this setup is true to its nonprofit mission by linking it with for-profit developers under the guise of “economic empowerment and transformative community development.”

Housing-related nonprofits have found ways to shimmy past IRS and HUD restrictions.

Rather than giving the gifts to purchasers of developers’ homes, Nehemiah will work with the developers as partners—and then presumably provide the down-payment gifts on homes that Nehemiah has (partly) developed. To us, the scheme sounds like circumvention.

The IRS has improved in clamping down on nonprofit credit-counseling agencies. These groups, which pledge to reduce tens of thousands of dollars of credit card debt and wipe out home-mortgage and car payments in a matter of months, are not just too good to be true. Many are on the highly dubious side of the nonprofit definition. We noted that in 2009 the IRS revoked the tax-exempt status of several groups, accounting for 41 percent of the revenue of the “nonprofit” credit-counseling industry. It approved only new three out of 110 applications for tax-exempt status for credit-counseling groups.

IX. THE NEWS ON THE NEWS

In a paradigm shift within journalism, some news sources have turned to the nonprofit sector as a model. Below we catalog recent shifts in the media and their implications for a free and independent press.

The scramble to protect free journalism from market forces has continued, with many ducking for cover under nonprofit status. This is a historic shift, but not without precursors. As NPQ’s fall 2005 article “The Five Pillars: Nonprofits and Media” indicated, “Both nonprofits and the media are creatures of the First Amendment. They are also creatures of government subsidy because both a free press and people’s free and active association are considered to be necessary for a healthy and informed citizenry.” For some time, a portion of journalism has been seated in nonprofits, but for-profit news outlets dominated until recently, when their business plans began to fall apart. In an interview with Mark Jurkowitz in the fall 2009 issue of NPQ, we covered the changes in the for-profit landscape.

In April 2010, the J-Lab at American University estimated that since 2005, $143 million in foundation grants went to news-media organizations, and half of that amount went to 12 investigative sites. Over the past six months, several startups of nonprofit centers for journalism have emerged in several forms. Many do investigative work in an effort to get picked up by mainstream news outlets; others specialize in topical areas.

Two issues that are front and center are (1) financial influence over editorial stance and (2) sustainability. When a major donor backs a journalistic effort, bias can become a problem.

Pete Peterson, the conservative hedge fund founder who would like to see Medicare and Social Security sharply reduced for the good of the country, for example, has backed the Fiscal Times Web site, which feeds editorial content to
CONCLUSION: ON THE JOURNEY AND IN THE TRENCHES

The Nonprofit Quarterly is a nonprofit publisher, but we also cover the nonprofit sector. Thus we are embedded in the community we serve. In 2000, we began publishing the print publication with the intention of providing nonprofits with a source of well-vetted, relevant, and challenging information. In late 2008, as we recognized that a period of intense change was on the horizon, we committed to following and interpreting the news so we could keep pace with this important community. It has been a fascinating journey. We feel like we are in the trenches with you but have a bird’s-eye view as well.

Like all of you, we have done more with less but also found improvements in that scarcity. And like many of you, we have found that we can count on our colleagues in the trenches for support and advice on the world and the battles to be fought from your perspective.

One of the lessons learned that we intend to build on is that many of our readers have insightful analysis to provide on what is happening in philanthropy, with government funding, and in their organizations. NPQ has always tried to tap this reader input, but it has been a more episodic process. As we move forward into a period of “sector reformation,” our intention is to engage you more as correspondents.

In this way, we can more thoroughly and consistently engage the collective intelligence of this sector throughout every field and geography. We hope you are ready.

To comment on this article, write to us at feedback@npqmag.org. Order reprints from http://store.nonprofitquarterly.org using code 170202.
In Search of Breakthrough (or Incremental?) Social Innovation

by Jon Pratt

By focusing on high-impact, results-oriented nonprofits, we will ensure that government dollars are spent in a way that is effective, accountable, and worthy of public trust.

—First Lady Michelle Obama on the Social Innovation Fund

In mid-2009, the Obama administration announced the launch of the Social Innovation Fund, which called on the private sector to join forces with government to invest in social problem-solving initiatives. The proposal allocated $50 million to these efforts.

Now, a year later, the Social Innovation Fund’s call for proposals has closed. These “socially innovative” initiatives will receive federal funds to address three priority areas:

• Economic opportunity. Increasing economic opportunities for economically disadvantaged individuals;
• Youth development and school support. Preparing America’s youth for success in school, active citizenship, productive work, and healthy and safe lives; and

Jon Pratt is the executive director of the Minnesota Council of Nonprofits and a contributing editor to the Nonprofit Quarterly.
• **Healthy futures.** Promoting healthy lifestyles and reducing the risk factors that can lead to illness.

The Social Innovation Fund faces clear obstacles in terms of scale and sustainability. The prospect of influencing three different fields with $50 million for a population of 300 million could create an expectation gap. But the biggest challenge is not the elusive definition of *social innovation* (which is itself a problem). The chief challenge is how to prevent these innovations from becoming short-term, novel projects that attract attention and then fade away. While the fund purports to foster innovation, a short-term infusion of dollars may not support lasting results.

Clearly, being innovative is a desirable trait. And the designation—even indirectly by the White House—of innovation could have major fundraising and publicity benefits for grantees.

So what is *social innovation*? According to the Corporation for National and Community Service’s Notice of Funds, *social innovation* is defined as the following:

The development of a potentially transformative practice or approach to meeting critical social challenges. An approach is “transformative” if it not only produces strong impact, but also 1) has the potential to affect how the same challenge is addressed in other communities, 2) addresses more than one critical social challenge concurrently, or 3) produces significant cost savings through efficiency gains.

Left out of this official definition is any mention of political conflict, despite our own national experience over the last 100 years, which has shown that implementing substantial social innovations has been very contentious, with changes facing opposition and public protest, frequently requiring legislation and litigation.

**The Roots of Social Innovation**

There is no question that huge shifts in the United States’ response to society’s changing needs have their roots in social innovation. Consider these examples:

• **Institutionalization of those with developmental disabilities.** There was a movement from large, impersonal, state-run institutions for people with developmental disabilities to community-based group homes and centers for independent living. This shift was not simple; and the change was supported by family members, the Arc of the United States (formerly the Association of Retarded Citizens of the United States) organizations, and mental-health professionals but resisted by legislators and public employees as well as through government inertia.

• **Domestic violence.** A network of domestic violence shelters that gave options to families suffering from abuse was created. The reform struggled against attacks that shelters undermined family relationships and promoted a feminist agenda. In fact the true innovation was not shelters but the elimination of the social acceptability of violence within family structures.

• **Charter schools.** A new K–12 choice of decentralized chartered schools was developed. It faced deep concern among teachers unions and school boards over the diversion of funds from public schools and the blurring of the public–private school distinction.

• **Abortion.** Legal alternatives to pregnancy became available, including birth control and safe abortion services, which triggered a religious and political battle.

Each of these social innovations began as pioneering efforts around the country, often supported by individual contributions and foundation grants before public funding became available. Students of social innovation may benefit from considering the role of resources that were committed early on, as in 1916 for Margaret Sanger’s first birth-control clinic in Brooklyn; the start of the National Association of Parents and Friends of Mentally Retarded Children in 1950; the 1964 founding of Haven House in Pasadena, California; and the 1991 support base that passed the first charter school law in Minnesota. These small starts began a process of demonstrating, experimenting, and finally promoting and advocating resources and replication.

The concept of social innovation implies that there are standard ways of doing things and new
possibilities: the old and the new. The new language of social innovation adopts positive business terms and perspective energized by an entrepreneurial spirit that captures efficiency through economies of scale and uses smart management that is accountable through rigorous measurement of results.

The current conversation about social innovation presents a positive, hopeful belief in evidence-based change that occurs by common agreement with broad public acceptance of an obvious improvement—not unlike the replacement of floppy disks by flash drives. Happily, flash drives were quickly recognized as more convenient, sturdier, cheaper, and with fewer moving parts (and no one publicly opposed it or got hurt by the change).

The mighty little flash drive demonstrated that innovation could be an immediately recognized clear improvement: simpler, cheaper, and just plain better. But for social innovations such as those described above, each was accompanied by resistance from sectors and institutions that felt threatened, undermined, or destabilized by the innovation.

Reconciling Conflict with Social Progress

Clearly, the landscape of social progress is more complicated than that of flash drives. No doubt the administrators of the Social Innovation Fund want to keep the debate free of the bitterly partisan wrangling in Washington, as the rancor over health care and debates over social and economic issues demonstrate. Perhaps by adopting business terminology, the phrase social innovation seems like a kinder, gentler, less political version of adaptation than is social change.

Lobbying, regulation, public funding, lawsuits, and court orders have been an important factor in establishing 14,000 group homes for people with developmental disabilities, 1,980 domestic-violence programs, more than 3,000 charter schools and 1,787 providers of legal abortion.

These four examples reflect the broad diversity of social innovation. There is no consensus on a single, straight path of social progress, and social innovation cannot be based primarily on financial efficiency.

Is Social Innovation Sustainable?

The public recognition generated by a high-profile competition—such as American Idol—can jump-start a career or expand fundraising for a nonprofit. In the case of the Social Innovation Fund, the intention is that the competition for funds will allow the best innovations to rise to the top so that they can be supported, thoroughly demonstrated, and replicated. As with any new product, the assumption is that the marketplace will beat a path to the door of social innovation, mostly by abandoning less-effective products and re-dedicating the freed-up dollars.

A critical challenge for the Social Innovation Fund is these resource questions: After the Social Innovation grant to pioneer an innovation concludes, what will generate continued and expanded funding? Will Social Innovation Fund grants drive the market to these innovations for postfund support and sustainability?

There are five scenarios in which these innovations could carry on, and each involves risks and varying degrees of probability.

1. **Displacement.** New social innovation will free new money by displacing older, less-effective programs or low-performing organizations. Or these new efforts will convince other organizations to adopt the innovation using ongoing resources.

   This method is based on a common but incorrect assumption: that the displaced funding is
Availability suggests, this scenario assumes that social innovation will make organizational operations more efficient and free up dollars to continue to support these innovations. In the case of youth development or school success—unlike the stamping out of flash drives—the personal nature of these activities limits the impact of technology and economies of scale—unless the strategy is to replace personal contact with interactive video. And in fact, higher education reports that online courses cost as much or more than classroom sessions.

Gaining these hoped-for efficiencies from management know-how (e.g., using sharper pencils as opposed to subject-matter expertise) are often tied to performance management systems’ “best practices” and outcome measures. Because these measurement systems aim to create benchmarks across organizations (frequently by measuring what is most easily measureable à la No Child Left Behind), they promote standardization and tend to depress innovation and local customization.

2. **Program fees from private sources.** In this scenario, the assumption is that social innovation will generate its own revenue by attracting fee-paying clients, tapping into the spirit of the related fields of social entrepreneurship and social enterprise.

But generating earned income is easier said than done, especially when clients are low income—unless they have dedicated funds, primarily from government sources. An underlying tenet of social enterprise is that business activities are available to generate funds for community services. But other than a few creative and rare examples, this is simply not a realistic prospect for the problems and populations the Social Innovation Fund seeks to address.

In 2006, U.S. nonprofits received $649 billion in program fees from private sources, but the bulk went to hospitals, colleges and universities, and health clinics, with few fees dedicated to economic opportunity, at-risk youth development, and health promotion. So the likelihood that Social Innovation Fund innovations will generate reliable and robust earned-income revenue is slim.

3. **Efficiency gains.** As the Notice of Funds Application suggests, this scenario assumes that social innovation will make organizational operations more efficient and free up dollars to continue to support these innovations. In the case of youth development or school success—unlike the stamping out of flash drives—the personal nature of these activities limits the impact of technology and economies of scale—unless the strategy is to replace personal contact with interactive video. And in fact, higher education reports that online courses cost as much or more than classroom sessions.

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4. **Charitable support.** Successful social innovation will attract increased charitable dollars and volunteers to continue and expand the activity. Corporate and foundation grants are rarely part of such a long-term plan because they move from special project to special project. Individual donations are most reliable for organizations when clients are from the same constituency as the donors (as with colleges, universities, and large cultural organizations). But these donations represent a small portion of the support for low-income beneficiaries. From Eugene Lang’s 1981 promise of a college education to 61 Harlem sixth-graders to the $500 million Annenberg Challenge in 1993 to the reform of K–12 education, philanthropy often seeks “new” projects but remains consistently episodic.

5. **Public funding.** In this scenario, after the benefits of a social innovation have been demonstrated, public funds will follow; this pattern occurred during the launches of Head Start, community-action agencies, and Legal Services Corporation.
While the prospect that significant new ongoing dollars will come from any government level seems dim in the near term, this scenario may be the most realistic over the long term. It is true that state and local governments (including school districts that serve low-income students) are under intense fiscal pressure, and federal deficits have prompted the Obama administration to release a flat 2011 budget for domestic discretionary spending. Nevertheless, and while recipients of stimulus funding know that these funds have a defined end date, the federal government is probably the most plausible source of substantial resources, but only if government funding is part of the Social Innovation Fund strategy from the start.

Front-End Quick Hits Won’t Cut It

The recession has only exacerbated the decreasing reliability and autonomy of nonprofit funding overall—for government and nonprofits in the education, community-health, and cultural fields, for example—especially for small organizations and nonfederally funded organizations serving low-income communities. Today, even Teach for America—one of the best-recognized social innovations—must compete for its federal earmark of $18 million a year. The chosen subgrantees for the Social Innovation Fund will undoubtedly struggle to find lasting commitments to sustain their work.

The track record of short-term demonstration grants, special projects, and model programs is unfortunately that of high levels of initial activity and “promising results”—and then, suddenly, they’re gone. Supporters of innovation should read Lisbeth Schorr’s 1988 book Within Our Reach: Breaking the Cycle of Disadvantage, which analyzed social programs that effectively combatted serious social problems (such as high rates of single parenting, youth violence, and school failure). According to Schorr, the good news was that many projects succeeded. The bad news was that, after being starved of resources for five years or more, these successful projects often disappeared.

By definition innovation is new. In the philanthropic world, innovation tends to attract attention and resources on the front end. It’s what comes after that will legitimately determine whether the Social Innovation Fund has been “transformative.”

Based on the goals for the Social Innovation Fund, short-term commitments without a chance of continuation will create more false hope and sabotage than true social innovation. This is particularly true when intermediaries are foundations, which will have to work hard to increase their attention span and willingness to make commitments.

There is a great deal of interest in how the Social Innovation Fund will be used. It will be up to the designated intermediaries and the Corporation for National and Community Service to make these grants the beginning of enduring investment that can be fairly described as “effective, accountable, and worthy of public trust.”

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The *Fatal* Design Defects of L3Cs

by Daniel S. Kleinberger

In 2008, Vermont enacted the first low-profit limited-liability company (L3C) statute. L3Cs are supposed to combine charitable giving and for-profit investing to empower socially productive enterprises. Since the passing of the Vermont statute, five other states have enacted parallel legislation.

L3C proponents laud L3Cs as a breakthrough in charitable giving that will permit private foundations to help fund for-profit entities with socially conscious aims. Advocates have claimed that L3Cs are destined to be fast-tracked for special treatment under provisions of the Internal Revenue Code (known as the Code, or IRC) that address charitable foundations’ program-related investments (PRIs). PRIs include equity investments as well as loans and loan guarantees and other kinds of nongrant investments in private enterprises.

Unfortunately, the glowing characterizations of L3Cs are flatly wrong.

The L3C is an unnecessary and unwise contrivance, and its very existence is inherently misleading. The notion that an L3C should have privileged status under the Code for access to tax-exempt foundation resources is inescapably at odds with the key policies that underpin the relevant Code sections, and L3Cs are not on track—let alone on a fast track—to receive special status under the Code. An ordinary limited-liability company (LLC) can perform precisely the same functions proclaimed of L3Cs. In addition, because of technical flaws, the L3C legislation adopted to date is nonsensical and useless.

**A False Panacea**

This assessment may seem harsh—even Grinch-like—given our nation’s current economic woes and the bright prospects painted by L3C...
proponents. Who wants to oppose benevolent efforts to “save existing farms . . . help an otherwise struggling company in today’s competitive environment or . . . buy an empty factory, re-equip it to be a source for many jobs . . . make a museum or other non-profit self sufficient . . . address food and housing issues . . . provide sustainable solutions to medical, sanitation, conservation, energy, and environmental issues”?1

Much better to agree with those who see L3Cs as providing a new horizon. “The arrival of the L3C potentially is a watershed moment for individuals and organizations that are dedicated to achieving social change,” write Cassady Brewer and Michael Rhim. “By combining the unique features of an LLC with the ‘soul’ of a nonprofit, the L3C may result in dramatic increases in the availability of both private and philanthropic capital for ventures that are designed to further charitable and educational purposes.”2

The reality, however, is starkly to the contrary, and growing ranks of L3C opponents have emerged to demystify the L3C model. These opponents include tax law experts, academics, and practitioners in the law of limited-liability companies; expert practitioners who work with nonprofit organizations; low-income housing and community-development financing; and charity officials. Authors of the country’s three leading treatises on LLC law have cosponsored a resolution to the American Bar Association Business Law Sections Committee on Limited Liability Companies, Partnerships and Unincorporated Entities that opposes the incorporation of L3C amendments into existing LLC acts and urges state legislatures not to adopt L3C legislation. An associate general counsel of a famous charitable foundation has identified six “myths” purveyed by L3C proponents and has described L3Cs as “less than meets the eye.”3

This article identifies and dissects the principal claims of L3C proponents to demonstrate that L3Cs are neither beneficial nor useful. Proponents’ principal claims are the following:

1. L3Cs “dovetail” IRS rules on PRIs, thereby enabling private-foundation investment in qualifying businesses that operate for socially beneficial purposes.

2. L3Cs permit “tranched investment” through which foundations can make high-risk, low-return investments, enabling profit seekers to make low-risk, high-return investments and bringing market-rate capital into socially beneficial enterprises.

3. L3Cs create a “brand” that enables easy comprehension and use of PRIs.

In fact, none of these claims is correct.

**Current Law: The Crucial Context**

L3C proponents argue that L3Cs will revolutionize the relationship between nonprofits and the marketplace by freeing up tax-advantaged PRIs. Before we can address that argument, though, we must understand the status of private charitable foundations under the IRC as well as the protective limitations the Code and the Treasury regulations place on private charitable foundations.4 In particular, we must understand the prohibitions on speculative investments and the requirement that foundations annually distribute a specified portion of their assets.

Private foundations enjoy tax-exempt status and must navigate myriad tax regulations designed to protect charitable assets from poor management and diversion to noncharitable purposes or private persons. These regulations have strong teeth; contravention brings excise taxes so heavy that they have been described as “toxic.” Speculative investments and investments for improper purposes—known as “jeopardizing investments”5—trigger substantial excise taxes not only for foundations7 but also for foundation managers who make these investments with the knowledge that they may jeopardize the carrying out of a foundation’s exempt purposes.8 Moreover, “private inurement” (i.e., benefits to ineligible purposes or persons) can destroy a foundation’s tax-exempt status,9 and in theory at least, this prohibition comes with “zero tolerance.”10 In addition, foundations face nearly confiscatory taxes to the extent that they fail to properly distribute at least 5 percent of their assets annually.11

These strictures provide the context in which PRIs make sense. The virtue of program-related investments is that they permit private foundations to make investments rather than grants in...
Devising a PRI arrangement requires careful and individualized investigation.

mission-appropriate enterprises (1) without these investments being considered speculative or otherwise “jeopardizing”; and (2) with the investments counting toward the minimum annual payout required of foundations.12

But PRI regulations are strict and specific. The following conditions must be met for an investment to qualify as a PRI:

1. an investment’s primary purpose must be to accomplish one or more of the purposes described in the IRC’s section on charitable purposes (section 170(c)(2)(B);
2. no significant purpose of an investment can be production of income or appreciation of property; and
3. no purpose of the investment can be to influence legislation or elections.13

While all three requirements may initially seem generic, the first is, in fact, foundation mission-specific. According to the Code, “[A]n investment shall be considered as made primarily to accomplish one or more of the [acceptable charitable] purposes . . . if it significantly furthers the accomplishment of the private foundation’s exempt activities and if the investment would not have been made but for such a relationship between the investment and the accomplishment of the foundation’s exempt activities”14

Consequently, every time a foundation considers making a PRI, the foundation must make a situation-specific determination that carefully considers the foundation’s mission, the purpose of the organization receiving the investment, the relationship of the receiving organization’s purpose to the foundation’s mission, and how the governance and financial structure of the receiving organization ensures that the receiving organization will operate within PRI requirements.

At minimum, this final determination requires the foundation to carefully monitor the activities of the receiving organization. Indeed, prudence likely requires at least some control. Either way, devising a PRI arrangement requires careful and individualized investigation, deliberation, negotiation, and drafting. An opinion of counsel is almost de rigueur, and prudence sometimes warrants seeking a private-letter ruling from the IRS.

Thus, as an Exempt Organization Tax Review article makes clear, there is nothing automatic or off the shelf about making PRIs.

Perhaps the reason many private foundations approach some PRI transactions with caution is that they realize arrangements between charitable entities and for-profit entities can be very complex, and it is inherently risky to intentionally invest assets in their portfolio in transactions expected to produce below-market returns. The reason many private foundations seek private-letter rulings may be because they understand that PRI transactions that push the envelope in terms of producing income or the appreciation of property should be approached with caution.15

Compare this view with the insouciance of L3C proponents, who apparently consider private-letter rulings a waste of time: “We honestly believe if an L3C is used and the IRS regulations are followed, there will not be an issue,” Robert Lang writes. “No one asks permission to drive the posted speed limit. Why ask the IRS if you can follow their regulations?”16

The Dangerous “Benefits” of L3Cs

With this background, we can now examine the three principal benefits that proponents claim are derived from L3Cs.

1. Consider the supposed “special” connection between L3Cs and PRIs. According to L3C proponents, an L3C is a brand-new tool in the foundation toolbox designed to expand the use of PRIs,17 thereby “opening up PRIs and the whole socially beneficial sector . . . [so that an L3C] will become a vehicle for bringing in more money to socially beneficial entities without compromising the return.”18

L3C proponents initially buttressed these claims by asserting that pro-L3C changes to the Internal Revenue Code were on a “fast track” to enactment.19 In fact, Congress has not created a special category of PRI treatment for low-profit limited liability companies and appears unlikely to do so.

Indeed, Congress cannot do so without turning the PRI concept upside down. To constitute a PRI, a foundation’s investment must fit the program of the investing foundation.

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Experts are skeptical that L3Cs will open the floodgates to billions of dollars. But experts are skeptical that L3Cs will open the floodgates to billions of dollars. In addition, tranched investing raises serious policy concerns and is dangerous as a tax matter. Foundations have the privileges of tax-exempt status and can receive deductible contributions. Tranched investing runs the risk of exporting these privileges to benefit noncharitable businesses, managers, and investors.

Tax law has a term for this sort of private benefit—known as private inurement—and transactions that create private inurement can create debilitating problems for charitable organizations. Properly constructed, a tranched investment arrangement might survive IRS scrutiny, but it is dangerous to advocate tranched investing by foundations as a generic, easy, and readily available device for social progress.

2. Consider “tranched investment,” which L3C proponents extol as the way to leverage foundations’ PRIs to access trillions of dollars of market-driven capital. Under a tranched approach, a foundation makes a low-return, high-risk investment in a venture with modest financial prospects but major possible social impact.

The first tranch enables a venture to draw investments from a second tranch: socially conscious investors who are willing to take below-market return to participate in a progressive form of free enterprise that betters the world. At the next level, a venture can attract regular, profit-maximizing investors, whose participation at market rates is made possible by the other two tranches.

According to proponents, L3Cs facilitate tranched investing with PRIs by “usually taking first risk position, thereby taking much of the risk out of the venture for other investors in lower tranches.” Further investment then occurs as follows:

The rest of the investment levels, or tranches, become more attractive to commercial investment by improving the credit rating and thereby lowering the cost of capital. It is particularly favorable to equity investment. Because the foundations take the highest risk at little or no return, it essentially turns the venture capital model on its head and gives many social enterprises a low enough cost of capital that they are able to be self sustainable. But experts are skeptical that L3Cs will open the floodgates to billions of dollars. In addition, tranched investing raises serious policy concerns and is dangerous as a tax matter. Foundations have the privileges of tax-exempt status and can receive deductible contributions. Tranched investing runs the risk of exporting these privileges to benefit noncharitable businesses, managers, and investors.

Tax law has a term for this sort of private benefit—known as private inurement—and transactions that create private inurement can create debilitating problems for charitable organizations. Properly constructed, a tranched investment arrangement might survive IRS scrutiny, but it is dangerous to advocate tranched investing by foundations as a generic, easy, and readily available device for social progress.

3. Consider the supposed “branding” value of the L3C label. As portrayed by L3C advocates, the L3C concept, or brand, connotes simplicity, even new offerings, such as “L3Cs (or PRIs through L3Cs) for Dummies.” But applying simplicity and templates to PRIs is a dangerous impediment, not a facilitator. When a private charitable foundation makes a PRI, the decision-making process should involve careful and individualized investigation, deliberation, negotiation, and drafting.

In this realm, due diligence is a serious matter and carries risk of substantial excise taxes for foundations and managers for inaccurate claims that an investment is a PRI. An L3C is not an easy—much less an automatic—avenue to foundation PRI due diligence. Thus, contrary to the assertions of L3C proponents, L3Cs neither facilitate nor provide efficiency for foundations considering PRIs. It is misleading to those who might establish L3Cs in expectation of foundation investment to promote L3Cs as a way to bypass the situation-specific determinations that foundations must make when deciding whether a proposed investment furthers a foundation’s tax-exempt purposes and otherwise qualifies as a PRI for that foundation.
4. Finally, L3C legislation contains a fundamental drafting error. The typical L3C statute extrapolates from language in the federal regulations on PRIs and provides that “no significant purpose of the company [can be] the production of income or the appreciation of property” (emphasis added).

But how can tranched investing possibly work under these constraints? The key tranch of investors comprises those seeking a market-rate return; their investment is premised on the expectation of profit. More generally, how is it possible to have a low-profit limited-liability company when no significant purpose of the company is the production of income or the appreciation of property? Viewed against the claims of L3C proponents, the statutory language evokes thoughts of Lewis Carroll’s White Queen, who “sometimes . . . believed as many as six impossible things before breakfast.”

Rejecting the Mirage

While advocates have touted the L3C model as a low-risk, efficient, and flexible way to achieve social progress, the facts are to the contrary. PRIs are an important tool for foundations willing to devote the care and time to look wisely for “social investment” opportunities. But nothing in the L3C model creates an entity any more eligible for PRIs than LLCs without the L3C “brand.” Worse, spreading the L3C delusion could damage the concept and practice of legitimate PRIs. The L3C adds nothing and risks much. Rather than providing real benefits, L3C legislation invites simplistic thinking and fosters false hopes.

Endnotes

5. Bishop, Bishop, “The Low-Profit Limited Liability Company (L3C).”
8. 26 CFR § 53.4944-(b).
12. Treasury Regulation § 53.4942(a)-3(a)(2)(ii) recognizes PRIs as qualifying distributions to satisfy the required minimum payout of 5 percent.
13. 26 C.FR § 53.4944-3(a).
17. Americans for Community Development Web site (www.americansforcommunitydevelopment.org/history.html).
22. David Edward Spenard, “Panacea or Problem,” 131, 133.
23. Lewis Carroll, Through the Looking Glass, chapter five.

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Nonprofit Salaries: Achieving Parity with the Private Sector

by Rick Cohen

W e nonprofit workers are underpaid: true or false?

The answer is a little of both. And this idea stands in contrast to the given wisdom: that the nonprofit sector pays lower salaries but attracts workers who want vocational mission and purpose, not just compensation. The quest for purpose doesn’t always translate into lower compensation; earnings are also dictated by organizational size and occupational activity.

Still, those who work for nonprofits are likely to be paid less than their counterparts in the private sector or in government, and particularly in higher-level jobs and management. The situation is more mixed at lower levels, but the overall picture is pretty clear. Nonprofit workers frequently earn less than their private-sector counterparts, according to unpublished July 2008 wage estimates for full-time private-industry workers and workers in the nonprofit sector from the National Compensation Study (NCS) by the Bureau of Labor Statistics (BLS).

Occasionally, BLS has published broad comparisons of nonprofit, private sector, and state and local government earnings (notably the reports of BLS statistician Amy Butler using 2007 NCS data). For this article, we use unpublished data from the most recent NCS and compare full-time employees’ earnings in some 250 occupations based on the 2000 Standard Occupational Classification System and by size of establishment.

What jumps off the page—or the spreadsheet, so to speak—is that nonprofit earnings, particularly in higher-status occupations such as management and technical jobs, lag other sectors, particularly at larger employers with 100 or more employees.

Management Occupations

For “management occupations,” median earnings for workers in large nonprofit establishments (i.e., those with 100 or more employees) were $72,509, compared with private-sector median earnings of $94,628. Thus private-sector management occupations pay 30 percent more than those in nonprofits. In small nonprofit organizations (i.e., those with fewer than 100 employees), the difference is less pronounced: $68,334 for private-sector
management occupations, compared with $61,407 for nonprofit management occupations.

In organizations with fewer than 100 employees, median private-sector CEO earnings were $161,189, compared with $100,000 for nonprofits. In these small private-sector organizations, CEO salaries were almost two-thirds higher than at nonprofits. One might guess that the disparity for larger employers is much greater. While we don’t have the nonprofit-sector data, the NCS data includes overall private-sector earnings for large establishments: median earnings are $258,440, and mean salary is $419,398.

Those for-profit earnings compare with some of the larger and better-paying nonprofits, such as colleges and universities. A recent Internal Revenue Service survey of 344 institutions of higher education, for example—presumably all of which had more than 100 total employees—cites median total compensation of the highest-paid “officer, director, trustee, or key employee” between $256,000 (for medium-size organizations) and $439,000 (for large organizations). In some instances, these salaries are paid to university CFOs, treasurers, and even school deans.

Nonetheless, looks are deceiving, particularly for higher-status jobs in the private sector. In addition to wages, for-profit sector CEOs generally receive substantial additional bonus compensation and equity (i.e., stock), neither of which is generally available in the nonprofit sector.

For specific kinds of management occupations at larger employers, income disparities with salaries at nonprofits are evident (see table 1, above). But for smaller nonprofits, the disparities nearly disappear (see table 2, above).

In larger organizations and in industries such as health care and social service, some management occupations do not show significant differences. Similar compensation levels suggest that the kind of occupational activity is sometimes more significant than the nonprofit or for-profit status of an employer (see table 3, above).

While not a management occupation, the position of attorney is generally considered to be well compensated. But lawyers at nonprofits earn far less than their peers in the private sector. They show median earnings of $86,068, compared with $150,345 at larger private-sector employers. The difference is smaller for small organizations: lawyers earning a median of $78,499 in nonprofits, compared with $82,616 in smaller private-sector
Some occupations—no matter the sector—do not garner large salaries. The implication for law school graduates is pretty clear: one sacrifices income to serve a nonprofit’s mission.

Social-Service Occupations
Some occupations—no matter the sector—do not garner large salaries. The BLS compensation survey data suggests that regardless of employer tax status, workers in the social-service sector are not particularly well compensated (see table 4, above).

In this category, the most significant median earnings disparity is the comparatively higher pay of medical and public-health social employees that work for private-sector employers. Because many nonprofit jobs are in the social-service and health-care service sectors, the lower earnings of nonprofit employees characterize a larger proportion of nonprofit employment than overall private-sector employment. Moreover, these positions are often paid for largely by government grants or contracts. So legislators and public-agency directors are in a position to address and correct these lower wages.

Administrative Support Staff
In the nonprofit sector, administrative and office staff members also receive lower wages as compared with the private sector (see table 5, above).

For smaller employers, the differences are relatively small. But for larger employers, the differences are notable: secretaries and administrative assistants earn 20 percent more in large private-sector establishments.

Child-Care and Home Health—Care Occupations
In some job categories where employees are poorly paid, the nonprofit sector appears—perhaps more than private industry—to pay better.

Child-care workers are routinely poorly paid—no matter the sector in which a worker is employed. In large nonprofit establishments, child-care workers have median annual earnings of $23,021; child-care workers in private-sector industry establishments earn $22,657. In smaller establishments, earnings are even worse: child-care workers earn $19,049 in the nonprofit sector, compared with $17,680 for those in private industry.

The same generally applies to home health-care occupations, where the nonprofit sector has led the charge in improving working conditions, particularly among large employers (see table 6 on page 48).

In small nonprofits, employees earn more in these occupational categories, though in general compensation levels are lower (see table 7 on page 48).

Nonprofits probably deserve some credit for raising the incomes of home-health aides, for example. The efforts of groups such as Cooperative Home Care Associates—the first worker-owned home health-care cooperative in

| Table 4: Social-Service Earnings at Nonprofits and Private-Sector Establishments |
|----------------------------------|----------|----------|----------------|----------|
| Occupation                       | Large Nonprofits | Small Nonprofits | Large Private-Sector Organizations | Small Private-Sector Organizations |
| Social workers                   | $36,360   | $31,500   | $40,003        | $36,402  |
| Child, family, and school social workers | $31,500   | $38,542   | $35,090        | $31,812  |
| Medical and public-health social workers | $38,542   | $37,190   | $52,625        | $40,008  |
| Mental-health and substance-abuse social workers | $37,190   | $27,944   | $34,451        | $38,667  |
| Miscellaneous community and social-service specialists | $27,944   | $25,000   | $28,246        | $28,187  |
| Social- and human-service assistants | $25,000   | $31,500   | $25,501        | $25,168  |

| Table 5: Administrative Earnings at Nonprofit and Private-Sector Establishments |
|----------------------------------|----------|----------|----------------|----------|
| Occupation                       | Large Nonprofits | Small Nonprofits | Large Private-Sector Organizations | Small Private-Sector Organizations |
| Secretaries and administrative assistants | $32,760   | $35,277   | $39,520        | $35,360  |
| Executive secretaries and administrative assistants | $37,174   | $39,520   | $44,970        | $41,912  |
The high proportion of nonprofit part-timers further depresses nonprofit wages.

Table 6: Earnings of Home Health–Care Workers at Large Nonprofit and at Private Sector Establishments

<table>
<thead>
<tr>
<th>Occupation</th>
<th>Large Nonprofits</th>
<th>Large Private-Sector Employers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Personal care and service occupations</td>
<td>$21,785</td>
<td>$18,200</td>
</tr>
<tr>
<td>Personal and home-care aides</td>
<td>$19,855</td>
<td>$19,284</td>
</tr>
<tr>
<td>Health-care support occupations</td>
<td>$24,606</td>
<td>$23,829</td>
</tr>
<tr>
<td>Nursing, psychiatric, and home-health aides</td>
<td>$23,331</td>
<td>$22,776</td>
</tr>
<tr>
<td>Home-health aides</td>
<td>$20,592</td>
<td>$19,968</td>
</tr>
</tbody>
</table>

Table 7: Health-Care Earnings at Small Nonprofits and at Small Private Sector Establishments

<table>
<thead>
<tr>
<th>Occupation</th>
<th>Small Nonprofits</th>
<th>Small Private-Sector Employers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Health-care support occupations</td>
<td>$22,256</td>
<td>$26,654</td>
</tr>
<tr>
<td>Nursing, psychiatric, and home-health aides</td>
<td>$21,466</td>
<td>$20,124</td>
</tr>
<tr>
<td>Home-health aides</td>
<td>$20,925</td>
<td>$19,760</td>
</tr>
<tr>
<td>Nursing aides, orderlies, and attendants</td>
<td>$23,296</td>
<td>$20,475</td>
</tr>
</tbody>
</table>

The United States, which was founded in 1985—and the Paraprofessional Healthcare Institute (PHI), whose mission is to “improve the lives of people who need home or residential care . . . by improving the lives of the workers who provide that care,” have helped protect the incomes and working conditions of home-care workers against the intrusion of low-wage and exploitative for-profit employers in the field.

**State and Local Government Occupations**

Earnings comparisons between nonprofit, private-sector, and government-sector employers frequently lean toward higher earnings in government, though this may be attributable to the impact of public-sector unionization (see table 8 on page 49). The pattern of lowest earning levels (which are indicated in gray in table 8) suggests that nonprofit employees at management levels tend to be paid less. In some categories, particularly low-level service jobs such as home-health care and child care, the private sector pays the lowest.

In many categories, however, local and state government median earnings are higher than in other sectors (the highest-earning sector is indicate in dark green in table 8), particularly in occupational categories where the benefits of unionization through the Service Employees International Union, the American Federation of State, County and Municipal Employees, and the teachers unions, for example, are prevalent (see table 9 on page 49).

The 2009 BLS Current Population Survey counted 7.9 million public-sector workers and 7.4 million private-sector employees in unions, though the total number of private-sector workers—union and nonunion—is five times that of public-sector workers. Local-government employees (43.3 percent) demonstrate the highest rate of unionization (which also benefits nonunionized workers who are covered by union-negotiated wage standards and contracts). It pays off in earnings, as full-time wage and salary workers represented by unions had median weekly earnings of $908, compared with nonunion workers with median earnings of $710.

**Earnings of Consequence**

Nonprofit-sector employment is hardly inconsequential. The Agency for Healthcare Research and Quality in the Department of Health and Human Services counted 15.4 million employees at 534,554 nonprofit organizations. This number probably includes churches and other tax-exempt or nonprofit private-sector workplaces, in addition to 501(c)(3) public charities.

Of this total, some 25 percent—3.4 million people—are part-time employees of nonprofits, compared with less than 20 percent of employees in for-profit workplaces. The high proportion of nonprofit part-timers has two implications. One is obvious: part-time employees—many desiring but unable to secure full-time positions—earn
Nonprofits tend to provide health benefits more frequently than do private employers.

The reality is that the nonprofit sector is a sector of small organizations. If earnings equity is approximated only on occasion in the largest nonprofit establishments, the bulk of the nonprofit sector will find itself relegated to subpar compensation levels.

Table 8: Earnings in Nonprofits, Private Organizations, and in State and Local Industry

<table>
<thead>
<tr>
<th>Occupational category</th>
<th>Nonprofit Organizations</th>
<th>Private Industry</th>
<th>State and Local Government</th>
</tr>
</thead>
<tbody>
<tr>
<td>All workers</td>
<td>$36,837</td>
<td>$34,341</td>
<td>$43,139</td>
</tr>
<tr>
<td>Management occupations</td>
<td>$64,943</td>
<td>$82,772</td>
<td>$76,151</td>
</tr>
<tr>
<td>Chief executives</td>
<td>$102,076</td>
<td>$187,870</td>
<td>$111,405</td>
</tr>
<tr>
<td>Public relations managers</td>
<td>$70,400</td>
<td>$78,562</td>
<td>$68,557</td>
</tr>
<tr>
<td>Administrative service managers</td>
<td>$56,888</td>
<td>$66,194</td>
<td>$68,453</td>
</tr>
<tr>
<td>Financial managers</td>
<td>$75,000</td>
<td>$83,500</td>
<td>$81,942</td>
</tr>
<tr>
<td>Human-resources managers</td>
<td>$65,000</td>
<td>$81,286</td>
<td>$78,287</td>
</tr>
<tr>
<td>Social- and community service managers</td>
<td>$49,002</td>
<td>$47,832</td>
<td>$68,368</td>
</tr>
<tr>
<td>Community- and social-service occupations</td>
<td>$33,312</td>
<td>$34,091</td>
<td>$44,307</td>
</tr>
<tr>
<td>Social workers</td>
<td>$36,576</td>
<td>$37,500</td>
<td>$41,517</td>
</tr>
<tr>
<td>Lawyers</td>
<td>$78,499</td>
<td>$118,000</td>
<td>$77,183</td>
</tr>
<tr>
<td>Health-care support occupations</td>
<td>$24,003</td>
<td>$24,107</td>
<td>$25,130</td>
</tr>
<tr>
<td>Nursing psychiatric and home-health aides</td>
<td>$23,254</td>
<td>$21,840</td>
<td>$23,982</td>
</tr>
<tr>
<td>Home-health aides</td>
<td>$20,592</td>
<td>$19,968</td>
<td>$20,405</td>
</tr>
<tr>
<td>Child care</td>
<td>$21,590</td>
<td>$18,200</td>
<td>$20,950</td>
</tr>
<tr>
<td>Personal and home-care aides</td>
<td>$21,464</td>
<td>$20,906</td>
<td>$25,990</td>
</tr>
<tr>
<td>Office and administrative support occupations</td>
<td>$31,013</td>
<td>$30,680</td>
<td>$32,698</td>
</tr>
<tr>
<td>Secretaries and administrative assistants</td>
<td>$33,405</td>
<td>$37,440</td>
<td>$33,925</td>
</tr>
<tr>
<td>Executive secretaries and administrative assistants</td>
<td>$38,343</td>
<td>$43,539</td>
<td>$38,085</td>
</tr>
</tbody>
</table>

Table 9: Wages of Unionized and Nonunionized Workers

<table>
<thead>
<tr>
<th>Union Status/Employment Sector</th>
<th>Nonunion Employees’ Mean Hourly Earnings</th>
<th>Unionized Employees’ Mean Hourly Earnings</th>
<th>Percentage Difference</th>
</tr>
</thead>
<tbody>
<tr>
<td>All civilian workers</td>
<td>$19.89</td>
<td>$24.74</td>
<td>24.4%</td>
</tr>
<tr>
<td>Private-industry workers</td>
<td>$19.62</td>
<td>$22.44</td>
<td>14.4%</td>
</tr>
<tr>
<td>State and local government workers</td>
<td>$22.59</td>
<td>$28.18</td>
<td>24.7%</td>
</tr>
</tbody>
</table>

less than their full-time counterparts. Not only do full-time nonprofit employees earn less than private-sector workers in general, but nonprofit incomes are lower still because many employees work only part time.

The other implication involves bonuses and other perks. As noted, nonprofit employees receive far less in bonuses than do private-sector workers and next to nothing in equity.

Nonprofits, however, tend to provide health benefits more frequently than do private employers: 94.3 percent of nonprofit organizations offered health insurance, compared with 88.7 percent of incorporated for-profit organizations and 77.7 percent of unincorporated for-profit workplaces.

Many nonprofits provide staff with health benefits—perhaps to compensate for lower wage rates. But part-time employees often fail to qualify for health insurance. Despite the higher proportion of nonprofit workplaces offering health insurance, only 61.1 percent of nonprofit employees are enrolled in their employers’ health plans, compared with 62.0 percent of workers at incorporated for-profits and 58.6 percent at unincorporated for-profits. The “competitive employment advantage” of nonprofit establishments over private organizations is thus negated somewhat by the sizable number of part-time employees in the nonprofit sector.

The reality is that the nonprofit sector is a sector of small organizations. If earnings equity is approximated only on occasion in the largest nonprofit establishments, the bulk of the nonprofit sector will find itself relegated to subpar compensation levels.
The norm is that nonprofit-sector salaries simply do not compete with private-sector wages.

Toward Competitive Nonprofit Compensation

As the survey data indicates, nonprofit jobs occasionally outperform private-sector employment in compensation. But the norm is that nonprofit-sector salaries simply do not compete with private-sector wages. Nonprofit employees are more likely to accept lower wages because they gravitate toward a sector based on mission, purpose, and “doing good.”

Mission and motivation are laudable, but substandard incomes are not. Thus, a major priority of the nonprofit sector has to be wage parity with the private sector. With many nonprofit jobs paid for by government, the idea of a nonprofit sector that pays 10 percent to 30 percent less than do state and local government jobs creates a two-tiered public-service economy. At the top tier are better-compensated jobs in local and state government, and in the bottom tier are lower-earning nonprofit jobs that are often human-service jobs. The nation risks what economist Robert Kuttner calls the “casualization” of the nonprofit sector into one of low wages, long hours, and burnout, calcifying into a below–living wage nonprofit industry standard. Low compensation ought to be a campaign issue for the nonprofit sector. A reasonable and forthright standard would be one like this proposition from Kuttner. “Let’s have a national policy to make every human-service job a good job: one that pays a living wage with good benefits, and includes adequate training, professional status, and the prospect of advancement—a career rather than casual labor.”

The alternative is a vision of nonprofit jobs structured as bargain-basement earnings and compensation, which nonprofit employees often
accept because of the intangible benefits of doing good or doing God’s work. But the reality is that mission and purpose cannot offset low wages, minimal bonuses, and negligible other forms of nonwage pay.

**Endnotes**


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Unstill Waters:
The Fluid Role of Networks in Social Movements

by Robin Katcher

It is a marvel that any social movement network stays together long enough to accomplish change.

A

n individual social movement can span many generations. During that time, it is likely to face many different, complicated political contexts. As time passes, a social movement develops its analysis of a problem and changes the language and definitions of things. Often, it meets success and then encounters the next round of problems caused by the preliminary solution gained. Its members will have passionate disagreements about strategy and approach such that they part ways and new members with new views emerge. In other words, movements are living beings, affected by all manner of influences and sometimes embodying great diversity. It is a marvel, then, that any social movement network stays knit together long enough to accomplish big societal change. How do these movement networks do it?

“Networks are not social movements; but social-justice movements need networks,” says Marco Davis, a veteran network builder in the Latino community. For anyone involved in a grassroots effort to create change, this statement

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The work of the network adds up to more than the sum of its parts.

What movement-oriented networks do best, and what it takes to build and invest in them over time, often seems difficult to pin down. At Management Assistance Group (MAG), my colleagues and I have worked with organizations that are part of movement networks, those that act as network hubs, and those that come together to create new networks. Some movement networks flourish and others falter. I set out to deepen our understanding of these movement networks by reviewing the scholarly research and interviewing creative, committed leaders who have built networks, even in the most unfriendly environments.

The organic and responsive nature of networks makes them difficult to study. Networks play essential roles within movements; but how they do so and even which roles they play are not static. This fluidity causes movement networks sometimes to appear disorganized and unwieldy, which has led some to devalue their contribution and others to push for formal structure and control.

But a deeper look suggests that openness and flexibility are necessary components. Without the ability to learn, adapt, and change, these networks wither and become uninviting and ultimately irrelevant to new leaders. They lose their ability to authentically respond to political and membership complexities and ever-changing needs of movements in the context of the unstill waters of society.

The Essential Roles of Movement Networks

While there are many different types of networks, for the purposes of this article we define movement networks as the following:

1. multi-organizational: movement networks link independent organizations and activists to one another and through a central hub organization;
2. movement oriented: movement networks intentionally contribute to a broader social movement;
3. focused on the long term: movement networks stick together for the long haul and join to advance interests that extend beyond a single-issue campaign; and
4. porous: movement networks have more flexible boundaries than a formal franchise structure, such as the Girl Scouts or Habitat for Humanity. Their purpose is not to serve members alone but to meaningfully analyze, understand, and foster the development of a movement by working with and for others in the network. My research suggests that these movement networks play the following concrete and essential roles to support and contribute to their social movements.

Building linkages and connection with a broader movement. Like most networks, movement networks must foster relationships among members. But members must also see their work as fundamentally linked to that of others and as part of the larger movement. Networks “help develop a movement consciousness: thinking of self as a part of something bigger than you,” emphasizes Dan Petegorsky, a longtime network builder in the progressive movement.

Members must agree that by joining together within the network, not only do they gain benefits for their own work but also the work of the network adds up to more than the sum of its parts. Its aggregate power results in gains that...
Political frames must grow and adjust over time. A network “allows people’s knowledge, creativity, [and] strength to flourish,” says Stephanie Poggi, a network builder in reproductive health and justice. It then pulls together local knowledge and diverse experiences to create a larger understanding of the problems that constituencies face. To do so, members are asked to see themselves as part of an “us” and examine how that “us” is positioned within and contributes to the broader movement.

Deepen agreement on a shared political frame. Together members must understand, integrate, and contribute to a shared vision; align on shared values and principles; and deepen a sense of trust, belonging, and identity. According to Rachel Tompkins, a longtime leader in rural education and children’s issues, networks “need to create a value system—not just information and policy . . . building and deepening values.” More than any other factor, this shared political frame connects individuals and organizations to networks, and networks to movements. “Networked nonprofits cannot take values alignment among partners for granted,” write Jane Wei-Skillern and Sonia Marciano. “Networked nonprofits are often far more productive because they don’t have to rely on formal control mechanisms. Instead, their partners’ internal motivation and commitment drive them to work hard for the shared vision of the network.”

Those we interviewed note that building such alignment is not a one-time activity at the start of a network (though at the outset, more work may be required), nor is it simple. Political frames must grow and adjust over time. The societal problems that movements seek to address are large and complex, and so is the analysis required to build and adjust the frame. What looks like a solution to some can unintentionally affect others. Unless it’s used to spark the network to deepen and adjust its analysis, this unintended impact can erode a network’s cohesion and effectiveness.

This requires movement networks to not only bring diverse constituencies together but also center analysis on the lived experiences of those most affected by the problem the movement seeks...
to solve. Networks provide the venue for the “understanding of how constituencies of different races, ethnicities, classes, genders, sexualities, immigrant status, ability, and other historically oppressed groups are differently impacted by the same problem,” observes Darlene Nipper, an LGBT leader.

Networks help build this analysis, says Peter Hardie, an economic-justice network leader, by “pushing political questions” and “deepening people’s understanding of other parts of the movement ideology, politics, campaigns, organizations.” Networks also intend to understand the opposition, its frame, and its strategies. As Petegorsky explains, networks “need to deal with wedge issues openly and honestly. Then they can’t divide you. Look at how potential allies are pitted against one another. Watch it closely, because this will change over time.”

**Coordinate efforts, take joint action, and disseminate information about what works.** Networks facilitate and support coordinated action among organizational members. Social movements need coordinated action to build momentum, demonstrate support, and push for change. Some networks engage in coordinated action by proactively designing and leading joint national efforts with their members; others coordinate, support, and amplify the existing work of members to deepen impact.

Networks become vehicles for dissemination of messages, approaches, programs, innovation, and ideas to network members and, sometimes, to the public at large. Effective dissemination requires strong, trusting relationships among innovators and possible implementers. As Marco Davis explains, members “need to understand new models [for doing the work], and [to spread them] you need credibility and trust so members can acknowledge the value and be willing to try it themselves. You need trusting relationships in order to spread innovation and successful approaches. [The network is] not just a space for sharing convictions; you also need mechanisms and how-to’s so the parts of the network can deliberately build the movement.”

**Engage in advocacy campaigns.** Some networks develop a shared policy framework that members advance locally, while others run specific, joint national legislative campaigns, and others do both. Effective policy campaigns help “cut the issue,” give members “clear handles” to focus, and specify the complex problems movements seek to address. They also must seek to win real improvements in the lives of constituencies.

Several interviewees discussed why they believe it’s critical to advance policy through a network. “If we try to shift policy in isolation, we often make mistakes,” says Moira Bowman, an experienced organizer in reproductive justice and progressive movement building.

Interviewees say that better policy emerges through the input of diverse perspectives and that networks have an important role in developing policies and mobilizing members to win change.

Effective campaigns require a combination of seizing political opportunities when they arise and engaging in the slow, steady work of building political power that must be exploited when the moment is ripe. Networks help create the level of organization necessary, according to Petegorsky, by “develop[ing] the leaders, materials, connections that prepare people to run campaigns.” This allows networks and their members to quickly take advantage of political opportunities.

Network membership alone is often insufficient to win a specific campaign. Interviewees have found that successful campaigns require creating coalitions with those outside the traditional boundaries of the network, including unlikely allies that may agree with the network on only one issue and that have significant political influence. In this way, campaigns are an important avenue for expanding and activating network members; reaching out to those at the periphery of the movement; and building power, influence, and visibility.

Unlike other policy-change efforts disconnected from movements, winning a specific policy change is not the end goal for networks, but rather a means to the ultimate end that gets one step closer to the movement’s long-term vision. Tompkins says that it’s important to win policy campaigns, but campaigns are also “about spreading values to others in members’ communities. Winning a campaign is great, but hopefully [it’s]
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We harness all our learning and experiences to produce practical, easy-to-use resources for nonprofits.
building more long-term support for the cause. We must . . . tie policy to values so that over time people connect to a set of values beyond a specific policy.”

**Marshall and increase resources and capacity.** The strength and power of networks are derived in large part from aggregating the strength and power of members. “Our power comes from our members,” observes Diann Rust-Tierney, a leader in the criminal-justice-reform movement. “We are only as strong as they are.” Networks therefore must focus on building the organizational capacity, effectiveness, and sustainability of members individually and collectively. The role of a network is to “help organizations to do their local work and connect those leaders to a broader movement and sustain[n] their organizations over time,” Poggi says. “We walk with them through their evolution.”

For nearly all the network leaders interviewed for this research, this means helping deliver capacity-building services (i.e., technical assistance, leadership development, training, coaching, and on-site organizational development) and actively working to raise money and visibility for the network and its parts. Some organize philanthropy and make a case for why expanding giving to network members can increase a foundation’s impact. According to Tompkins, a network should help “make the parts more credible and legitimate and sustainable, especially since networks can sometimes get access to national foundation money that locals could never reach on their own.”

**Cultivate new leaders and build their identity as part of the movement.** Most movement leaders gain experience by first engaging with local organizations in their own community. But their capacity to develop concrete leadership skills, think strategically, build relationships, and broaden their own movement analysis is often enhanced by involvement in movement networks.

Leadership development efforts must ensure that critical constituencies previously excluded from leadership roles have a place at the network table. “Networks need to keep bringing in those most affected by the issue and make room for them,” Nipper says. “We should push the boundaries of the network to include constituencies traditionally marginalized.”

**Identify and fill gaps in the movement’s capacity to win.** Networks ought to build an honest and shared analysis about where the network is strong and where it lacks the capacity to be an effective player in the movement. As Bowman says, “Networks are catalysts for building capacity for movements and not just individual organizations.” Networks must thus focus on “the spaces between [organizations]” and identify “what’s the necessary leverage point to get to the next stage of movement building.” This doesn’t mean that network hubs should fill all these gaps, but it suggests that networks have an important role in helping members identify need and how it might be met.

While networks often aspire to play all these roles, they often fail to live up to their promise. The competition for resources, the pressures of building individual organizations, and the divide between national and local organizations often act as sizable barriers. So while networks can play each of these roles, rarely does one play all simultaneously.

The work of the movement network is shaped and driven by the movements they seek to support rather than only the network itself or its members.

**Beware: Calcified Structures Can Clog Network Arteries**

 Networks are complex and require balancing many varied and seemingly contradictory elements. They juggle the autonomy of individual members with the need for collective action and accountability; hold the needs and engagement of existing and emerging members; straddle political disagreements and differing approaches to the work; and balance transparency and engagement in decision-making processes with the need for efficiency and rapid responses. To get the work done and create predictability and organization, people in networks (and those that attempt to support them) tend to build structures, rules, and procedures.

The problem isn’t that we build structures; it’s that we get attached to them and believe that they will provide the glue to hold these networks
Structures get rigid, hardened, calcified. Rather than being vehicles to open space or advance critical work, they start to block the vitality of the network. “Shifts are happening minute by minute and subtly,” Nipper says. “A lot depends on where the network comes in during the movement’s development.” She pauses, then adds, “We need to ask ourselves, ‘Do structures help or hurt what the network is called to do?’”

**Fostering Flexibility**

My work suggests that networks that emphasize structure are less effective than those that adeptly learn and change. To support adaptation, interviewees sought to engaging members in some of the following:

- **Analyze the movement.** The network must consider questions such as, “What does the movement call on us to provide?” It examines the current political context, the trajectory of the movement’s own development, the opposition, and the movement’s successes and failures. It considers other actors within the movement, and looks at what is currently provided and what is missing.

- **Accept the network’s real and potential power.** For networks that seek to empower their organizations, leaders, and constituents to take action, it can be difficult to accept the political power of a network. But networks must assess where they do not have the power to effect change. Networks often skip this conversation to their own detriment. It’s almost impossible to design winning campaign strategies and build necessary capacity when networks aren’t honest about the starting line.  

- **Minimize permanent structure.** Effective networks create temporary subunits comprising members within the network that work together to advance goals and engage in certain activities. Depending on the goal, members may need to cede greater or lesser control to a key leader within the network or staff member at the central hub. In this way, aspects of networks’ work can be open and decentralized and others highly centralized. Many effective networks avoid making even the best-run units permanent; they allow them to exist for the length of the task and no longer to create room for the next task.

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Make space for marginalized and new voices. Networks that fail to give space to marginalized voices and bring in new leaders wither. In progressive social-justice movements, we must understand how societal oppression plays out within our networks. If we do not, our vision for a just future, our principles, and our values no longer ring true, and the very glue of the movement network disintegrates.

Learn from those outside their movement. When two networks from different movements come together to learn, space for creativity and increased strength opens up. Interviewees for this article were eager to learn how other networks operating within submovements developed, learned, innovated, and adapted. But in the press of their daily work, they rarely found the time to document their own approach and reach out to learn from others.

Experiment. Networks cannot seek agreement from everyone on everything; they would never get work done. Trying to get consensus not only slows the process but also drains an idea of creative juice. Networks can create an environment that welcomes small-scale experiments. Ideas come forth, and those within the network with the energy to pursue these ideas design a small experiment. If the experiment works, it will attract others over time. If it fails, scarce time and resources haven’t been wasted. As Bill Traynor writes, effective networks “resource the specific demand” and “starve bad ideas and activities that don’t have genuine value.”

Identify innovation. Networks should seek innovation and remember that it most frequently emerges from those working on the ground and closest to the issue and constituency. Poggi suggests that network leaders have to pay more attention to visionaries and innovators on the ground and be “a step ahead but without getting too far forward.” Doug McAdam echoes this sentiment and says that “peaks in movement activity tend to correspond to the introduction and spread of new protest techniques” or “tactical innovation.”

Encourage disagreement and disruption. Networks can become places for experimentation and disruption that help movements innovate and stay ahead of the opposition. “Good movements force [network] leadership to reevaluate, to see new perspectives and fresh ideas, to challenge old ways,” says an interviewee. “[You] have to fight; this is the messy part of it. The very innovation that starts well and gets established can get in the way. Upheaval is good.”

Change does not always fit neatly into a structure or a process, but seeing the need for it and the ability to harness the creative opportunities that come with change are essential. “The art of leadership in today’s world involves orchestrating the inevitable conflict, chaos and confusion of change so that the disturbance is productive rather than destructive,” write Ronald Heifetz, Alexander Grashow, and Marty Linsky.

Create time and space for reflection. Network leaders need to build in opportunities to reflect on past efforts and integrate them into the culture of the network. It’s critical to include the insight and experiences of those directly affected by the problem that a network seeks to address.

Networks benefit from cultures that honor strategic risk taking and appreciate mistakes as opportunities to learn. They benefit from asking, “Could we have greater impact if we did something differently?” Networks ought to be “less concerned with making ‘correct’ decisions than with making correctable ones; less obsessed with avoiding error than with detecting and correcting for error,” writes Robert Reich, a professor at the University of California, Berkeley.

Connect and align action with vision. While networks seem to learn and adapt best in flexible environments, they also need to consciously build unity, loyalty, and connection to keep members of the network together. The ongoing development and recommitment to shared vision, values, and long-term goals is essential. “When networked nonprofits share the same values, they do not have to try to manage for every contingency” and are less apt to “exert control to ensure quality,” write Wei-Skillern and Marciano.

Accepting the Organic Nature of Networks

The highly adaptive nature of networks that seek to contribute to and support social movements challenges the past 30 years of traditional thinking on what it takes to build and develop nonprofit networks benefit from cultures that honor strategic risk taking and appreciate mistakes as opportunities to learn.
organizations. If we want to support the development of social movements, we must understand not only individual organizations but also what it takes for them to come together in strong, fluid, adaptive, and effective networks. This requires us to embrace the often messy process of creating and growing networks and to engage in more thinking and discussion to better understand what supports movement networks’ learning and adaptation so that they can answer the call at each critical moment.

ENDNOTES
4. Ibid.
6. Doug McAdam, “Tactical Innovation and the Pace of Insurgency.”

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Not Paying Your Taxes? Your Board Could Be Personally Liable

By Francis J. Serbaroli

If a nonprofit fails to pay taxes, the IRS may go after individual board members and executives to repay the money. Don’t fall prey to this fate.

In the face of the current economic downturn, many nonprofits have found themselves in dire financial straits. Contributions have plummeted and endowments have dwindled, while the need for these charities’ services has continued to grow. In the event of a cash shortage, even a charity with the best intentions may be tempted to delay tax payment or “borrow” its employees’ federal withholding taxes and use that money to meet other needs.

But charitable organizations should avoid this temptation at all costs. In seeking payment of these taxes, the Internal Revenue Service (IRS) will pursue not only a charity’s assets but also the personal assets of individuals who were directly or indirectly associated with a nonpayment of taxes.

Here we explore the critical lessons to be learned from cases in which nonprofit board members and executives have been held liable for a nonprofit’s failure to remit taxes. If you’re a board member or executive with ties to the purse strings, here’s how to avoid getting into trouble.

The Law
The law concerning nonpayment of withholding taxes is clear and unambiguous. The Internal Revenue Code (or “the Code”) requires employers to withhold federal income and Social Security taxes as well as Medicare and Federal Insurance Contributions Act (FICA) taxes from employees’ wages. The Code classifies these funds as held by employers in trust for the United States and specifically prohibits employers from using these funds for operational or business expenses.

The Code provision that holds individuals personally responsible for nonpayment is broadly worded: “Any person required to collect, truthfully account for, and pay over any tax imposed by this title who willfully fails to collect such tax, or truthfully account for and pay over such tax, or willfully attempts in any manner to evade or defeat any such tax or the payment thereof, shall, in addition to other penalties provided by law, be liable to a penalty equal to the total amount of the tax evaded, or not collected, or not accounted for and paid over.”

The Code’s definition of a “person” includes any officer or employee of a corporation who has a duty to collect, account for, or pay withholding taxes.

If an individual falls into one of the following categories, there is a fig leaf of protection for unpaid volunteer board members of tax-exempt organizations:

• the individual serves solely in an honorary capacity;
• the individual does not participate in day-to-day or financial operations of an organization, and
• the individual had no knowledge of the failure on which a penalty has been imposed.

Still, the provision goes on to state, “The preceding sentence shall not apply if it results in no person being liable for the penalty imposed by subsection (a).” Thus, if the IRS cannot assess against a liable party, even the fig leaf disappears.

An individual found personally liable for nonpayment of taxes must pay the IRS, but he can then take legal action to share the pain with others. “If more than 1 person is liable for the penalty,” the provision states, “with respect to any tax, each person who paid such penalty shall be entitled to recover from other persons who are liable for such penalty an amount equal to the excess of the amount paid by such person over such person’s proportionate share of the penalty.”

Real-World Cases
Last year two federal court decisions were the latest in a line of cases in which the IRS has successfully held board members and executives of charitable organizations liable for misuse of withholding taxes that should have been remitted to the government.

In Doulgeris v. United States, a federal district court held the president
of a charitable nonprofit hospital personally liable for the hospital’s unpaid withholding taxes. James Doulgeris served as the interim president and CEO of Granada Hills Community Hospital (GHCH), a bankrupt facility in Florida. When Doulgeris arrived, GHCH was already delinquent in paying its withholding taxes, and Doulgeris was aware of the problem. The CEO had authority to write checks on the hospital’s accounts, including those for “payroll” and “taxes.” As interim president, he signed some 57 checks that totaled $2.9 million and were payable to creditors, even though he knew that the hospital had been delinquent in paying withholding taxes.

When the IRS took action, Doulgeris claimed that he merely signed checks prepared by GHCH’s chief financial officer and that he was not in control of whom the hospital paid. Nonetheless, the court held him personally liable for the full amount owed: more than $1.93 million. Doulgeris then filed suit in federal court seeking relief.

The court held that Doulgeris was responsible for paying taxes owed to the government and could not shirk that responsibility by delegating it to others. The court noted that Doulgeris (1) knew that payroll taxes had not been paid to the government; (2) had the authority to make payments on behalf of the hospital; (3) signed checks to pay other creditors despite knowledge that the hospital was delinquent in tax payments; and (4) had the power to directly transfer hospital funds to the government and had previously done so. The court concluded that Doulgeris willfully failed to pay withholding taxes to the government, upheld the IRS’s findings, and awarded the IRS the full amount of unpaid taxes.

In Verret v. United States, the IRS went beyond a charitable organization’s management and reached directly into its boardroom. A federal district court in Texas upheld the IRS’s determination that the chairman of a nonprofit hospital’s board of trustees was personally liable for the hospital’s nonpayment of withholding taxes.

Stephen Verret had been the chairman of the board of Doctors Hospital in Groves, Texas. In 2001, as the hospital’s financial condition deteriorated, Verret was informed by the hospital’s executive director, David Cottey, that the hospital had failed to remit to the IRS some $400,000 in withholding taxes. Verret immediately arranged for the hospital to satisfy this tax liability with borrowed funds. Verret and the board informed Cottey that under no circumstances should the executive director fail to pay these taxes again. Thereafter, when the board repeatedly inquired about the taxes, Cottey reassured board members that the hospital’s remission of its withholding taxes was current. But Cottey ultimately informed Verret and the board that withheld income and FICA taxes for the third and fourth quarters of 2001 had not been paid to the government. In 2003 the hospital filed for bankruptcy.

The IRS commenced an action against Verret, Cottey, and the hospital’s chief financial officer, Angela Massey, and held them as “responsible parties” for the hospital’s failure to pay withholding taxes. The IRS settled with Cottey and claimed that Massey owed $182,000. The IRS assessed a penalty of more than $407,000 plus $1,821 of interest against Verret, who paid the assessment and then filed suit in federal district court to obtain a refund.

The court noted that for personal liability purposes, the crucial inquiry in determining a responsible party is whether an individual has the power to pay the withholding taxes: that is, whether an individual “actually could have ensured the satisfaction of the tax obligations.” According to the court, factors that determine whether an individual is a responsible party include the following:

- Is the individual an officer or member of the board of directors?
- Does the individual own a substantial amount of stock in the company?
- Does the individual manage a business’s day-to-day operations?
- Does the individual have authority to hire and fire employees?
- Does the individual make decisions on the disbursement of funds and payment of creditors?
- Does the individual have the authority to sign company checks?

Although Verret claimed that the board lacked the authority to dictate which bills should be paid, the court observed that the hospital’s corporate bylaws gave the board final authority over numerous matters, including reviewing the performance of the executive director, who had misled the board about the payment of taxes. Another crucial consideration was Verret’s intimate involvement with the hospital, which included the following activities:

- Verret’s 26-year-tenure as a board member and his position as board chairman at the time the taxes were not paid;
- his involvement in the development of new cash-flow strategies for the hospital;
- his frequent presence at the hospital;
- his daily discussions with the executive director;
- his authority to sign checks on hospital accounts;
- his action to ensure payment of delinquent withholding taxes on a prior occasion;
- his signature on the hospital’s IRS Form 990; and
- his authority, along with the board’s, to hire and fire the executive director.

The court rejected Verret’s arguments that he exercised no power, authority, or control over the actual payment of the
The following story details how a small nonprofit arts organization survived a potentially deadly financial crisis and successfully negotiated a payment plan with the IRS concerning unpaid payroll taxes and filing penalties.

An eight-year-old arts organization had a budget of slightly less than $200,000 annually, six volunteer board members, and five paid staff members, all of whom were artistic, with the exception of the organization’s managing director.

The managing director intentionally misled the board about the organization’s financial condition. When it came to managing the organization’s finances, the managing director was well meaning but out of her depth.

With the organization already facing a cash-flow challenge, a project that involved a national touring artist went well over budget. To resolve the situation, the artistic director gave the organization a personal loan of approximately $25,000. The organization continued to thrive artistically but struggled to rise above what was perceived as moderately challenging financial circumstances.

At each board meeting, the board received Excel spreadsheets containing financial reports, which the managing director had created. The board treasurer position was vacant, and no additional financial oversight had been put into place. Then the financial crisis hit.

### The Time Line of a Crisis

<table>
<thead>
<tr>
<th>Date</th>
<th>Event Description</th>
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<tbody>
<tr>
<td>JULY 2000</td>
<td>The organization’s managing director announces her resignation, citing that she has “outgrown” the organization.</td>
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<tr>
<td>FALL 2000</td>
<td>All artistic members are assigned administrative duties, in addition to their artistic duties. These combined roles continue to this day.</td>
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<tr>
<td>OCTOBER 2000</td>
<td>The organization receives $20,000 from its largest grant funder to fund a part-time financial consultant for one year. The consultant presents a plan to untangle the financial mess, manage the organization’s finances, and develop best practices. The plan includes developing financial procedures, securely a line of credit, improving quality and frequency of financial reporting, and training administrative staff on financial management. The board and staff also develop a fundraising plan, including a strategy to approach the organization’s major grant supporters to candidly explain the situation and outline the steps for resolution and prevention. Board members are charged with securing emergency funds from potential major donors.</td>
</tr>
<tr>
<td>DECEMBER 2000</td>
<td>Filings to the state attorney general’s office are now up to date.</td>
</tr>
<tr>
<td>JUNE 2001</td>
<td>The organization sends a letter to the IRS documenting the events that led to the crisis. The organization also provides minutes that document the board’s lack of knowledge about the organization’s financial crisis.</td>
</tr>
<tr>
<td>AUGUST 2001</td>
<td>The IRS demands a second meeting. Despite making payments, the organization is informed that the IRS will begin a “trust-fund penalty case” of approximately $30,000 against parties that it deems responsible for unpaid payroll taxes. The board chair contacts a consultant to act as the intermediary in negotiations with the IRS. The intermediary forestalls trust-fund penalty action and helps the IRS to understand that the organization is taking action to repay the outstanding principal in full.</td>
</tr>
<tr>
<td>APRIL 2002</td>
<td>The lender accepts the loan, and the organization makes an offer to the IRS via the consultant for repayment in full of all back taxes, penalties, and interest owed.</td>
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</table>

Shelly Chamberlain is the manager of operations and human resources at the Minnesota Council of Nonprofits.
hospital’s accounts and held that he had personal liability if he merely possessed the effective power to pay the taxes. The court found that when a responsible person clearly should have known and was in a position to find out easily that there was a grave risk that withholding taxes were not being paid, that person acts with reckless disregard and, thus, willfully for purposes of liability. It also explained that the Code’s imposition of personal responsibility is intended to have a prophylactic effect and to encourage multiple responsible persons, including officers, directors, and high-level employees, to stay informed of the timely payment of all withholding taxes to the government.

Lessons to Be Learned

There are several lessons to be learned from cases where individuals have been held personally liable for a charity’s unpaid withholding taxes.

Lesson one. The IRS has repeatedly demonstrated that it will aggressively seek to tag board members, executives, and employees as “responsible persons” and hold them personally liable for unpaid withholding taxes. Absent strong evidence to the contrary, federal courts usually agree. The IRS has also repeatedly demonstrated that it will treat charitable organizations and nonprofits no differently than their for-profit counterparts. Nonprofit executives should heed this warning: courts are prepared to mete out harsh punishment to individuals regardless of the 501(c)(3) status of the organizations they oversee.

Lesson two. Virtually any alternative—including taking on additional debt, restructuring, downsizing, and filing for bankruptcy—is better than failing to remit withholding taxes to the government.

Lesson three. Board members, executives, and employees who fall within the Code’s definition of a responsible person

AUGUST 2000: The organization hires a contract financial consultant to handle the organization’s financial management. Three days after the consultant begins work, the crisis emerges. The consultant discovers unfiled tax returns and unpaid payroll taxes, unopened notices from the IRS, unopened bills, and accumulated credit card debt.

SEPTEMBER 2000: A full financial picture emerges. It is determined that the organization owes approximately $72,000 to its creditors, including $35,000 in unpaid payroll taxes to the state and federal governments; $17,000 in accumulated credit card debt; and $20,000 in preexisting long-term debt. The two previous Internal Revenue Service Form 990s had been filed six and nine months late, respectively, and the required filings with the attorney general’s office had not been filed. The board agrees to meet monthly until further notice.

NOVEMBER 2000: Quarterly payroll tax filings that had not been filed previously are filed, and the IRS promises to contact the organization about repayment. A payment plan is arranged with the state Department of Revenue.

MAY 2001: The IRS demands a meeting with staff. The organization is encouraged to begin to make payments, regardless of the status of the IRS’s action. It is later determined that these payments have been applied only to interest and penalties owed, not to the principal.

JULY 2001: The organization makes a formal request to the IRS for abatement of penalties for late filings of both Form 990 for the prior two fiscal years and unfiled Form 941s.

SEPTEMBER 2001: The organization applies for a loan to cover repayment of all outstanding payroll taxes owed to the IRS.

MAY 2002: The IRS accepts the organization’s offer for repayment of payroll taxes in full, and the trust fund penalty case is dropped.

2010: Today the organization is thriving artistically and structurally. The organization is well respected locally and nationally and has seven paid staff (including a new managing director), has instituted financial accountability procedures, and has grown its budget to $450,000 annually. All the original debt has been paid off.
should actively ensure that their nonprofit has remitted all withholding taxes to the government on time.

**Lesson four.** If you are in a position to do something about unpaid withholding taxes, the fact that you are a voluntary, uncompensated board member of a charitable organization affords you little protection. Because the definition of a responsible person is so broadly worded, the IRS can hold any of the following personally responsible:
- a chairman of the board;
- board officers and board committee chairs (e.g., the finance committee);
- a president or CEO;
- a CFO;
- a controller; and
- other officers or employees responsible for payment of withholding taxes.

In determining a responsible person, job titles matter less to the IRS than do the duties and authority of a given position.

**Lesson five.** Pointing the finger at other board members, executives, and employees doesn’t shift responsibility. The IRS wants its money and will attempt to recover it from those it identifies as responsible persons. As noted previously, once the IRS has been paid in full by one or more responsible persons, the law leaves it to these individuals to fight it out among themselves.

**Lesson six.** Corporate bylaws should carefully delineate the responsibilities of a governing body versus those of management. These cases underscore the importance for nonprofit board members and executives to know their proper roles and responsibilities. In the Verret case, for example, had the board chairman not been so intimately involved in day-to-day operations—even to the point of signing hospital checks—the outcome might have been different.

**Lesson seven.** Directors’ and officers’ liability insurance coverage should include indemnification of individual board members and senior executives for liabilities incurred by a charitable corporation.

The bottom line is this: The IRS doesn’t want to discourage service on the boards of charitable organizations. But the IRS wants its money and will get it any way it can and from whomever it can prove was a responsible person. Board members and senior executives of any charitable organization should be vigilant in ensuring that an organization is current in all its payment obligations to taxing authorities.

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**Endnotes**

1. 26 U.S. Code Sections 3102(a); 3402(a).
2. 26 U.S.C. Sections 7501(a).
3. 26 U.S.C. Sections 3102(b), 3403, 7501(a).
4. IRC Sec. 6672(a).
5. IRC Sec. 6671(b).
6. IRC Sec. 6672(e).
7. IRC Sec. 6672(d).
10. Verret’s relationship with the hospital was not entirely voluntary. He was also paid by the hospital for consulting services; his company was a providing vendor to the hospital, and his wife was employed for several months as the chief operating officer of the hospital.

**Francis J. Serbaroli** is an attorney and shareholder in the New York office of Greenberg Traurig LLP, an 1,800-lawyer multinational law firm. For more than 30 years, Serbaroli has advised and represented charitable nonprofit organizations.

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Dear Dr. Conflict,

I am the executive director at a small but dynamic nonprofit. Two months ago, my board informed me that it would launch a search for my replacement. Our organization has been through a rough couple of years after the previous administration left and created a severe budget deficit of nearly 20 percent of the total.

After I recognized the need for new skills on the board that some members lacked, I recruited local business people, who in turn recruited additional members. Unfortunately, for this group, micromanagement has been the rule of thumb over the past 18 months. The mostly absent board leader does not advocate a teamwork ethic and has undermined my authority with board members and staff.

It is now commonly acceptable for board members to have conversations with staff about other staff members, about department heads, and about me. Unfortunately, a few staff members are quite comfortable with this arrangement and often exploit it. At this point, I have little authority with staff.

I have sent out my résumé but have not received solid feedback. I do not want to leave this organization because I still believe in its mission and am proud of my contribution to turning things around. But I fear that too much dysfunctional behavior has made it very difficult for me to successfully fill a different position in the organization.

Woe Is Me

Dear Woe Is Me,

To be frank, there may be very little you can do now. You regrettably missed several chances to “nip it in the bud,” as Barney Fife used to say. That’s because you forgot a fundamental law of nature and leadership.

Although there is debate about the origin of the concept—some say it was the philosopher Parmenides, others attribute it to Aristotle—you got into this mess because nature abhors a vacuum. Remember that eighth-grade science experiment in which a teacher put a dab of shaving cream into a vacuum jar and then pumped out the air? How the shaving cream grew into a massive blob and filled the empty space? And how the blob dissipated when the air was let back in?

Now imagine you’re inside that jar. Instead of shaving cream, there are micromanaging, chain-of-command-breaking board members. The more you avoid them, the more they expand their influence until you are obliterated. Do you get the picture? Your avoidance created the blob that ate your nonprofit and your job. In other words, human nature abhors a vacuum.

If there’s a vacuum in the leadership of a nonprofit, especially when a major problem arises, an executive director must act quickly or someone else will. That someone might be a board member, a staff member, a funder, or even the press. But trust Dr. Conflict: someone always fills a vacuum.

Some may think that leading by example—walking your talk—is enough to stop bad behavior. “If my board members and employees see that I respect the chain of command, they’ll do it too,” the thinking goes. But this greeting-card leadership doesn’t deliver and certainly doesn’t fill the vacuum. When you see something major go wrong in your agency, you have to take action. Walking the talk of good behavior is fine, but to be truly effective and fill the vacuum, you...
must also actively oppose bad behavior. You had two opportunities to oppose the bad behavior of your board members. First, when you recruited these skilled board members, you missed the chance to explain the rules. "But surely," you say, "board members know that disrespecting the chain of command is a bad thing." Last time Dr. Conflict checked, clairvoyance was an elusive art practiced only by the Amazing Kreskin. Your board members may be a lot of things, but they aren’t mind readers. Neither is your staff.

You can be excused for not establishing the rules up front; only a rare board clarifies its guidelines of behavior. Oh, sure, most boards have job descriptions for the board, and a good number also have them for board members. But how many have guidelines of conduct? After all, it is one thing to say board members have a duty to raise funds and quite another to say that they should respect the chain of command.

This is why Dr. Conflict recommends that boards craft guidelines of conduct for themselves, for committees and officers, for board members, and for the executive director. Taking the time to do so—and it doesn’t take much—is the low-hanging fruit of better boards. This way you have the rules to explain up front and it becomes much easier to address the problems. "Remember at our meeting before joining the board and then again at the orientation when we talked about micromanagement and chain of command?"

Second, you missed the chance to address the micromanagement and accountability breaches when they first arose. Plenty of conflicts are worth avoiding, including those that don’t matter (i.e., when aggressive telemarketers call, just hang up) and some that do (i.e., when assaulted by a mugger with a gun, give up your wallet). But micromanagement and breaking the chain of command don’t fall into the don’t-matter category.

With or without guidelines in place, you should always use Dr. Conflict’s Secret Number One to get issues out in the open. Conflict begins with the word you and ends with I. When you raise the issue, use statements that begin with I. When you start with you, others are likely to be put on the defensive. "You’re overstepping your authority when you go around my back to my staff members" will raise hackles, as opposed to "I am concerned that my staff members are becoming confused about whom they work for.”

When you describe the problem behavior—as specifically as possible—continue to use I statements. Include what has happened as a result of the behavior, which can include how it makes you feel. Remember that you want to enlist the other party to help you, and you can’t do that with you statements and generalities. The remarkable thing about I statements is they often beget I statements from the other party. That’s because I statements require self-disclosure, which in turn builds trust that naturally elicits reciprocation.

There’s nothing you can do now about most of what has happened. But you can try to move forward. Your best bet is to begin with the board chair and with the best I statement of all: “I need your help.” And then use more I statements to find a way to move forward.

Dr. Conflict is the pen name of Mark Light. In addition to his work with First Light Group (www.firstlightgroup.com), Light teaches at the Mandel Center for Nonprofit Organizations at Case Western Reserve University. Along with his stimulating home life, he gets regular doses of conflict at the Dayton Mediation Center, where he is a mediator.

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by the editors
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Jon Pratt
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Daniel S. Kleinberger
Limited-liability corporations (L3Cs) are supposed to combine charitable giving and for-profit investing. In many philanthropic circles, L3Cs are the new darlings, touted as solid alternatives to traditional philanthropy—and without the hassle. But opponents charge that the model is dangerous and no more effective than traditional charitable giving.

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Francis J. Serbaroli
If an organization fails to pay its taxes, legal precedent may allow the IRS to hold board members responsible for repaying the money. But you can dodge the bullet of personal liability.

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Shelly Chamberlain
In this case study, the author reviews how a mismanaged nonprofit organization emerged from a mountain of debt to the IRS and revised its management practices along the way.

Dr. Conflict
Mark Light
A micromanaging board has stepped in to address what it perceives as a power vacuum, and now the executive director’s job is threatened. The only antidote, counsels Dr. Conflict, is action.
Phil Anthrop, continued from page 72

and community—that build authentically great organizations,” Satveer said.

Taking a page from Daniel Pink’s new book, Drive: The Surprising Truth about What Motivates Us, the Meaningful Purpose Foundation publicly asked corporations to kick out their paid consultants and contemplate a new model for compensation.

After considering a roster of candidates, MPF chose AIG as its first pro-bono engagement. Following the collapse, the public vitriol over AIG bonuses spilled over to the end of executives’ driveways, where protesters shouted and waved signs. While AIG was a ward of the state, almost all bonus recipients felt pressured to forgo half of their millions in bonuses—only to later unanimously rescind their give-back pledges. AIG was a poster child for how out of whack the entire field of corporate compensation had become.

AIG’s reaction to the Meaningful Purpose Foundation’s recommendations was quite bitter.

“That’s when we realized that corporate America had a lot to learn from the nonprofit sector in how to reasonably motivate people, pay them fairly with good benefits, and, mostly, to offer equal amounts of encouragement and succor alongside moderate amounts of cash and equity,” Haddad said.

The Meaningful Purpose Foundation launch event was a mirror image of the Corporate Philanthropy Day event in New York City, with 20 nonprofit HR directors pledging $10 million in free consulting time to help struggling banks get back on their feet. Speaking at the dinner at Trump Plaza, Chad Wilson, the volunteer lead on the AIG project, and the director of human resources for Community Services, Nashville, announced their recommended compensation plan for AIG:

- Eliminate commissions on sales
- Readjust salary bands so that the ratio of compensation from the top to the bottom is no more than 100:1
- Eliminate compensation for board directors (other than reimbursement for expenses)
- Provide one-on-one coaches to corporate board members (e.g., volunteer nonprofit board to buddy up and talk public service).

According to Wilson, “Highly accomplished nonprofit boards attract top talent and have no need to compensate their university or major art institution trustees. When corporate boards stop paying their boards beyond reimbursement for expenses, the conflict of interest surrounding compensation will diminish. Clearly corporate board members, including the so-called independent board members, don’t want to be seen as beholden and unwilling to question management.”

- Create bonus schedules based on 720-degree evaluations, with equal weight given to opinions of panels of community members in communities affected by corporate operations.

“The entire field of corporate compensation consulting has been corrupted and needs to be replaced with nonprofit advisers and legitimate, evidence-based compensation surveys,” Wilson said.

AIG’s reaction to the Meaningful Purpose Foundation’s recommendations was immediate and quite bitter.

“Who are these people?” one former AIG bond trader who requested anonymity complained. “And what exactly do they know about our business? It’s fine if they want to drive Volkswagen Beetles and send their kids to public schools, but don’t impose your life on us! I don’t work 80 hours a week to make other people feel better. This is pathetic!” This reaction echoed the bulk of the feedback the foundation received. AIG management scheduled a meeting but later canceled it and the board of directors declined to meet, citing a conflict of interest.

“These industries are hard to change, especially financial services.”

—John Crosby, professor of international relations

The altruistic impulse on the part of the nonprofit volunteers, who only wished to make finance a more humane work environment for its workers, was lost on the banking community.

“These industries are hard to change, especially financial services,” concluded industrial relations professor John Crosby, the author of Compensation and Incentives: Practice Fails to Apply to Theory. “Despite some excellent conceptual work on the rewards of life, almost all our research shows that a substantial part of the population places a greater value on money than on human relationships. They just really, really like it.”

“Nevertheless, I hope the Meaningful Purpose Foundation will keep raising these compensation issues, but maybe with a different occupational group,” Cosby concluded. “Perhaps with musical instrument makers, organic farmers, or even philanthropists.”

Phil Anthrop is a consultant to foundations in the G8 countries.

To comment on this article, write to us at feedback@npqmag.org. Order reprints from http://store.nonprofitquarterly.org, using code 170209.
International Corporate Philanthropy Day in New York City was an irony and an inspiration. A celebration of worldwide business generosity was held shortly after the same lauded corporations were scorned for their shortsighted greed and blamed for the Great Recession. The fact that following the downturn there had been no apparent change of heart led a group of enterprising volunteers to come to the aid of the financial services industry in an unexpected way.

“When we saw the painful circumstances of the TARP [Troubled Asset Relief Program] recipients and their public struggle with how to fairly compensate their hardworking bond traders, we knew it was time to give back to those who gave so much advice to us,” recalled Jennifer Haddad, the director of human resources for Habitat for Humanity International.

“Surely what we have learned from millions of volunteers is that money alone does not build great organizations. The carrot and stick have failed. Americans yearn for purpose-driven lives,” —Jennifer Haddad, director of human resources, Habitat for Humanity International

After the banking meltdown and its aftermath, with the embarrassing scene of billion-dollar New York banks skulking to Washington hat in hand, Haddad and other charity leaders felt a duty to give back. America’s nonprofits had benefited so much from the free, unsolicited advice they had received for years from these corporations.

Bringing Purpose to the Financial Sector

In 2010 the Meaningful Purpose Foundation (MPF) launched to offer confidential technical assistance to reengineer corporate compensation structures, bringing motivational concepts refined over the past 10 years by innovative nonprofits as well as Silicon Valley–based startups. Newly appointed Meaningful Purpose Foundation CEO Rinal Satveer noted that “corporate philanthropy has long combined pro-bono consulting help to improve the management of nonprofits with their cash gifts and in-kind contributions and volunteers. In our case, MPF will zero in on strategic HR and compensation consulting for the financial services industry.”

While nonprofit organizations have grumbled good-naturedly about corporate volunteers that behaved as though virtually any corporate executive was inherently qualified to give any nonprofit organization management advice on any subject, Haddad and Satveer wanted to avoid any hint of presumption by adopting a narrow mission.

“These corporations have a right to learn that people are not motivated primarily by material things; that only cheapens the employer relationship. Million-dollar bonuses have never achieved the intended result—only a desire for more and more—as we saw from the abominable judgment and rank perfidy rife in the ranks of AIG, Bear Stearns, and Countrywide Financial. At the end of the day, it is intrinsic reward—such as meaning, autonomy,
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