Stanford SOCIAL INNOVATION REVIEW

Summer 2009 Volume 7, Number 3

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Mission-Driven Governance
By Raymond Fisman, Rakesh Khurana, & Edward Martenson
Page 36

Platforms for Collaboration
By Satish Nambisan
Page 44

The Hidden Costs of Cause Marketing
By Angela M. Eikenberry
Page 50

Ethics and Nonprofits

How nonprofit leaders can promote ethical behavior within their organizations.
By Deborah L. Rhode & Amanda K. Packel
Page 28

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Stanford Social Innovation Review

Ethics and Nonprofits | Mission-Driven Governance | Platforms for Collaboration | The Hidden Costs of Cause Marketing

Summer 2009 | Vol. 7, No. 3

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Contents › Features

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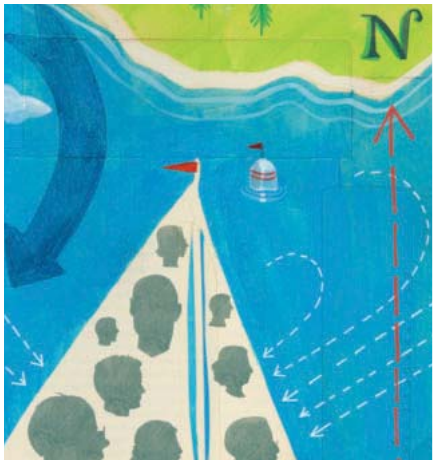
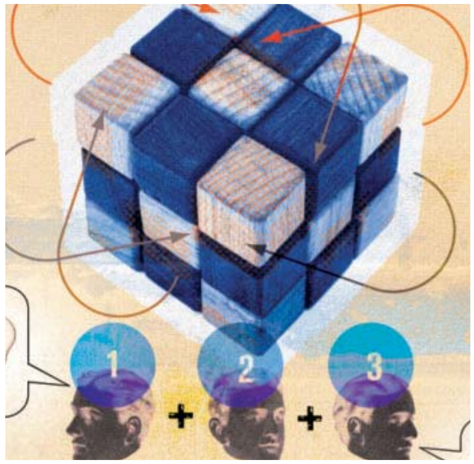


▲ P.36



▲ P.44

▲ P.50

ON THE COVER: Illustration by Richard Mia

Contents > Departments

▲ P.7

▲ P.13

▲ P.25

▲ P.68

ON THE WEB
www.ssireview.org

Bloggers
Mario Morino, chairman of Venture Philanthropy Partners, explains why the United States must become more socially *and* commercially innovative if it is going to maintain its status in the world.

Podcasts
Listen to a fascinating discussion about ways to end world hunger, featuring Goldman Sachs vice chair Robert D. Hormats, CARE president Dr. Helene Gayle, and Acumen Fund CEO Jacqueline Novogratz.

Feedback
Angela M. Eikenberry provides a biting critique of cause marketing in "The Hidden Costs of Cause Marketing." Are her criticisms valid or are they simply utopian? Go to *SSIR*'s Web site and weigh in.

PARKING

By *James A. Phills Jr. & Eric Nee*

Social Innovation Gathers Steam

Seeing President Obama establish the new White House Office of Social Innovation and Congress establish the Social Innovation Funds Pilot Program not only lifted our hearts, but reinforced our confidence in the potential and power of the idea of social innovation. As much as we are tempted, we will resist overreaching by trying to take credit for these historic advances. Nevertheless, we do—with some pride—point out that it was in the spring 2008 issue of the *Stanford Social Innovation Review* that Obama advisor Michele Jolin first laid out a proposal to create such an office. And it was in the fall 2008 issue of *SSIR* that academic editor Jim Phills grilled pundit, former presidential advisor, and Harvard University professor David Gergen on what he would do as director of a prospective "office of social innovation."

Although we take satisfaction in these recent events, we also want to offer our own friendly amendment to these admirable initiatives. Specifically, we take issue with the legislation establishing the social innovation fund that explicitly limits its scope to "social entrepreneurs and *other* [italics added] nonprofit community organizations in tackling national and local challenges." Although there are no doubt practical challenges involved in allocating public funds to organizations that are not 501(c)(3)s, we believe that defining social entrepreneurs or innovators as only nonprofit community organizations will limit the sources and kinds of innovative solutions the funds can support. (See "Rediscovering Social Innovation" in the fall 2008 issue of *SSIR*.)

Gergen clearly endorses *SSIR*'s cross-sector approach to innovation, eschewing the notion that social entrepreneurship or social innovation should be defined in ways that exclude for-profits, public institutions, or large established nonprofits. In his *SSIR* interview, he cautions: "There are those who believe that social entrepreneurs should by definition be nonprofit. I don't share that view. ... Many people in traditional larger nonprofits have taken offense at the notion that you are a social entrepreneur only if you're new. ... In truth, a lot of people have committed themselves to social change and have done great work. They should all be celebrated and seen as partners in the larger struggle."

Despite our quibble with the legislation, we laud the federal government's objectives. These include (quoting directly from the legislation) the following goals: "Leverag[ing] federal investments to increase state, local, business, and philanthropic resources to replicate and expand proven solutions." "Increas[ing] private and public investment ... [to] allow [effective] organizations to replicate and expand proven initiatives or support new initiatives." "Seeding experimental initiatives focused on improving outcomes." And "Strengthen[ing] the infrastructure to identify, invest in, replicate, and expand initiatives with effective solutions to national and local challenges."

As editors of a journal of ideas we obviously believe in the power of language—that words matter. That is why we are so pleased to see our political leaders' growing embrace of the term *social innovation*. It is a clear indication that in the war of ideas, the idea that we believe offers the most potential—social innovation—is making significant headway. ■

Stanford SOCIAL INNOVATION REVIEW

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Raising Money

Congratulations for publishing "Ten Nonprofit Funding Models" (*SSIR*, vol. 7, no. 2, p. 32). The article does a good job of describing the various funding models that an NGO can pursue. I have found that to create a robust fundraising and partnership program for my organization (which has revenues of more than $100 million annually, more than 90 percent of which comes from fees), I have also had to spend a lot of time understanding my organization's tolerances for various funding models. Some of the variables I have had to analyze are the following ones.

Appetite: What is the appetite for fundraising within my organization? Do I have to raise a lot of money very quickly, or is there time to build a foundation for giving?

People: What are the human resources available in my organization now? What resources and skills will I be able to draw upon in the future?

Information Technology: Can my organization's IT infrastructure support fundraising that requires high data resources? Can our fundraising create more support for IT?

Finance: Can my organization's finance infrastructure support complex financial transactions? Can it support a lot of transactions? Can it support transactions in multiple currencies or in multiple jurisdictions?

Legal: Can my organization's legal infrastructure support multi-country approaches? Can it undertake partnerships? Can it work within the tax guidelines of multiple countries? Will transactions in one country affect its work in another?

Communications: How flexible is my organization in massaging its message to meet the needs of different audiences?

Project Management: What is my organization's capacity for absorbing new donor-funded projects?

Intangibles: Are there unspoken metrics for success within my organization that I need to consider, such as having a wide geographic distribution of donors or engaging the board in solicitation? Are leaders in my organization going to turn over?

Andrea Lucard
Director of Development
International Baccalaureate Organization
Geneva

I have found that to create a robust fundraising and partnership program for my organization, I have also had to spend a lot of time understanding my organization's tolerances for various funding models.

—Andrea Lucard

I am perplexed about why the fee-for-service model was left out of the 10 funding models in the article "Ten Nonprofit Funding Models." Early in the article, the fee-for-service model was discounted because the author could not find an example of a large nonprofit operating off of what he writes is a "strictly fee-for-service" model.

According to *The Nonprofit Almanac 2007*, fee-for-service is the single largest source of all nonprofit revenue, accounting for 70 percent of revenues (private contributions are second at 12 percent and government is third at 9 percent). In addition, many of the country's largest nonprofits—such as major hospitals, universities, museums, and theaters—earn a large majority of their revenue through fee-for-service.

Brittany Vasseur
Associate
Community Wealth Ventures
Washington, D.C.

The article "Ten Nonprofit Funding Models" provides guidance and language to simplify strategic planning discussions for nonprofits. The authors cleverly translate business model shorthand, commonly used to categorize and communicate market-facing strategies, into an equally efficient shorthand to shape and communicate strategies for managing the growth and sustainability of nonprofit enterprises. The authors' use of case studies to describe the characteristics of each model and their suggestions of simple questions to test for fit create an easily adopted framework for nonprofit managers to streamline their fundraising strategy.

One of the things I am left wondering after reading the article is What questions about an organization's "capability" should be considered when crafting an approach or assessing the fit within a given nonprofit funding model? My question about capabilities is motivated by my work on public-private partnerships, and, more recently, my work on hybrid organization structures that many believe are the key to achieving scale and impact. I think there may be an opportunity to extend the "Ten Nonprofit Funding Models" thinking to help understand gaps and strengths in the capability of a given nonprofit or social enterprise. Adding a set of "capability fit" questions to each model to supplement the authors' suggested "fundraising fit" questions can guide internal development efforts and help in identifying potential partners, funding organizations, and collaborators with resources that can bridge capability gaps or complement capability strengths.

The Ten Models framework, with capability questions added, would then allow an organization first to identify a funding model, and then to narrow the list of funding (or partnership) prospects based on capability gaps and complements, and finally to create an integrated funding, internal development, and network partner strategy around each given model. Progressive adoption of this framework would go a long way in bringing systems thinking into play with the promise of building efficiency and scale in social capital and social enterprise networks.

Rhesa Jenkins
Strategy and Planning Fellow
Fronde Baliste
San Francisco

More Volunteering

Thank you for the timeliness of the article on volunteerism and nonprofits ("The New Volunteer Workforce," *SSIR*, vol. 7, no. 1, p. 32). Although I appreciated the points expressed by the authors, I was disappointed to see the article describe volunteerism primarily from a Western perspective and focus on large-scale organizations. As a consultant working in cross-cultural leadership and organizational development, I have found that we need to be more inclusive of other practices and thinking about volunteerism, especially when it comes to the new volunteer workforce.

First, nonprofits must be cognizant of how volunteerism is defined and perceived within cultural systems different from their own. From the research that I am conducting with the Minnesota Association for Volunteer Administration in volunteerism in immigrant communities, definitions and perceptions of volunteerism differ on multiple cultural levels. For example, a culture's orientation toward individualism or collectivism can influence the habits, behaviors, and beliefs of those within the culture, including beliefs on volunteerism.

In many Southeast Asian cultures, social obligations and social identity serve as motivation for individuals to volunteer within their communities. This contrasts with notions of volunteerism from individualistic-based societies such as the United States, in which volunteers seek a personal benefit or gain first. In addition, the benefits of volunteerism in developing countries are not measured in dollars. That is not because volunteerism is not valued, but because the emphasis is on the relationship that is built, not on the financial return.

It is also important for nonprofits to recognize that strategies for managing volunteers will differ depending on the organization's size and whether the organization is structured formally or informally. For example, information technology is a great way to increase reach and create social networks, but smaller nonprofits and volunteer groups often lack the technological resources, skills, and funding to be strategic about how they do this.

Although it is of great service to highlight the work that larger nonprofits are doing, there is much to be learned from smaller agencies and informal groups that are able to develop volunteer talent with very few resources. Certainly they can bring wisdom to this arena.

It is my belief that for the nonprofit sector to build and sustain the volunteer workforce of the future, it must make a commitment to evaluating cultural assumptions, systems, and thoughts inherent in volunteer management and practices. If it fails to do so, it will fall short in developing volunteer talent that is ready to be of service.

Mai Moua
President
Leadership Paradigms Inc.
Saint Paul

Q & A P. 13
Reviews P. 17
First Person P. 21

By Alana Conner

PHOTOGRAPH BY BARTON SILVERMAN/THE NEW YORK TIMES/REDUX

Many people, such as Yankees pitcher Andy Pettitte, act unethically not to get ahead but to avoid falling behind.

SOCIAL RESPONSIBILITY

At a Loss for Ethics

▶ New York Yankees pitcher Andy Pettitte is famous not only for his phenomenal left arm, but also for his rock-solid integrity. So when he confessed in December 2007 to illegally using human growth hormone following an elbow injury, Dolly Chugh, an assistant professor at New York University's Stern School of Business, listened closely.

"I felt an obligation to get back to my team as soon as possible," Pettitte explained in a statement. "I wasn't looking for an edge; I was looking to heal."

What Pettitte revealed in his statement Chugh captures in the laboratory: People are more likely to bend their ethics to avoid a loss—such as letting down their teammates—than to attain a gain—such as extra muscle and the competitive edge that comes with it. Indeed, in a recent series of studies, when Chugh and her coauthor framed identical situations as either a cause for loss or an opportunity for gain, more participants lied and cheated in the former situation than in the latter one.

In a laboratory experiment, for example, the researchers cast undergraduates in the role of an entrepreneur who wants to buy a business from a competitor with unknown intentions. Half of the participants learned that they had a 25 percent chance of gaining the acquisition (the *gain-frame* condition), and the other half learned that they had a 75 percent chance of losing the acquisition (the *loss-frame* condition). Although their odds of success were identical, participants in the loss-frame condition were more willing to seek insider information about the competitor's business than were participants in the gain-frame condition. Similarly, in a negotiation game, MBA students who read that they had a 75 percent chance of losing a deal told more lies and made more false promises than did MBA students who read that they had a 25 percent chance of gaining a deal.

To explain these findings, Chugh and coauthor Mary C. Kern, an assistant professor at Baruch College's Zicklin School of Business, draw on the Nobel Prize-winning work of Princeton University psychologist Daniel Kahneman. With the late Stanford psychologist Amos Tversky, Kahneman developed prospect theory to capture the fact that in the mind's eye, losses often loom larger than gains. Likewise, although "greed and the desire to get ahead can lead people to do bad things, fear of doing worse than before, or worse than others, may more often cause people to take the low road," says Chugh.

Because loss-frames and gain-frames are matters of perception, not reality, "we don't have to be in a bad economy to see more unethical behavior," says Chugh. At the same time, however, the economy does not have to improve to make people more scrupulous. "To protect yourself from deception, try to figure out how the other person is seeing the situation," she says, and then make sure that he or she does not feel cornered. "Remember that you contribute to how others view the situation." ■

Mary C. Kern and Dolly Chugh, "Bounded Ethicality: The Perils of Loss Framing," *Psychological Science*, 20(3), 2009.

PHILANTHROPY

When Swag Backfires

▶ Embroidered T-shirts, discounted tickets, exclusive concerts, and other charity carrots can sometimes rouse people to donate more time and money to nonprofits. But incentives can also stifle giving, finds Dan Ariely, a professor of behavioral economics at Duke University's Fuqua School of Business and author of *Predictably Irrational*. With his colleagues, Ariely shows that when donors' gifts are public, nonprofits need not gild the lily by offering trinkets—social approbation is reward enough. But when gifts are private, nonprofits should use loot to inspire even greater generosity.

"Part of the reason we give is so that others will think better of us," Ariely explains. "But when the signals are mixed"—that is, when we cannot clearly convey that we are just doing good, because we are also doing well—"we give less." Conversely, when no one's watching, we may need a small prize to unleash our inner altruist.

To explore how incentives can heighten or hinder prosocial behavior, the researchers conducted a laboratory experiment and a field experiment. In both studies, they gave half of the participants a monetary reward for performing tasks (clicking computer keys, riding a stationary bike) that would lead to donations to charities, and gave the other half no such reward. At the same time, the researchers randomly assigned half of the participants to a public condition, in which other people knew about their efforts; and the other half to a private condition, in which their labors went unwatched. Both studies showed that the money inspired greater charitable exertions in the private conditions. But in the public conditions, offering cash for charity either had no effect or actually depressed participants' charitable output.

Ariely speculates that his team's findings hold true not only for fundraising gifts, thank-you events, and donor privileges, but also for tax incentives and price breaks. "If I drive a Prius, and you think I'm driving it because I'm a good green guy, then I get to project that image to you. But if my Prius is cheap, then you don't know whether I'm good or just cheap."

"Public giving is good, and incentives are good, but you don't want to mix them," Ariely adds. ■

Dan Ariely, Anat Bracha, and Stephan Meier, "Doing Good or Doing Well? Image Motivation and Monetary Incentives in Behaving Prosocially," *American Economic Review*, *99*(1), 2009.

CULTURE

The Violent Death of Benevolence

▶ Players of the video game *MadWorld* can use their Nintendo Wiis to impale enemies on spikes, gouge out their eyes with street signs, and chop them in half with chain saws. The *Mortal Kombat* series offers its users similar thrills: ripping foes' heads from their bodies, tearing their hearts out of their chests, and burning the flesh off their skeletons.

Although their producers argue that these games have no ill effects, a new research article shows that violent media blunt people's altruistic tendencies. In one experiment, for example, participants who played a violent video game took longer to respond to an emergency than did participants who played a nonviolent game. And in a second study, theater patrons exiting a violent film responded more slowly to a woman in distress than did patrons exiting a nonviolent film.

"Violent media make people numb to the pain and suffering of others," concludes Brad J. Bushman, a professor at the University of Michigan's Institute for Social Research and the article's lead author. His coauthor is Craig A. Anderson, a professor at Iowa State University and an expert on media violence.

Previous research shows that viewing violent media makes both children and adults more physically aggressive. Other studies further indicate that playing violent video games desensitizes people to the violence of others. Yet Bushman and Anderson's studies are the first to connect the dots between viewing violent media and failing to help people in need, including victims of brutality.

For their first study, Bushman and Anderson randomly assigned 320 men and women to play either a violent video game (e.g., *Mortal Kombat*, *Carmageddon*, or *Future Cop*) or a nonviolent game (e.g., *Austin Powers*, *Tetra Madness*, or *3D Pinball*). After 20 minutes of play, the researchers gave participants a bogus survey to complete. A staged fracas then erupted outside the lab, replete with thrown chairs, banged doors, and one party loudly complaining about an injured ankle. The researchers found that the players of violent games tarried longer before responding to the emergency, were less likely to report that they heard a fight, and judged the fight to be less serious than did the players of nonviolent games.

Taking their findings into the real world, Bushman and Anderson next planted a female confederate with crutches and a bandaged ankle outside a movie theater. After the confederate dropped her crutches, a hidden assistant measured how long it took bystanders to help her. Once again, the researchers found that people spilling out of a violent movie took longer to help than did people exiting a nonviolent movie.

Many people seem to think that "if violent media don't make you kill someone, then they have no effect," says Bushman. As his research findings underscore, however, gratuitous gore and casual cruelty can quietly chip away at civility. ■

Brad J. Bushman and Craig A. Anderson, "Comfortably Numb: Desensitizing Effects of Violent Media on Helping Others," *Psychological Science*, *20*(3), 2009.

Gruesome video games like MadWorld *(below) numb people to the suffering of others, as do violent movies.*

IMAGE COURTESY OF SEGA CORP.

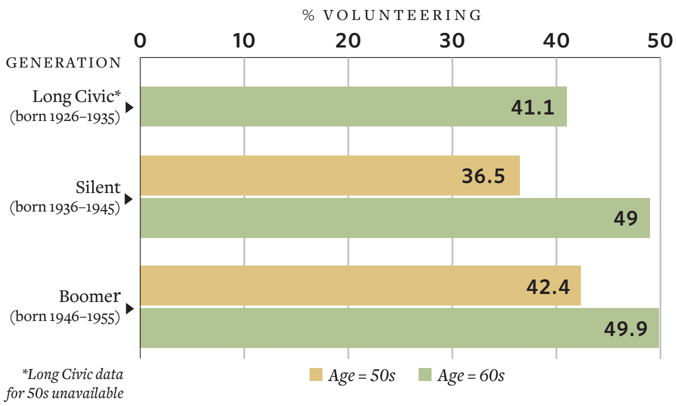
MANAGEMENT

The Volunteer Boom

▶ Commentators such as former *NBC Nightly News* anchor Tom Brokaw and Robert Putnam, author of *Bowling Alone*, contend that Americans who came of age during World War II are the "greatest generation," shouldering more than their fair share of civic duty and patriotic discipline. Meanwhile, observers criticize the baby boomers—Americans born in the years following WWII—as selfish whiners and disenchanted laggards.

But when it comes to volunteering, "this basically isn't true," finds DePaul University sociologist Christopher J. Einolf in a recent research article. "Not only are baby boomers volunteering at a higher rate than the cohorts before and after them, but also the sheer size of their cohort means that the number of elderly volunteers is going to double," he says. "If anything, nonprofits will soon have more volunteers than they know what to do with," he predicts.

Einolf compared rates and amounts of volunteering for three distinct generations: the long civic generation (also called the greatest generation), which was born between 1926 and 1935; the silent generation (so-called because of its small size and relative absence from public discourse), which was born between 1936 and 1945; and the baby boomer generation, that sudden swell of Americans born between 1946 and 1955. Using data from the 1995 and 2005 waves of the John D. and Catherine T. MacArthur Foundation's Midlife Development in the United States (MIDUS) survey, he not only examined participants'



self-reported volunteering and giving in their 50s and 60s, but also predicted how much boomers would volunteer in 2015, after most of this cohort will have retired.

As the chart above shows, Einolf discovered that more baby boomers donated their time during their 50s (that is, in 2005) than did silent generation members at the same age (that is, in 1995). (Because long civic generation members were in their 50s before the MIDUS study began, data for this group are missing in this analysis.) When he statistically modeled rates and amounts of volunteering in 2015 for the baby boomers, he further found that this allegedly self-absorbed cohort's volunteering would outstrip that of both preceding generations during their retirement years.

Previous studies of generational differences in volunteering have confounded age with cohort, says Einolf, and have therefore underestimated baby boomers' altruistic moxie. Comparing 60-year-old members of the greatest generation with 40-year-old baby boomers is fraught because the older cohort is already retired, while the younger generation is still embroiled in earning a living. A more accurate analysis is to compare different cohorts at the same age, which is what a longitudinal study such as MIDUS allows.

To take advantage of the mounting tide of volunteers, nonprofits should start cultivating 50-somethings now, says Einolf. "People who volunteer in retirement are the same people who volunteered before retirement, only they give more hours," he notes. "If you want to get retired volunteers, recruit them now before they leave the labor force." ■

Christopher J. Einolf, "Will the Boomers Volunteer During Retirement? Comparing the Baby Boom, Silent, and Long Civic Cohorts," *Nonprofit and Voluntary Sector Quarterly*, 38(2), 2009.

MANAGEMENT

Color Blindness Is Shortsighted

▶ Now that the American workforce is more diverse than ever before, what do we do with the differences? The old-school approach is to pretend that racial and ethnic distinctions either do not exist or do not matter—a worldview called color blindness.

As a new psychology study shows, however, "just sweeping race under the rug can be bad for everybody in an organization," says Victoria C. Plaut, an assistant professor at the University of Georgia and the study's lead author.

Color blindness cloaks difference like the emperor's new clothes: Everyone can see that race and ethnicity influence people, but no one can talk about it. Rather than making minorities feel comfortable, though, this implicit gag order actually leads them to feel less loyal to their employers and less engaged with their work, find Plaut and her colleagues.

In contrast, acknowledging and even celebrating diversity—a worldview called multiculturalism—inspires greater commitment, pride, and conscientiousness among minority employees. Organizations with these "psychologically engaged" workers, in turn, are more productive and profitable and have less turnover than do organizations with a more alienated workforce, previous research shows.

To examine how colorblind versus multicultural worldviews affect minority workers, Plaut and her colleagues surveyed 4,915 employees across 18 work units in a large U.S. health care organization. The researchers found that the more a unit's white employees espoused color blindness, the less psychological engagement its minority employees reported. Conversely, the more a unit's white employees endorsed multiculturalism, the more loyal and enthusiastic its minority employees felt.

Verizon Communications Inc.'s Matthew J. Dreyer agrees that a multicultural outlook helps harness the human potential of diverse workplaces like his. "By definition, a color-

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blind approach denies a key dimension of diversity and discourages employees from bringing their whole selves to work," says Dreyer, who is a member of Verizon's diversity management team. "We use a multicultural approach that not only acknowledges our employees' diversity, but also encourages them to bring their unique ideas, talents, backgrounds, and perspectives to work." Employees respond favorably: Verizon routinely makes the top 10 lists of best places for minorities and women to work.

In their study, Plaut and her coauthors further discovered that the more color-blind the unit, the more racial bias minority employees experienced. Plaut gives two explanations for this finding. "Other research shows that if you think you should avoid the topic of race, you act more distant with people of other races," she notes, which may leave minority workers feeling bewildered and left out. A more insidious reason is that "some people actually use color blindness to maintain the racial status quo," she says. "If diversity feels threatening to you, you may claim to be color blind to block efforts to create greater equality."

At the same time, noticing race and ethnicity does not mean indulging hackneyed prejudices, Plaut warns: "This research does not say that you should judge people by the color of their skin instead of by the content of their character. Rather, it says that ignoring race in a color-coded society can lead to negative consequences." ■

Victoria C. Plaut, Kecia M. Thomas, and Matt J. Goren, "Is Multiculturalism or Color Blindness Better for Minorities?" *Psychological Science*, 20(4), 2009.

SOCIAL ENTREPRENEURSHIP

Think Passionate

▶ Building a company is so hard that "if you don't have a passion, you'll give up," said Steve Jobs, CEO of Apple Inc., in a 2000 *Fortune* article. Investors know this, and so they screen for entrepreneurial passion when deciding which ventures to fund.

But not all kinds of passion attract cash, finds a new research article. Instead, cognitive passion—as revealed in entrepreneurs' preparation, thoughtfulness, and logic—brings the bucks, while affective passion—as evident in facial expressions, gestures, and tone of voice—does little to court capital.

"There are different levels of passion," explains Xiao-Ping Chen, a professor at the University of Washington's Foster School of Business and the study's lead author. "On the surface level—affective passion—you see whether people are excited, whether their faces light up. A deeper level is their cognitive processes—how much and how deeply they think about their idea. An even deeper level is behavior: Did the entrepreneurs, say, quit their jobs to start their own business? How much of their own money did they invest?"

To test whether and what kinds of passion win venture funding, Chen and her colleagues first created scales that observers could use to rate other people's cognitive and affective passion. (The scale does not measure behavioral passion.) They then asked 55 investors hailing from venture capital firms, banks, and financial companies to use the passion scales in rating 31 presentations at a university business plan competition. The researchers found that the more prepared—that is, cognitively passionate—the entrepreneurs, the more likely they were to win funding from the judges. Affective passion, however, did not lure the lucre.

The founders of D.light Design, a company that creates safe, affordable lighting for people in the developing world, can attest to the importance of preparation in securing commercial capital. Since its founding in 2006, D.light has so far clinched some $6 million in venture funding. “Really knowing the market is critical,” says Nedjip Tozun, the company’s president. “We spent a lot of time with customers, and so we understood their core needs. There were a lot of other initiatives with solar-powered LED products [like D.light’s], but they were frankly just too expensive. We knew our customers’ price point, and were able to articulate that to investors.”

Two women in Uttar Pradesh, India, can now study at night because of their safe and affordable D.light lamp.

PHOTOGRAPH COURTESY OF D.LIGHT DESIGN

D.light’s engineers also worked a year without pay to develop a prototype of the company’s first product. “Our passion was obvious by what we created without any funding. We could say [to potential investors], here’s the product, here’s the market, and here’s the plan for getting the product to market.”

Such extra preparation may be even more important for social entrepreneurs than for ordinary business entrepreneurs, says Chen. “Every social entrepreneur has a compelling story,” she notes, “and so to differentiate themselves, they have to show more careful analysis.”

“It’s a lot of hard work, and so it’s not for the faint of heart,” agrees Tozun. “But if you’re really passionate about something, it’s doable.” ■

Xiao-Ping Chen, Xin Yao, and Suresh B. Kotha, “Entrepreneur Passion and Preparedness in Business Plan Presentations: A Persuasion Analysis of Venture Capitalists’ Funding Decisions,” *Academy of Management Journal*, 52(1), 2009.

PHOTOGRAPHS BY JENNIFER ALTMAN

Judith Rodin is funding new innovation processes, like crowdsourcing and collaborative competitions.

JUDITH RODIN HEADS the Rockefeller Foundation, one of the world's oldest, most influential, and innovative foundations. Many of the 20th century's big breakthroughs—Social Security, the Green Revolution, the discovery of DNA, and family planning—can be traced to early funding from the Rockefeller Foundation.

Today, Rodin is doing her best to keep the Rockefeller Foundation at the forefront of new and big ideas. The foundation continues to fund organizations tackling specific problems like poor health care and environmental degradation. But Rodin has taken a different tack by also funding organizations that are creating new innovation *processes*—like crowdsourcing and collaborative competitions—which can be applied to solving all types of social problems.

In this interview with *Stanford Social Innovation Review* Managing Editor Eric Nee, Rodin explains the impact that the economic downturn has had on the Rockefeller Foundation and its grantmaking ability. She goes on to discuss in some detail why the foundation is funding organizations developing new innovation processes and which processes are proving most fruitful. And last, Rodin explains how the Rockefeller Foundation is adapting its grantmaking to the new opportunities provided by the Obama administration.

Eric Nee: How is the economic downturn affecting the Rockefeller Foundation?

Judith Rodin: Nobody foresaw the magnitude of the economic crisis or the rapidity with which it occurred. Our endowment was down somewhere in the neighborhood of 25 percent at the end of '08. And we will, undoubtedly, be well over our traditional 5 percent payout this year. But our investment managers were attentive to the market turbulence, and in early 2008 we took out a sizable line of credit with a large bank. With access to that money, we did not have to sell our holdings into a declining market to meet our grantmaking needs. We plan to honor all of our approved grants and move forward with all of our ongoing initiatives. The Rockefeller Foundation has been around for more than 90 years, and with the confidence of that history we're well positioned to weather this financial crisis.

What lessons did the foundation learn from going through the Great Depression?

Just as the federal government saw the opportunity to initiate major programs during that time of need, so too did the Rockefeller Foundation. It spent substantial resources on significant programs, such as the development of Social Security. We are planning to do the same thing now.

What impact will the economic downturn have on nonprofits?

Clearly, there will be fewer nonprofits, at both the level of givers and the level of grantees. This may be the moment for consolidation in an "industry"—in quote marks—that's really proliferated, and where there may not have been the incentive or the motivation for economies of scale. And so, regrettably, this may be an opportunity for that. I also think that innovation is going to be critical, accomplishing more with less, working together, leveraging resources, sharing data, and creating models for change that can be more easily replicated. All of these things are going to be absolutely urgent in this economic climate.

You mentioned innovation. One of the Rockefeller Foundation's program areas is funding innovation. Can you explain what you are doing in that area?

Innovation is not just a product, it's a process. We want to focus our funding on the how, not just on the what. We're funding organizations that are at the cutting edge of the process of innovation. Our hope is that those processes can be used by lots of different organizations in lots of different fields. What we've found is that a lot of the innovative processes that have been created in the private sector can be applied to solving not-for-profit social challenges in the fields in which we work—health care, economic security, climate change, poverty alleviation, and capacity building.

We're focusing our efforts on two core innovation ideas. First, that the most successful solutions will often come from the place where you'd least expect them. Here we are funding organizations involved in crowdsourcing techniques and collaborative competitions. Second, that the innovations that focus on the user often lead to extraordinary and, we think, different outcomes. Here we are funding organizations focused on user-driven innovation.

Let's talk about the first type of innovation model you mentioned, crowdsourcing.

We began with a partnership with a for-profit company called InnoCentive that has linked together a network of about 150,000 engineers, scientists, and entrepreneurs around the world. They use a Web-based platform to gather solutions to problems that have confounded people working in just one place, such as an R&D department at a large pharmaceutical company. Hundreds or even thousands of people who have never met, and never will, compete to solve a problem. The best solution, which is determined by the organization that posted the problem, wins a prize.

We thought this would be an amazing platform for finding solutions to world problems. I'll give you an example. BoGoLight had developed a solar-powered flashlight and wanted to expand on that to develop a product that could light a whole room for people who had no electricity. So they posted the problem on InnoCentive. The winner was a scientist in New Zealand, someone with whom BoGoLight, which is based in Houston, would never have come into contact. Just as important, BoGoLight said the process was much more economical and allowed them to see the problem differently. The new light is now being used in African villages and in the Gaza Strip.

One of the interesting things is how many of the solvers have sent e-mails back to InnoCentive saying: "I can't tell you how fantastic it feels to be working on social problems. It's not that I don't like the prize money, and I like working on the for-profit problems, too. But it feels terrific to be working on socially important problems that I know can help people."

Who are you funding in the area of collaborative competitions?

An example is Changemakers, an Ashoka-founded NGO. Here again our interest is in the process. At InnoCentive, the problem solvers don't see one another's solutions, but at Changemakers all of the solutions are posted so that everyone can read them and perhaps build on one another's solutions. They aren't in the same room, but they can collaborate virtually, making it possible to create a different and better solution. It's through collaborative revision and iteration that the best ideas come and new and creative solutions are developed. Coca-Cola, for example, sponsored a global water challenge at Changemakers. They were looking for ways to help impoverished communities gain access to sanitation and drinking water. Almost 300 competing applications came in from 54 countries. Four of these entrants were named winners and are splitting $1 million to create scalable, replicable, and sustainable models that can be applied around the world.

The second type of process that you are funding is user-driven innovation. Can you explain what that is?

The design firm IDEO is one of the best practitioners of user-driven innovation. Their concept is that innovations are most successful if the people who will be using the product or the service are given a real voice in the development process. IDEO usually works with large for-profit companies to help design new products and services. We funded IDEO to work with nonprofits to help solve social problems. One grantee they've been working with is Conversion Sound, a social enterprise that develops hearing aids for poor people in rural India. Through the IDEO process they discovered that because authority commands such respect, particularly in the rural parts of India, hearing aid technicians would be more effective if they wore uniforms. It's certainly not something that I would have thought of, or even thought was important, but the users identified this as critical. In this instance, a small change in the program made a very big difference.

Another example of user-driven innovation is the work done by Positive Deviance, a group at Tufts University. Their idea is that every community has positive outliers, people who stand out because their behavior is different from most of the other people in the group and because they are more successful. What Positive Deviance does is identify the behaviors that have made these outliers successful, and then teach and institutionalize these behaviors to others in the group. Positive Deviance gets credit for showing what reduced hospital-acquired infections. They found that in hospitals where the infection rate was very low, individuals were using hand sanitizers, and that that was not the case systematically in those hospitals with high infection rates. Positive Deviance spread those practices to other hospitals.

With our funding, Positive Deviance is

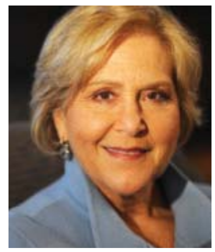
trying to figure out ways to decrease corruption in governments of developing countries. They're identifying the behaviors of the most ethical public officials in developing countries and what behaviors they engage in to root out waste, fraud, abuse, and corruption, and then they are trying to generalize and teach those behaviors. Their belief is that some of the abuse comes from lacking the skills to behave ethically, rather than simply looking for fraudulent ways to hurt people.

How does the Rockefeller Foundation get these lessons and skills about innovative processes out to the rest of the world?
That is the critical question. We think innovation is a skill that can be taught. Our Innovation Initiative has three parts. The first part, which I've already described, is to make the grants to do the work. The second part is monitoring and evaluating the work. This involves not only measuring success in the more traditional terms—does the innovation work—but also evaluating whether the process made the work of the grantee better, different, more cost-effective, and a whole cascade of other parameters. The third part is to disseminate the process through conferences, written materials, and other means. Our success will be realized only if all of this spreads and goes to scale. We've already begun bringing the grantees together, both actually and virtually, to share what they have learned.

One of the things we are also doing is to turn the lens on ourselves and ask are we, the Rockefeller Foundation and the philanthropy sector as a whole, using these innovation tools and techniques? If we are, are we using them as effectively as we might? And if we're not, can we go through the same kind of training that we've been doing with our grantees? We've held one workshop for several foundations that were interested in embarking on this journey with us. And we've held a couple of workshops for ourselves. If we really get good at this, we believe that by using some of these innovation practices we can make up for some of the financial cuts in our endowment.

Let's talk about President Obama. What impact will his administration have on the foundation's work?
We did a national poll last summer with *Time*—well before the economic crisis really hit. What we found is that Americans want new public policies. They want government and their employers to enter into a new kind of social contract. Americans also understand that their roles will have to change and that the 21st century is going to demand different things of them as well. We were struck by their embrace of government. So I think President Obama has that mandate.

The opportunity for innovation is real, in part because resources are limited. Whether it's innovation in public policy, whether it's a White House Office of Social Innovation, whether it's new kinds of models of public-private partnership, all of these are going to be necessary. I don't think it's a choice between public and private approaches to solving social problems. It's going to require all of the sectors. We may need to redefine the roles of each and how they interact. But the problems are so big that we need both the markets and the public sector to engage, but we need them to engage in different ways. That's what this discussion in Washington and literally around kitchen tables everywhere in the United States is really all about.



What is the Rockefeller Foundation doing now to take advantage of this situation?
We worked on the economic stimulus bill, trying to draw attention to issues like infrastructure, climate change and the environment, poverty, and urbanization. Some of our grantmaking has changed to capitalize on this shift as well.

We just funded a conference at NYU's Furman Center called "A Crisis Is a Terrible Thing to Waste." This conference looked at the mortgage and housing crisis and asked, "What are the opportunities for new ideas about homeownership and how mortgages and financing need to occur?" The new U.S. Department of Housing and Urban Development secretary, Shaun Donovan, was a keynote speaker.

You launched a new program last summer called Campaign for American Workers. How has that program adjusted to the new economic and political reality?
It was very clear to us that the growing inequality around the world was going to have enormous impact, and that government was not providing major solutions to that set of issues. So as we thought about this, we said, "Has the social contract for the 20th century now changed so much that we really ought to examine what the 21st century contract should be?" The Campaign for American Workers is an effort to produce new social research and create new public policy solutions, all motivated toward increasing the economic security of the American worker. Our view is that you can't use protectionist trade policies or immigration policies to solve that problem. It's about doing what America has always been good at, which is growing the pot through innovation and economic development and expanding the workforce.

What are some programs that you have funded in this area?
One example is the Tax Policy Center, which has developed the idea of a guaranteed retirement account. If workers don't have access to a conventional defined benefit pension plan, they could contribute 2.5 percent of their income to the plan and the government would pay the first 60 percent of that amount, and then the employer would kick in another 2.5 percent. It's similar to a 401(k). The difference is that the money is deposited into an individual account with the Social Security Administration, which pools the money and puts it into relatively conservative investments.

Are you optimistic about the future?
I think we will find solutions. This is an amazing opportunity for Americans. We can't afford to squander it, because it's a once-in-a-generation opportunity. ■

We think innovation is a skill that can be taught. We've already begun bringing the grantees together, both actually and virtually, to share what they have learned.

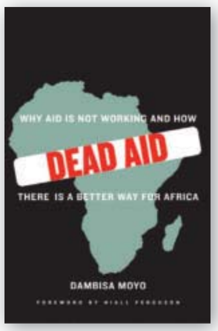
Ideas › Reviews

Just Say "No"

Review by Jane Wales

DEAD AID: Why Aid Is Not Working and How There Is a Better Way for Africa
Dambisa Moyo
188 pages, Farrar, Straus, and Giroux, 2009

As the global financial crisis unfolds, those least responsible—our world's poor—will be most affected. Many have called upon President Obama to uphold his campaign commitment to double foreign assistance. But Dambisa Moyo's book, *Dead Aid*, challenges us to think again. Although we can all agree that ending poverty is an urgent necessity, there appears to be increasing disagreement about the best way to achieve that goal.



Born and raised in Lusaka, Zambia, Moyo has spent the past eight years at Goldman Sachs as head of economic research and strategy for sub-Saharan Africa, and before that as a consultant at the World Bank. With a PhD in economics from Oxford University and a master's degree from Harvard University's John F. Kennedy School of Government, she is more than qualified to tackle this subject.

In *Dead Aid*, Moyo comes out with guns blazing against the aid industry—calling it not just ineffective, but "malignant." Despite more than $1 trillion in development aid given to Africa in the past 50 years, she argues that aid has failed to deliver sustainable economic growth and poverty reduction—and has actually made the continent worse off. To remedy this, Moyo presents a road map for Africa to wean itself of aid over the next five years and offers a menu of alternative means of financing development.

Moyo opens her case by writing, "Between 1970 and 1998, when aid flows to Africa were at their peak, poverty in Africa rose from 11 percent to a staggering 66 percent." Today, Africa is the only continent where life expectancy is less than age 60. Sub-Saharan Africa remains the poorest region in the world, where literacy, health, and other social indicators have plummeted since the 1970s.

Pulling us through a quick history of aid, Moyo covers the many ways its intent and structure have been influenced by world events. She systematically challenges assumptions about the efficacy of the Marshall Plan, International Development Association graduates, and "conditionalities" that require adherence to prescribed economic policies. "By thwarting accountability mechanisms, encouraging rent-seeking behavior, siphoning away talent, and removing pressures to reform inefficient policies and institutions," aid guarantees that social capital remains weak and countries poor. And Moyo's list of aid's sins goes on—including the crowding out of domestic exports and raising the stakes for conflict.

So what does Moyo propose we do? In her own version of shock therapy, she asks, "What if, one by one, African countries each received a phone call, telling them that in exactly five years the aid taps would be shut off—permanently?" The shock would force them to create a new economic plan that phases in alternative financing mechanisms as aid is phased out, she argues. These new financing mechanisms should include increased trade (particularly among African nations and with emerging markets like China, India, and Brazil), foreign direct investment, entrance into international capital markets, and increased domestic savings through remittances and microfinance. The end goal is to phase reliance on aid down to 5 percent or less within five years.

Sound impossible? Moyo doesn't think so. Implementing this plan will be "dead easy," she claims, but will require political will. This political will, Moyo argues, must be rallied by Western activists, for they are the only ones with the ability and the incentive to drive change. "It is, after all, their money being poured down the drain." She is not the first to call for a move away from aid dependency—although she may be the fiercest.

Moyo has only proven correlation, not causation, and although we can't be sure how her prescriptions would hold up in the face of a global recession, she challenges us to think before we act. Moyo expands the boundaries of the development conversation—one that has become both more vibrant and more nuanced in recent months. Those of us rethinking aid can all agree that the time has come for deeper and more direct involvement of Africans in setting their own development course. As the African proverb goes: "The best time to plant a tree is twenty years ago. The second-best time is now." Let us not waste any more time. Africa's moment, and our moment, is now. ■

Jane Wales is vice president of the Aspen Institute, founding CEO of the Global Philanthropy Forum, and CEO of the World Affairs Council of Northern California. Previously, Wales served as special assistant to the president and senior director of the National Security Council in the Clinton administration, as well as associate director of the White House Office of Science & Technology Policy.

Greening the Corporation

Review by Amory Lovins

STRATEGY FOR SUSTAINABILITY: A Business Manifesto
Adam Werbach
240 pages, Harvard Business Press, 2009

Adam Werbach is a wunderkind—at age 23, the youngest-ever national president of the Sierra Club—who has never suffered from conformity. When big environmental groups were being self-congratulatory, he deflated them with his iconoclastic 2004 speech and essay, "Is Environmentalism Dead?" When it was fashionable to bash Wal-Mart Stores Inc., he was one of a handful of environmentalists who saw promise and jumped in headfirst, creating the Personal Sustainability Project for Wal-Mart's 1.9 million employees, revealing how to influence the firm's 200 million regular U.S. shoppers. Werbach went on to help create the "S" division (for sustainability) at the global advertising agency Saatchi & Saatchi.

Now in his mid-30s, Werbach is a fertile innovator of ways to make the world fairer, richer, cooler, and safer, all led by business for profit. He's distilled his varied experi-

Amory Lovins is cofounder, chairman, and chief scientist of Rocky Mountain Institute and coauthor of *Natural Capitalism*.

ences into the useful and refreshingly nondoctrinaire book, *Strategy for Sustainability*.

The thesis of Werbach's book is arrestingly simple: harness corporations' capabilities, exploit their aversion to outcomes (like disease, climate change, and poverty) that are ultimately bad for creating a durable business, help them steer by a tall star, and then their innovations can help everyone. After all, corporations *do* rule the world, so how would you have them do it? (Of the world's 150 largest economic entities, the majority are companies, not countries. Wal-Mart in 2007, for example, was No. 33, bigger than Sweden.)

Fortunately, businesses, coevolving with a vibrant civil society, are the most dynamic force we know. They have the resources, skills, speed, leadership, and motivation to solve big problems quickly and to take those solutions to scale. How they innovate and lead will determine whether their success will bring benefit or harm to others and to the Earth.

The honor roll of firms that grasp this idea and are doing very well by doing good continues to grow and their achievements to inspire. Many have already saved billions of dollars by substituting energy efficiency for fuel—thus proving that climate protection is not costly but profitable. Increasingly, successful firms draw their strategic insights from nature—a 3.8 billion-year experiment in which the 99-odd percent of designs that didn't work got recalled by the manufacturer, and those that are still around teach us wonderfully about resilient design. Werbach notes scores of those lessons. (He misses a vital one—you can't get really good without strong competitors—but catches it later by advising firms to engage their critics as improvement advisors.) On this biological foundation, and assembling many companies' experiences, he builds a rough-and-ready but useful guide to changing corporate culture and operations in order to get ahead of change and build a resilient firm that benefits all.

Werbach prescribes three rules that companies should adopt to remain agile: transparency, engagement, and networking. He explains how both companies and their critics can succeed, not by confrontation but by mutual learning and *aikido*. The compelling cases in Chapter 4 make this thesis irresistible.

Strategy for Sustainability is useful not because it's long but because it's bite-sized; not because it's profound but because it's simple; not because it's densely packed with abstruse theories but because it tells vivid and interlocked stories that stick in the brain. It explains the obvious in ways that are inescapably virtuous, profitable, right, and fun.

I enjoy this book especially because, like my own work, it's practice, not theory; solutions, not problems; and transformational, not incremental. I might wish that it more systematically applied the operational principles my coauthors and I developed in *Natural Capitalism* in 1999, but that wouldn't be fair: This book is about how to set and reach overarching corporate goals, not what the goals should be. Within this modest framework, Werbach has compressed much insight and some wisdom into a compact scope that tells you how to do right, make money, and thereby (to paraphrase Mark Twain) gratify some and astonish the rest. ■

Unleash the Hordes

Review by Carl Schramm

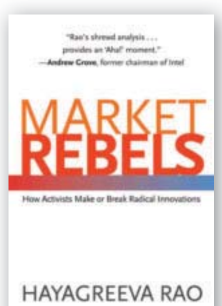
MARKET REBELS: How Activists Make or Break Radical Innovations
Hayagreeva Rao
222 pages, Princeton University Press, 2008

Lost in many of the histories of Silicon Valley is the important role played by the Homebrew Computer Club. Founded in March 1975 (one month before Microsoft Corp.), the club was one of the cradles of the personal computing revolution about to sweep the United States. An avid group of people who enjoyed building their own computers and writing their own software, Homebrew eventually spawned 22 companies, including Apple Inc.

It is precisely this type of story that Hayagreeva Rao covers in his interesting new book, *Market Rebels*. For Rao, the untold story of economic change is the role of social movements in either promoting or suppressing innovations, often against stacked odds. He starts with the automobile. Rao sets out to deflate what he says is popular mythology that Henry Ford created the auto industry. Instead, it was the myriad automobile clubs that sprang up between 1895 and 1910, holding demonstrations and reliability contests, that "established the car as a cultural category." This is undoubtedly true, but Ford played no small role in the car's popularity. The emerging culture, after all, needed an object to venerate. Ford provided that with the introduction of the Model T in 1908.

Rao's next example is microbrewing: In 1980 there were eight microbrewers in the United States; by 2003, there were 1,492. What drove this extraordinary growth? "Evange-ale-ists," says Rao: "Beer enthusiasts were rebels who constructed a *hot cause* (the atrocious taste of mass-produced beer) and relied on *cool mobilization* (small brewpubs using traditional methods and authentic artisanal techniques that offered distinctive beers and, therefore, added to cultural diversity)." Hot cause and cool mobilization are the intended catchphrases of the book—activists in each area unfreeze an equilibrium and refreeze a new one. It's clever, but somehow feels forced.

In his presentation of social movements as an alternative to economic models, Rao caricatures economists as solely concerned with the iron invisible hand, not the "joined hands" that Rao celebrates. This is unfair. There are many economists concerned with the intricacies of economic behavior and its relation with larger social patterns. Rao simply dismisses Adam Smith's invisible hand as irrelevant, drawing a distinction between individual and collective action. But his descriptions of auto enthusiasts and PC evangelists seem exactly like people pursuing their own self-interests, with the result that society is better off. And Smith was part of the Scottish Enlightenment, which not only influenced the founders of the American republic but also put much stock in the idea of spontaneous order. What are Rao's social movements but examples of this?



In other words, Rao describes exactly the phenomenon of economic change, and we should be thankful that he has connected social and eco-

Carl Schramm is the president and CEO of the Ewing Marion Kauffman Foundation. He is the author of *The Entrepreneurial Imperative* and coauthor of *Good Capitalism, Bad Capitalism.*

nomic activities that are often treated separately. We speak of "the economy" as some disembodied mechanism that is malleable to our ministrations; we treat consumption of goods and services as if it were somehow shoved upon us by diabolical corporations. Yet, as Rao shows, much of what we call "the economy" is inseparable from everyday life. We enjoy the freedom (and pollution) of cars not because of that evil Henry Ford or scheming multinationals, but because a cadre of people were determined that they represented the future.

But not all is smooth sailing: The other side of what Rao's market rebels do is "break" innovation. The two examples here are the anti-chain store and anti-biotechnology movements. In these instances, "weaker organizational forms" take on, through "nonmarket" strategies, more powerful organizations such as Wal-Mart Stores Inc. No one enjoys seeing independent stores shut down, but there is good evidence that chain stores bring huge benefits in employment and efficiency. Plus, once you realize that many anti-Wal-Mart groups are funded by unions, the heroic rebels vs. evil empire archetype fades a bit.

Slightly more complex is biotechnology. True, many questions of morality and safety remain, but there is also great promise in new types of drugs. Rao focuses on the activist groups that in the late 1980s and early 1990s drove biotechnology research out of Germany. No matter your position on biotechnology, it can be difficult to see equivalence between automobile enthusiasts and groups that use arson as a method of persuasion.

A cynical reviewer might say that Rao has simply discovered capitalism. In the 1940s, Joseph Schumpeter wrote of the "perennial gales of creative destruction" that buffet the established companies of any economy. For Schumpeter, too, this was as much a social as an economic phenomenon.

The narrative of economic growth is always one of challenges to established interests. In this sense, Rao's book appears at just the right time, when questions about whether and how to bail out entrenched interests—carmakers, financial conglomerates—are persistent. Rao's answer, which he may not even see, is a resounding no: allow the rebellious hordes to save our economy. ■

DOG-EARED

The Ultimate Second Act

Review by John Wood

THE UNFINISHED PRESIDENCY
Douglas G. Brinkley
512 pages, Viking Press, 1998

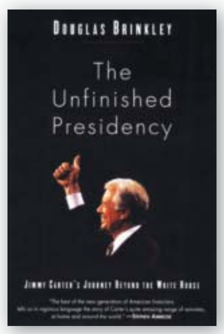
Many of us will confront a luxury that our parents and grandparents never dreamed possible: the opportunity to create and live a "second act" of our adult lives. Retirement was once a brief window, enjoyed by the few and often filled with travel, television, and tedium. Now, as people retire earlier and live longer, many are discovering that there are two, three, or even four decades to fill.

Ideally, older people would watch the curtain rise on Act 2. Yet many Americans are failing miserably at creating a second life. A doctor friend of mine at a private clinic in Vail, Colo., reports that the leading prescription drug for wealthy retirees is antidepressants and the biggest family counseling problem is alcoholism. Rather than seizing the opportunity to use the wisdom of age and experience to redefine themselves, many Americans choose to languish.

For those interested in staging a second act, I strongly encourage reading *The Unfinished Presidency*, a stunningly inspiring and entertaining account of President Jimmy Carter's "journey beyond the White House." Noted historian Douglas G. Brinkley provides an account in depth of Carter's resurrection from a failed one-term President to a widely respected, globe-trotting do-gooder.

The ashes from which this phoenix rose were formidable. Three major failures marked Carter's presidency: 52 American hostages held for more than a year in Iran; an inflation rate of 13.5 percent; and unemployment of 7.5 percent. The nation felt humiliated by the Iran situation, and the economic conditions were so bad that presidential candidate Ronald Reagan talked of a "misery index" that was calculated by adding together the inflation and unemployment rates.

It would have been easy for Carter to retreat to a dark corner and quietly lick his wounds. Or perhaps follow President Gerald Ford's example and retire to the golf course. Carter, however, chose to find his redemption through action. With wife Rosalynn by his side, he donned coveralls and hammered nails on Habitat for Humanity building projects and launched the Carter Center in Atlanta. He flew (commercial!) to locations from Africa to Latin America to supervise elections and agitated for Middle East peace in various power centers. He launched an ambitious drive to wipe the treacherous guinea worm off the face of the Earth and at age 69 summited Mount Fuji. Never had the world seen such a peripatetic ex-President, nor one so devoted to helping create a more just and peaceful world.



I often consulted this book during my own journey of discovery. I spent Act 1 of my adult life working for nearly a decade at Microsoft Corp. For Act 2, I dreamed of launching an NGO (Room to Read) that would bring books and libraries to millions of children across the developing world. But I was fearful of the loss of income and status that would be the doppelganger to this move. And then Brinkley's book struck me like a gauntlet: If Carter could find a meaningful life after being the most powerful man on Earth, then what was to stop a mid-level 35-year-old executive from doing the same?

Many of us will have the great good fortune to have time for a second act, to do what my friend Dipak Jain, dean of Northwestern University's Kellogg School of Management, calls "moving from success to significance." We would do well to learn all we can from Carter's inspiring example. By reading (or rereading) this book, all of us can aspire to aim high while contemplating our next acts. ■

John Wood is the founder and executive chairman of Room to Read, a San Francisco-based nonprofit that has established a network of more than 750 schools and 7,000 multilingual libraries across the developing world. He is the author of *Leaving Microsoft to Change the World*, a book chosen by Amazon.com as one of the top 10 business narratives of 2006.

Social Entrepreneurship Revisited

Not just anyone, anywhere, in any organization can make breakthrough change

By Paul C. Light

Social entrepreneurship is one of the most alluring terms on the problem-solving landscape today, and is in use even in the new Obama administration. The President is quite familiar with the term and has embraced a first-of-its-kind investment fund for social entrepreneurship.

The question is not whether *social entrepreneurship* is a term in good currency, but what it actually means. This question motivated my three-year search for social entrepreneurship, which was funded by the Skoll and Ewing Marion Kauffman foundations.

Ashoka founder and CEO Bill Drayton first used the term "social entrepreneurship" in the early 1980s, and it continues to inspire images of audacious social change—the kind that sweeps away the old approaches to solving intractable social problems such as disease, hunger, and poverty. Like business entrepreneurship, social entrepreneurship involves a wave of creative destruction that remakes society. Although we will always need traditional social services—even more during times of great economic turmoil—social entrepreneurship focuses on changing the underlying dynamics that create the demand for services in the first place. Instead of treating society's distress, social entrepreneurship holds hope for eliminating the distress altogether.

Although people generally agree on this broad definition of social entrepreneurship, confusion reigns over the specifics. Some observers believe that the social entrepreneur himself or herself is the linchpin of change, whereas others focus on the idea, the opportunity for change, or the organization that provides the muscle for scaling up to maximum effect. But which one of these four components comes first? Which one is most important for imagining change, launching an idea, accelerating diffusion, and sustaining impact long enough to create a wave of creative destruction?

The answer depends largely on the assumptions underlying one's notion of social entrepreneurship. My own journey through this thicket of assumptions began with an article I published in the fall 2006 *Stanford Social Innovation Review,* titled "Reshaping Social Entrepreneurship." In that article, I argued for an inclusive, big-tent definition of the term *social entrepreneurship* that acknowledged the small contributions of many people, groups, and organizations.

Since that time, though, I have drilled through hundreds of articles and books on social and business entrepreneurship, and I have surveyed 131 highly, moderately, and not-too-entrepreneurial organizations.

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ILLUSTRATION BY HARRY CAMPBELL

And I discovered that many of the assumptions that I rejected in 2006 turned out to be true after all. Whereas I once believed that virtually everyone could become a social entrepreneur, I am now convinced that there are special sets of attitudes, skills, and practices that make social entrepreneurs and their work distinctive from more traditional public service. As a result, I have become much more concerned about how we can identify potential social entrepreneurs, give them the training and support they need, and increase the odds that their work will succeed.

New Insights

Here are four assumptions about social entrepreneurship that I initially rejected, but now accept:

1. *Social entrepreneurs are not like other high achievers.* I initially rejected the notion that social entrepreneurs bring unique motives, behaviors, and insights to the socially entrepreneurial process. I assumed, wrongly, that they are deflected into social entrepreneurship by the same kinds of opportunities that exist for any pattern-breaking enterprise.

My research suggests otherwise. Social entrepreneurs appear to make quite deliberate decisions to solve social problems, rather than simply stumbling into their work by accident or circumstance. They are often quite sober about their decision to attack a social problem, and they usually understand the consequences of challenging the status quo.

I also find that social entrepreneurs are driven by a persistent, almost unshakable optimism. They persevere in large part because they truly believe that they will succeed in spite of messages to the contrary. This optimism can border on overconfidence, but is essential to their 24/7 commitment.

2. *Socially entrepreneurial ideas are big.* There is considerable debate about the proper scale of socially entrepreneurial ambition. Some argue that small-scale change is just as important as global intent, whereas others reserve the term *social entrepreneurship* for grand impacts, such as those that the microfinance movement has achieved.

Through my research, I find that the greatest ideas often start small, but eventually expand to break the social equilibrium. And so although social entrepreneurs should celebrate small-scale changes, they should ultimately aim to diffuse those changes as broadly as possible.

Likewise, when small-scale ideas have potential, funders ought to invest in spreading them. And where large-scale ideas have shown proof of concept, funders should provide the dollars for growth. To date, most of the work on social entrepreneurship focuses on imagination, invention, and launch. But ultimate impact requires scaling up, diffusion, sustained pressure, and navigation of what J. Gregory Dees, professor of business at Duke University, calls the "ecosystem" of change. (See "Cultivate Your Ecosystem" in the winter 2008 issue of the *Stanford Social Innovation Review.*)

3. *Opportunities for grand change come in waves.* I initially believed that the time was always ripe for sweeping changes. But there is good evidence that socially entrepreneurial opportunities arise during specific punctuations, or focused periods in history. During these periods, the prevailing wisdom weakens, revealing the failure of the status quo to solve problems such as inequality. Having tried for a half century to improve the public schools with little sustainable success, for example, we acquire an appetite for new ideas. These punctuations in history fuel the hope for widespread change and the experimentation that drives it.

Today, the world appears to be experiencing a punctuation of opportunities, which is drawing new funders into the field of social entrepreneurship. No one knows for sure how long these punctuations last—a few years, a decade, or more?—but we do know that these punctuations produce a wave of activity that feeds on itself.

4. *Socially entrepreneurial organizations are built to make change.* I used to believe that all organizations, big or small, old or young, could generate social entrepreneurship. But over the past three years, I have found considerable evidence that most socially entrepreneurial organizations, new and old, are different from traditional organizations. They are relatively flat, singularly focused on the idea of change, and often inexperienced in the administrative procedures needed for transparency and tight governance.

These differences from traditional organizations are both strengths and weaknesses. Driven to succeed at all costs, socially entrepreneurial organizations may neglect organizational infrastructure, possibly resulting in underinvestment in measurement and governance. They may also be so committed to their path that they reject the possibility that they could be wrong, with all that entails for wasted motion and delay. Search as I did, I found little interest among social entrepreneurs and their funders in research and development.

Funders seem to prefer new organizations as platforms for change. At best, they dismiss old organizations as incapable of change. At worst, they view them as protectors of the status quo. Yet I find considerable evidence that old organizations can produce change, especially if they are able to rejuvenate themselves. In short, socially entrepreneurial organizations do not have to be new.

TRIED TRUTHS

Although my definition of social entrepreneurship has become more exclusive over the past three years, I still stand by two of my original, more inclusive assumptions. First, social entrepreneurs do not always act alone. Lone-wolf social entrepreneurs can and do succeed, but so do teams, networks, and communities. Even as the field concentrates on finding heroic individuals, the research suggests that teams of experts often hammer together big breakthroughs. Research on small-business entrepreneurship suggests that teams produce more patents than do lone wolves.

I also circle back to my original assumption that old organizations can nurture social entrepreneurship. Creating a socially entrepreneurial organization within an existing structure is no doubt difficult—rejuvenation involves great pain and disruption. But older agencies can harbor social entrepreneurship if they reverse the bureaucratic effects of organizational aging, as well as through incubators, acquisitions, spin-offs, and more general reward and incentive systems designed to provoke new ideas. The challenge is to protect innovations from people within the organization who have a stake in the status quo. There is nothing stopping an existing organization from producing change except itself.

After my own search for social entrepreneurship, I conclude that the concept is definitely real. I have come to believe in a more exclusive definition, but one that allows for more varieties of endeavor. At the same time, I have also come to believe that social entrepreneurs need considerable help to succeed. Just as organizations such as Ashoka provide networks and consulting for their entrepreneurs, schools of public service can offer training for nascent entrepreneurs and executives.

Perhaps it is just naïveté that drives me, but I believe that this punctuation in history can produce a wave of new entrepreneurs who can come together through networks to break down the social equilibrium. The more the better. ■

Reward Progress, Reduce Poverty

Most antipoverty programs fail to nurture the strengths of individuals and communities By Maurice Lim Miller

Derek had recently been released from juvenile hall in San Francisco, after serving time for robbery—a robbery in which his friend Benjamin had refused to participate. Benjamin convinced Derek to go with him to apply for a construction training program that would help them get "real jobs" and end their involvement in gangs and crime.

I was the director of the training program, and we had only one open slot. Like most social services, my program prioritized the "most in need," so Derek got that last slot. I told them whom we accepted and why. "See! You should have gone on that job with me!" Derek said to Ben. It was then that I realized the message my organization and I were sending.

A decade later in 2004, Flora, a single mother of four, was participating in Hawaii's Family Independence Initiative (FII), an antipoverty project I started. I distinctly remember what she told me: "I work as a cashier, and every day these guys who were just released from drug rehab come in to buy food. They have their EBT card (ATM-like food stamp cards) and some of them have thousands of dollars on them."

"They have more money for food than I have for my kids," she continued. "So what do I have to do—quit my job and get on drugs to get any help?"

Indeed, a study on the economic impact of government benefits on low-income families in Hawaii found that Flora would have been better off working half time and earning only $13,000 a year, because she would then qualify for most welfare programs. When combined with her income, the welfare would provide more than she made working full time. But once her earnings exceeded about 130 percent of the poverty level, she was no longer eligible for much welfare, the Earned Income Tax Credit (EITC), or even training programs like the ones I ran.

My experiences with Derek and Flora, as well as with many other people, have led me to believe that most antipoverty programs do not support the strengths and capabilities of low-income families. Instead they create reverse incentives, negative reinforcements, and ridiculous choices for all involved. The current system that provides benefits based on need is necessary for people in crisis. But to help people end the cycle of poverty, we must reward progress, as well as people who help each other succeed.

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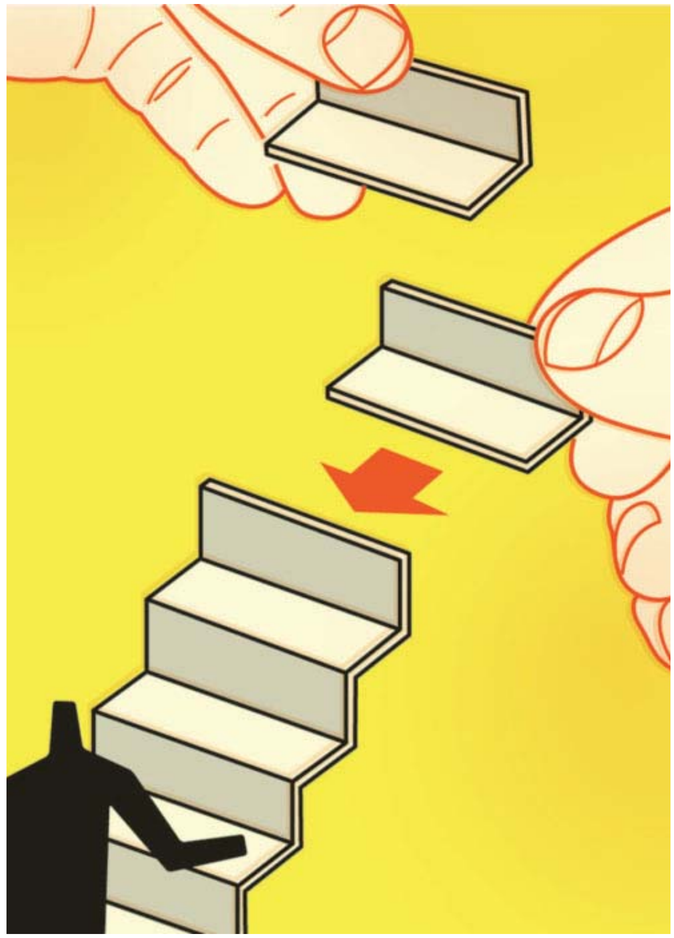

ILLUSTRATION BY HARRY CAMPBELL

BENEFITS THAT BENEFIT

A study by the Corporation for Enterprise Development found that in fiscal year 2005, the federal government gave out $367 billion in benefits. The problem is, 88.7 percent of those benefit dollars—including retirement account incentives, home mortgage interest deductions, and business tax credits—went to households with annual incomes of more than $80,000. In other words, benefits are available to people who already have money, as well as to people living below the poverty level.

But for the working poor—those people who clean our rooms, cut our lawns, and harvest our food—there is very little support, unless they lose a paycheck and fall into crisis, or, less likely, suddenly start earning a lot more money. With a little help, however, this population—already working—has the best chances of reaching a stable middle-income status. A self-employment tax credit could help grow microfirms and informal businesses. Property tax relief could help build assets. Targeted scholarships and fellowships could create more graduates. And if refundable tax credits like EITC could be extended to the working poor, people like Flora could get closer to the middle class.

Even if the government distributes benefits more equitably, it cannot reduce poverty on a large scale unless it encourages the types of strong community bonds that once flourished in the United States. In the 1800s, Irish, Chinese, and other immigrants helped each other find construction jobs, start laundries, and undertake other businesses. After slavery, African-Americans created vibrant communities—Harlem and independent townships—by pooling their talents and money. In the 1990s native tribes in Alaska formed large companies such as Sealaska Corp., and Cambodian refugees came to own more than 80 percent of the donut shops in California. Today, African-Americans have opened the Black New World Social Aid & Pleasure Club as part of a resident effort to create a cultural and economic district in one of the most economically disenfranchised areas of Oakland, Calif.

The biggest obstacle to reducing poverty is not low-income communities' lack of capacity, but society's stereotype that they are unable to help themselves.

Having studied historic and more recent models of entire communities moving from poverty to self-sufficiency, I believe that a community needs three elements to succeed and to sustain its success. First, friends and family must rely on one another for jobs and careers. They can refer one another to jobs they've heard about, teach friends how to start their own businesses, or through role-modeling create the expectation that education is a path to success.

People in communities must also trust each other enough to share funds. They can make personal loans or gifts to each other. They may also create more formal loan pools where each contributor takes a turn accessing the pool.

Finally, community members must feel pride in their elders, culture, and religion. The need for a sense of individual and cultural community pride is greatly underestimated in professional antipoverty work. As Min Saechan, a young leader in the Iu Mien (refugees from Laos) community in Oakland once told me: "The gang violence has gone way down because parents and other young people did things like starting our own tiny scholarship fund and showing pride in our culture. It wasn't youth programs that stopped the violence."

COMMUNAL WEALTH

To catalyze this kind of initiative and mutuality, funders, policymakers, and service programs must recognize and reinforce the strength and pride that exists in so many communities, the kind of pride shown by the volunteers who created the Black New World and other enterprises in West Oakland. These thriving organizations have little public or philanthropic support, yet survive because of the personal ownership and enthusiasm of the residents who formed and run them. Meanwhile, many heavily funded government and foundation programs in the neighborhood have closed.

Residents have told me this time and again. The leader of another low-income community in East Oakland put it this way, "If programs survive because there are professionals who can write good proposals, rather than because our families really want them and use them, then our culture gets weaker." Another leader told me, "If you treat people like they are helpless they begin to believe they are helpless."

Taking these last words to heart, I started FII in 2001 and began to work in Oakland with a group of eight African-American families, 11 Mien families, and six Salvadoran refugee families, all of whom agreed to help each other. Participants learned that if they made verifiable progress—kids' grades improved, credit ratings increased, new jobs secured, etc.—they could earn up to $500 quarterly for two years.

Because we wanted to see what families could do on their own, we told FII liaisons that they would be fired if they gave the families any direction. This created a vacuum of leadership that took patience on our end—but soon enough the families filled this vacuum and started to lead their own change.

Encouraging people to create a village and giving the Oakland families an opportunity to earn extra cash by making progress led to an average jump of 27 percent in family income (not counting the FII awards) during the project's two years of operation. People started new businesses, and many families helped each other purchase homes. Even without monetary awards in the third year of the program, participants' incomes continued to grow, increasing a total of 41 percent on average.

Our second pilot was in Hawaii, where income went up 18 percent in only 20 months. And in our current San Francisco project, average income has jumped 21 percent in just 18 months.

An outside evaluator confirmed our findings and interviewed a sample of the families to account for their success. They all answered that the small monetary awards were important, but that the respect and trust they felt from FII helped them focus on their goals and strengthen their sense of community.

This tells me that the biggest obstacle to reducing poverty is not low-income communities' lack of capacity or unwillingness to change, but society's stereotype that they are unable to help themselves and unwilling to help others. By observing the families in FII, I have come to believe that although some low-income families need professional services, the large majority would prefer that society help them by recognizing their strengths—not by taking the social service approach of focusing on their needs.

Under President Obama, America has renewed its commitment to supporting and growing the middle class. To do this, we must give the working poor the same respect and opportunities that we give to other hardworking people. ■

Your Nonprofit Construction Manager

Complex solutions need dedicated project managers, as well as the funds to pay them

By Elisabeth D. Babcock

ILLUSTRATION BY HARRY CAMPBELL

Imagine this scenario: A bank wants to build a new flagship headquarters, but the bank's leaders want to keep costs to a minimum, and so they decide to take a new approach to the project. Instead of hiring a construction manager, they compose an advertisement that says, "Wanted: Bank headquarters. Fifty stories tall. Must feature innovative architecture." They then send the ad to all the specialty contractors—electricians, architects, plumbers, etc.—they need to build the skyscraper.

After hiring the lowest bidders in each of these fields, the bankers tell them: "Okay, talk among yourselves to get the job done on time, at the lowest cost, with the highest quality. Please. Thank you."

Unimaginable? Of course. The for-profit world has long understood that complex tasks require high-quality project management. Project management is its own area of expertise, with industry-specific professional training, organizations, journals, and tools. Companies would never attempt a project that requires coordinating many distinct areas of professional skill without it.

And yet we do this all the time in the nonprofit world. We assume that when solving a problem requires better coordination between nonprofits, the nonprofits will spontaneously collaborate without additional expertise, staff, or funding. Yet in many cases what nonprofits need is to develop and pay for specialized coordination—that is, project management. "Talk among yourselves" is a poor solution to complex social problems such as homelessness, post-incarceration recidivism, and high school incompletion. The sector also needs to be willing to pay for project management expertise.

EMPTY PARTNERSHIPS

In today's world of limited resources and rapidly growing demand for charitable services, both public and private funders exhort nonprofits to collaborate, without seriously considering whether such collaborations are really the best way to achieve their goals. A 2005 Urban Institute study of 1,192 foundations found that 69 percent sought to fund collaborations, and 42 percent stipulated collaboration as a requirement of funding.

Yet 72 percent of nonprofits have annual budgets of less than $500,000 per year, and thus little or no excess administrative capacity. When faced with the "prove you are collaborating" exhortation, nonprofits typically respond by creating shallow relationships with large numbers of partners. Using the ubiquitous "letters of support" format, the partner organizations write letters promising that they will cooperate, but then often do little else to build a collaboration. Other organizations form deeper relationships, but with limited numbers of partners. The result is that few partnerships ever begin to create anything remotely resembling the intersectoral resource management necessary to solve complex social problems.

Development of the specialized project management expertise that is needed to make a dent in complex social ills requires investment. But funders are notoriously unwilling to pay for such skill development, or to continue funding it until it becomes true expertise. In declining to invest in project management, though, they're ignoring an important lesson from the for-profit world: Good project management pays for itself.

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PROJECT MANAGEMENT IN ACTION

Consider, for example, the Program of All-Inclusive Care for the Elderly (PACE), a national nonprofit program whose sole purpose is project management. Created in San Francisco in 1986, the PACE program now includes a network of 42 organizations operating in 22 states and caring for more than 16,000 elderly people.

PACE's mission is to keep extremely frail, nursing home-eligible elders living at home. PACE elders want to stay out of nursing homes, but cannot coordinate the nutrition, personal care, housing, transportation, medical, physical therapy, pharmacy, mental health, and social services that they need to reside safely at home.

That's where PACE steps in. Each PACE program receives a monthly stipend from Medicare, Medicaid, or a private payer for every elder enrolled. The stipends are less than the average cost of nursing home care (the average in 2007 was $77,745 per person per year). In exchange for this amount, the PACE program pays for and manages all of the services that would normally be covered by Medicare or Medicaid.

To get care, a PACE elder attends an adult day health site a few days per week, where an interdisciplinary team coordinates his or her care. The typical PACE team includes a coordinator (usually a social worker), doctor, nurse, psychiatric nurse-practitioner, physical therapist, occupational therapist, clinical assistant, and nutritionist. Together this team manages a larger network of resources on behalf of the client, including pharmacies, medical specialists, diagnostic testing facilities, hospitals, transportation, home care, and meals contractors. The PACE team chooses these contract providers on the basis of their quality, cost, and ability to work with other specialists. It then uses outcome measures to decide which vendors to retain and which to terminate.

What funders and public policy officials need to realize is that the level of coordination needed to achieve complex social goals often calls for more than mere collaboration.

Notice that the PACE model uses classic project management tools, including client assessment, goal setting, risk management, contract management, outcomes measurement, and cost-benefit analysis. In contrast, independent hospitals, doctors, nutritionists, labs, and home care companies simply do not use these tools in the same way. We could never turn to these groups and say, "Organize yourselves and keep frail elders at home through improved collaboration." It's not that the individual organizations would be unwilling or unable to see the value in such collaboration. It's that such management is *not what they do.*

But PACE has demonstrated its ability to manage projects effectively. Independent evaluations show that PACE saves the federal government 40 percent in Medicare costs and state governments 10 percent or more in Medicaid costs. At the same time, PACE clients have better health, functionality, and personal satisfaction than similarly frail elders.

And although all PACE clients are eligible for institutional care, only 5 percent of them are in hospitals or nursing homes at any given time. More than twice as many PACE clients are able to die at home—often patients' preferred outcome—as the general Medicare population. Not surprisingly, in the Balanced Budget Act of 1997, the federal government reauthorized and expanded the program.

In 1995, I cofounded a PACE program in Massachusetts called the Elder Service Plan of the North Shore (ESPNS). It began as one location serving 20 elders. Now ESPNS serves 970 elders out of six locations. And even though its typical client has 10 or more concurrent specialty services at any given time, ESPNS's 2006 operating margin was $3,123,787, on annual revenues of $29,349,121.

TOOLS FOR CONSTRUCTION MANAGERS

I apply the project management wisdom that I learned at ESPNS in my current role as president of the Crittenton Women's Union (CWU). Located in Boston, CWU helps women in poverty reach economic independence—a goal every bit as complex as that of PACE. At CWU, we developed a project management system we call Mobility Mentoring. Through our Mobility Mentoring policies, procedures, software, and staff, we coordinate the resources women need to get ahead, including housing, child care, education, training, financial management, and social and behavioral health services.

One of our Mobility Mentoring tools is our Hot Jobs software. This software matches our clients with Massachusetts jobs that require less than two years' post-secondary education and pay more than $45,000 per year. Philanthropy paid for the initial development of this and other new tools, but public funding is increasing.

To build Mobility Mentoring, we developed new processes to assess and motivate clients, formulate goals, and evaluate outcomes. This research and development takes considerable time and effort, but we expect the investment to pay off, as it did with PACE. Already, we can measure increases in women's skills and earnings, and over time we expect to measure our impact on other client outcomes. Impact is our product, and our goal is to demonstrate that savings in government expenditures and increased earnings for poor families offset the cost of our product. Unless they are designed to do so, agencies cannot create or measure this kind of impact, no matter how long they "talk among themselves."

When I advocate for more project management organizations in the nonprofit sector, I am not minimizing the need for more partnerships between existing nonprofits, or even the need for more mergers. My own organization was born of a merger between two competing organizations--an event that both stabilized us financially and propelled us forward programmatically.

But organizational partnerships are best at remediating problems of scale or coordinating fairly straightforward programs. What funders and public policy officials need to realize is that the level of coordination necessary to achieve complex social goals in a cost-effective, high-quality way often calls for more than mere collaboration. It requires highly sophisticated expertise in the management and coordination of multiple resources and professional players. Until funders are prepared to call for and pay for such coordination, nonprofits will continue trying to solve complex social problems with inadequate tools. ■

ETHICS *and* NONPROFITS

By Deborah L. Rhode & Amanda K. Packel | Illustration by Richard Mia

Unethical behavior remains a persistent problem in nonprofits and for-profits alike. To help organizations solve that problem, the authors examine the factors that influence moral conduct, the ethical issues that arise specifically in charitable organizations, and the best ways to promote ethical behavior within organizations.

THOSE WHO WORK ON ISSUES OF ethics are among the few professionals not suffering from the current economic downturn. The last decade has brought an escalating supply of moral meltdowns in both the for-profit and the nonprofit sectors. Corporate misconduct has received the greatest attention, in part because the abuses are so egregious and the costs so enormous. Chief contenders for most ethically challenged include former Merrill Lynch & Co. CEO John Thain, who spent $1.22 million in 2008 to redecorate his office, including the purchase of a $1,400 trash can and a $35,000 antique commode, while the company was hemorrhaging losses of some $27 billion.[1]

Still, the corporate sector has no monopoly on greed. Consider EduCap Inc., a multibillion-dollar student loan charity. According to Internal Revenue Service records, the organization abused its tax-exempt status by charging excessive interest on loans and by providing millions in compensation and lavish perks to its CEO and her husband, including use of the organization's $31 million private jet for family and friends.[2]

Unsurprisingly, these and a host of other scandals have eroded public confidence in our nation's leadership. According to a *CBS News* poll, only a quarter of Americans think that top executives are honest. Even executives themselves acknowledge cause for concern. The American Management Association Corporate Values Survey found that about one third of executives believed that their company's public statements on ethics sometimes conflicted with internal messages and realities. And more than one third of the executives reported that although their company would follow the law, it would not always do what would be perceived as ethical.

Employee surveys similarly suggest that many American workplaces fail to foster a culture of integrity. Results vary but generally indicate that between about one-quarter and three-quarters of employees observe misconduct, only about half of which is reported.[3] In the 2007 National Nonprofit Ethics Survey, slightly more than half of employees had observed at least one act of misconduct in the previous year, roughly the same percentages as in the for-profit and government sectors. Nearly 40 percent of nonprofit employees who observed misconduct failed to report it, largely because they believed that reporting would not lead to corrective action or they feared retaliation from management or peers.[4]

Public confidence in nonprofit performance is similarly at risk. A 2008 Brookings Institution survey found that about one third of Americans reported having "not too much" or no confidence in charitable organizations, and 70 percent felt that charitable organizations waste "a great deal" or a "fair amount" of money. Only 10 percent thought charitable organizations did a "very good job" spending money wisely; only 17 percent thought that charities did a "very good job" of being fair in decisions; and only one quarter thought charities did a "very good job" of helping people.[5] Similarly, a 2006 Harris Poll found that only one in 10 Americans strongly believed that charities are honest and ethical in their use of donated funds. Nearly one in three believed that nonprofits have "pretty seriously gotten off in the wrong direction." These public perceptions are particularly troubling for nonprofit organizations that depend on continuing financial contributions.

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Amanda K. Packel is the associate director of the Stanford Center on the Legal Profession. Before joining Stanford University she was an associate at the law firm Covington & Burling, where she practiced white-collar criminal defense.

Addressing these ethical concerns requires a deeper understanding of the forces that compromise ethical judgment and the most effective institutional responses. To that end, this article draws on the growing body of research on organizational culture in general, and in nonprofit institutions in particular. We begin by reviewing the principal forces that distort judgment in all types of organizations. Next, we analyze the ethical issues that arise specifically in the nonprofit sector. We conclude by suggesting ways that nonprofits can prevent and correct misconduct and can institutionalize ethical values in all aspects of the organization's culture.

Causes of Misconduct

Ethical challenges arise at all levels in all types of organizations—for-profit, nonprofit, and government—and involve a complex relationship between individual character and cultural influences. Some of these challenges can result in criminal violations or civil liability: fraud, misrepresentation, and misappropriation of assets fall into this category. More common ethical problems involve gray areas—activities that are on the fringes of fraud, or that involve conflicts of interest, misallocation of resources, or inadequate accountability and transparency.

Research identifies four crucial factors that influence ethical conduct:

- Moral awareness: recognition that a situation raises ethical issues
- Moral decision making: determining what course of action is ethically sound
- Moral intent: identifying which values should take priority in the decision
- Moral action: following through on ethical decisions.[6]

People vary in their capacity for moral judgment—in their ability to recognize and analyze moral issues, and in the priority that they place on moral values. They also differ in their capacity for moral behavior—in their ability to cope with frustration and make good on their commitments.

Cognitive biases can compromise these ethical capacities. Those in leadership positions often have a high degree of confidence in their own judgment. That can readily lead to arrogance, overoptimism, and an escalation of commitment to choices that turn out to be wrong either factually or morally.[7] As a result, people may ignore or suppress dissent, overestimate their ability to rectify adverse consequences, and cover up mistakes by denying, withholding, or even destroying information.[8]

A related bias involves cognitive dissonance: People tend to suppress or reconstrue information that casts doubt on a prior belief or action.[9] Such dynamics may lead people to discount or devalue evidence of the harms of their conduct or the extent of their own responsibility. In-group biases can also result in unconscious discrimination that leads to ostracism of unwelcome or inconvenient views. That, in turn, can generate perceptions of unfairness and encourage team loyalty at the expense of candid and socially responsible decision making.[10]

A person's ethical reasoning and conduct is also affected by organizational structures and norms. Skewed reward systems can lead to a preoccupation with short-term profits, growth, or donations at the expense of long-term values. Mismanaged bonus systems and compensation structures are part of the explanation for the morally irresponsible behavior reflected in Enron Corp. and in the recent financial crisis.[11] In charitable organizations, employees who feel excessive pressure to generate revenue or minimize administrative expenses may engage in misleading conduct.[12] Employees' perceptions of unfairness in reward systems, as well as leaders' apparent lack of commitment to ethical standards, increase the likelihood of unethical behavior.[13]

A variety of situational pressures can also undermine moral conduct. Psychologist Stanley Milgram's classic obedience to authority experiment at Yale University offers a chilling example of how readily the good go bad under situational pressures. When asked to administer electric shocks to another participant in the experiment, about two-thirds of subjects fully complied, up to levels marked "dangerous," despite the victim's screams of pain. Yet when the experiment was described to subjects, none believed that they would comply, and the estimate of how many others would do so was no more than one in 100. In real-world settings, when instructions come from supervisors and jobs are on the line, many moral compasses go missing.

Variations of Milgram's study also documented the influence of peers on individual decision making. Ninety percent of subjects paired with someone who refused to comply also refused to administer the shocks. By the same token, 90 percent of subjects paired with an uncomplaining and obedient subject were equally obedient. Research on organizational behavior similarly finds that people are more likely to engage in unethical conduct when acting with others. Under circumstances where bending the rules provides payoffs for the group, members may feel substantial pressure to put their moral convictions on hold. That is especially likely when organizations place heavy emphasis on loyalty and offer significant rewards to team players. For example, if it is common practice for charity employees to inflate expense reports or occasionally liberate office supplies and in-kind charitable donations, other employees may suspend judgment or follow suit. Once people yield to situational pressures when the moral cost seems small, they can gradually slide into more serious misconduct. Psychologists label this "the boiled frog" phenomenon. A frog thrown into boiling water will jump out of the pot. A frog placed in tepid water that gradually becomes hotter will calmly boil to death.

Moral blinders are especially likely in contexts where people lack accountability for collective decision making. That is often true of boards of directors—members' individual reputations rarely suffer, and insurance typically insulates them from personal liability. A well-known study by Scott Armstrong, a professor at the Wharton School of the University of Pennsylvania, illustrates the pathologies that too often play out in real life. The experiment asked 57 groups of executives and business students to assume the role of an imaginary pharmaceutical company's board of directors. Each group received a fact pattern indicating that one of their company's most profitable drugs was causing an estimated 14 to 22 "unnecessary" deaths a year. The drug would likely be banned by regulators because a competitor offered a safe medication with the same benefits at the same price. More than four-fifths of the boards decided to continue marketing the product and to take legal and political actions to prevent a ban. By contrast, when a different group of people with similar business backgrounds were asked for their personal views on the same hypothetical, 97 percent believed that continuing to market the drug was socially irresponsible.[14]

These dynamics are readily apparent in real-world settings. Enron's board twice suspended conflict of interest rules to allow CFO Andrew Fastow to line his pockets at the corporation's expense.[15] Some members of the United Way of the National Capital Area's board were aware of suspicious withdrawals by CEO Oral Suer over the course of 15 years, but failed to alert the full board or take corrective action.[16] Experts view the large size of some governing bodies,

> PUBLIC CONFIDENCE IN NONPROFIT PERFORMANCE IS AT RISK. ONLY ONE IN 10 STRONGLY BELIEVED THAT CHARITIES ARE HONEST AND ETHICAL IN THEIR USE OF DONATED FUNDS.

such as the formerly 50-member board of the American Red Cross, as a contributing factor in nonprofit scandals.[17]

Other characteristics of organizations can also contribute to unethical conduct. Large organizations facing complex issues may undermine ethical judgments by fragmenting information across multiple departments and people. In many scandals, a large number of professionals—lawyers, accountants, financial analysts, board members, and even officers—lacked important facts raising moral as well as legal concerns. Work may be allocated in ways that prevent decision makers from seeing the full picture, and channels for expressing concerns may be inadequate.

Another important influence is ethical climate—the moral meanings that employees give to workplace policies and practices. Organizations signal their priorities in multiple ways, including the content and enforcement of ethical standards; the criteria for hiring, promotion, and compensation; and the fairness and respect with which they treat their employees. People care deeply about "organizational justice" and perform better when they believe that their workplace is treating them with dignity and is rewarding ethical conduct. Workers also respond to moral cues from peers and leaders. Virtue begets virtue, and observing integrity in others promotes similar behavior.

Ethical Issues in the Nonprofit Sector

These organizational dynamics play out in distinctive ways in the nonprofit sector. There are six areas in particular where ethical issues arise in the nonprofit sector: compensation; conflicts of interest;

publications and solicitation; financial integrity; investment policies; and accountability and strategic management.

Compensation. Salaries that are modest by business standards can cause outrage in the nonprofit sector, particularly when the organization is struggling to address unmet societal needs. In a March 23, 2009, *Nation* column, Katha Pollitt announced that she "stopped donating to the New York Public Library when it gave its president and CEO Paul LeClerc a several hundred thousand-dollar raise so his salary would be $800,000 a year." That, she pointed out, was "twenty times the median household income." Asking him to give back half a million "would buy an awful lot of books—or help pay for raises for the severely underpaid librarians who actually keep the system going." If any readers thought LeClerc was an isolated case, she suggested checking Charity Navigator for comparable examples.

The problem is not just salaries. It is also the perks that officers and unpaid board members may feel entitled to take because their services would be worth so much more in the private sector. A widely publicized example involves William Aramony, the former CEO of United Way of America, who served six years in prison after an investigation uncovered misuse of the charity's funds to finance a lavish lifestyle, including luxury condominiums, personal trips, and payments to his mistress.[18] Examples like Aramony ultimately prompted the IRS to demand greater transparency concerning nonprofit CEO compensation packages exceeding certain thresholds.[19]

Nonprofits also face issues concerning benefits for staff and volunteers. How should an organization handle low-income volunteers who select a few items for themselves while sorting through noncash contributions? Should employees ever accept gifts or meals from beneficiaries or clients? Even trivial expenditures can pose significant issues of principle or public perception.

Travel expenses also raise questions. Can employees keep frequent flyer miles from business travel? How does it look for cash-strapped federal courts to hold a judicial conference at a Ritz-Carlton hotel, even though the hotel offered a significantly discounted rate? The Panel on the Nonprofit Sector recommends in its *Principles for Good Governance and Ethical Practice* that organizations establish clear written policies about what can be reimbursed and require that travel expenses be cost-effective. But what counts as reasonable or cost-effective can be open to dispute, particularly if the nonprofit has wealthy board members or executives accustomed to creature comforts.

Conflicts of Interest. Conflicts of interest arise frequently in the nonprofit sector. The Nature Conservancy encountered one such problem in a "buyer conservation deal." The organization bought land for $2.1 million and added restrictions that prohibited development such as mining, drilling, or dams, but authorized construction of a single-family house of unrestricted size, including a pool, a tennis court, and a writer's cabin. Seven weeks later, the Nature Conservancy sold the land for $500,000 to the former chairman of its regional chapter and his wife, a Nature Conservancy trustee. The buyers then donated $1.6 million to the Nature Conservancy and took a federal tax write-off for the "charitable contribution." [20]

Related conflicts of interest arise when an organization offers preferential treatment to board members or their affiliated companies. In another Nature Conservancy transaction, the organization received $100,000 from SC Johnson Wax to allow the company to use the Conservancy's logo in national promotion of products, including toilet cleaner. The company's chairman sat on the charity's board, although he reportedly recused himself from participating in or voting on the transaction.[21]

These examples raise a number of ethical questions. Should board members obtain contracts or donations for their own organizations? Is the board member's disclosure and abstention from a vote enough? Should a major donor receive special privileges, such as a job or college admission for a child? In a recent survey, a fifth of nonprofits (and two-fifths of those with more than $10 million in annual expenses) reported buying or renting goods, services, or property from a board member or an affiliated company within the prior two years. In three-quarters of nonprofits that did not report

> ONE OF THE MOST CRITICAL STEPS NONPROFITS CAN TAKE TO PROMOTE ETHICAL CONDUCT IS TO ENSURE THAT THEY HAVE ADEQUATE ETHICAL CODES AND EFFECTIVE COMPLIANCE PROGRAMS.

any such transactions, board members were not required to disclose financial interests in entities doing business with the organization, so its leaders may not have been aware of such conflicts.[22]

Despite the ethical minefield that these transactions create, many nonprofits oppose restrictions because they rely on insiders to provide donations or goods and services at below-market rates. Yet such quid pro quo relationships can jeopardize an organization's reputation for fairness and integrity in its financial dealings. To maintain public trust and fiduciary obligations, nonprofits need detailed, unambiguous conflict of interest policies, including requirements that employees and board members disclose all financial interest in companies that may engage in transactions with the organization. At a minimum, these policies should also demand total transparency about the existence of potential conflicts and the process by which they are dealt with.

Publications and Solicitation. Similar concerns about public trust entail total candor and accuracy in nonprofit reports. The Red Cross learned that lesson the hard way after disclosures of how it used the record donations that came in the wake of the 9/11 terrorist attacks. Donors believed that their contributions would go to help victims and their families. The Red Cross, however, set aside more than half of the $564 million in funds raised for 9/11 for other operations and future reserves. Although this was a long-standing organizational practice, it was not well known. Donor outrage forced a public apology and redirection of funds, and the charity's image was tarnished.[23]

As the Red Cross example demonstrates, nonprofits need to pay particular attention to transparency. They should disclose in a clear and non-misleading way the percentage of funds spent on administrative costs—information that affects many watchdog rankings of nonprofit organizations. Transparency is also necessary in solicitation materials, grant proposals, and donor agreements. Organizations cannot afford to raise funds on the basis of misguided assumptions, or to violate public expectations in the use of resources.

Financial Integrity. Nonprofit organizations also face ethical dilemmas in deciding whether to accept donations that have any unpalatable associations or conditions. The Stanford Institute for Research on Women and Gender, for example, declined to consider a potential gift from the Playboy Foundation. By contrast, the ACLU's Women's Rights Project, in its early phase, accepted a Playboy Foundation gift, and for a brief period sent out project mailings with a Playboy bunny logo.[24] When Stanford University launched an ethics center, the president quipped about what level of contribution would be necessary to name the center and whether the amount should depend on the donor's reputation. If "the price was right," would the university want a Ken Lay or a Leona Helmsley center on ethics?

Recently, many corporations have been attempting to "green" their image through affiliations with environmental organizations, and some of these groups have been entrepreneurial in capitalizing on such interests. The Nature Conservancy offered corporations such as the Pacific Gas and Electric Co. and the Dow Chemical Co. seats on its International Leadership Council for $25,000 and up. Members of the council had opportunities to "meet individually with Nature Conservancy staff to discuss environmental issues of specific importance to the member company." [25]

There are no easy resolutions of these issues, but there are better and worse ways of addressing them. Appearances matter, and it sometimes makes sense to avoid affiliations where a donor is seeking to advance or pedigree ethically problematic conduct, or to impose excessive restrictions on the use of funds.

Investment Policies. Advocates of socially responsible investing argue that nonprofit organizations should ensure that their financial portfolio is consistent with their values. In its strongest form, this strategy calls for investing in ventures that further an organization's mission. In its weaker form, the strategy entails divestment from companies whose activities undermine that mission. The issue gained widespread attention after a Jan. 7, 2007, *Los Angeles Times* article criticized the Bill & Melinda Gates Foundation for investing in companies that contributed to the environmental and health problems that the foundation is attempting to reduce.

Many nonprofit leaders have resisted pressure to adopt socially responsible investing principles on the grounds that maximizing the financial return on investment is the best way to further their organization's mission, and that individual divestment decisions are unlikely to affect corporate policies. Our view, however, is that symbols matter, and that similar divestment decisions by large institutional investors can sometimes influence corporate conduct. Hypocrisy, as French writer François de La Rochefoucauld put it, may be the "homage vice pays to virtue," but it is not a sound managerial strategy. To have one set of principles for financial management and another for programmatic objectives sends a mixed moral message. Jeff Skoll acknowledged as much following his foundation's support of *Fast Food Nation*, a dramatic film highlighting the adverse social impacts of the fast-food industry. "How do I reconcile owning shares in [Coca-Cola and Burger King] with making the movie?" he asked.[26] As a growing number of foundations recognize, to compartmentalize ethics inevitably marginalizes their significance. About a fifth of institutional investing is now in socially screened funds, and it is by no means clear that these investors have suffered financial losses as a consequence.[27]

Accountability and Strategic Management. By definition, nonprofit organizations are not subject to the checks of market forces or majoritarian control. This independence has come under increasing scrutiny in the wake of institutional growth. In 2006, after a $30 billion gift from Warren Buffet, the Gates Foundation endowment doubled, making it larger than the gross domestic product of more than 100 countries. In societies where nonprofits serve crucial public functions and enjoy substantial public subsidies (in the form of tax deductions and exemptions), this public role also entails significant public responsibilities. In effect, those responsibilities include fiduciary obligations to stakeholders—those who fund nonprofits and those who receive their services—to use resources in a principled way. As a growing body of work on philanthropy suggests, such accountability requires a well-informed plan for furthering organizational objectives and specific measures of progress. A surprising number of nonprofits lack such strategic focus. Many operate with a "spray and pray" approach, which spreads assistance across multiple programs in the hope that something good will come of it. Something usually does, but it is not necessarily the cost-effective use of resources that public accountability demands.

Money held in public trust should be well spent, not just well-intentioned. But in practice, ethical obligations bump up against significant obstacles. The most obvious involves evaluation. Many nonprofit initiatives have mixed or nonquantifiable outcomes. How do we price due process, wilderness preservation, or gay marriage?

Although in many contexts objective measures of progress are hard to come by, it is generally possible to identify some indicators or proxies. Examples include the number and satisfaction of people affected, the assessment of experts, and the impact on laws, policies, community empowerment, and social services. The effectiveness of evaluation is likely to increase if organizations become more willing to share information about what works and what doesn't. To be sure, those who invest significant time and money in social impact work want to feel good about their efforts, and they are understandably reluctant to spend additional resources in revealing or publicizing poor outcomes. What nonprofit wants to rain on its parade when that might jeopardize public support? But sometimes at least a light drizzle is essential to further progress. Only through pooling information and benchmarking performance can nonprofit organizations help each other to do better.

Promoting Ethical Decision Making

Although no set of rules or organizational structures can guarantee ethical conduct, nonprofits can take three steps that will make it more likely.

Ensure Effective Codes of Conduct and Compliance Programs. One of the most critical steps that nonprofits can take to promote ethical conduct is to ensure that they have adequate ethical codes and effective compliance programs. Codified rules can clarify expectations, establish consistent standards, and project a responsible public image. If widely accepted and enforced, codes can also reinforce core values, deter misconduct, promote trust, and reduce the organization's risks of conflicting interests and legal liability.

> WHERE THERE IS NO CONSENSUS ABOUT ETHICALLY APPROPRIATE CONDUCT, LEADERS SHOULD STRIVE FOR A DECISION-MAKING PROCESS THAT IS TRANSPARENT AND RESPONSIVE.

Although the value of ethical codes and compliance structures should not be overlooked, neither should it be overstated. As empirical research makes clear, the existence of an ethical code does not of itself increase the likelihood of ethical conduct. Much depends on how standards are developed, perceived, and integrated into workplace functions. "Good optics" was how one manager described Enron's ethical code, and shortly after the collapse, copies of the document were selling on eBay, advertised as "never been read." [28]

A recent survey of nonprofit organizations found that only about one third of employees believed that their workplace had a well-implemented ethics and compliance program. This figure is higher than the corresponding figure for the business (25 percent) and government (17 percent) sectors, but still suggests ample room for improvement.[29] Part of the problem lies with codes that are too vague, inflexible, or narrow. Only about half of nonprofit organizations have conflict of interest policies, and fewer than one third require disclosure of potentially conflicting financial interests.[30] A related difficulty is compliance programs that focus simply on punishing deviations from explicit rules, an approach found to be less effective in promoting ethical behavior than approaches that encourage self-governance and commitment to ethical aspirations.[31]

To develop more effective codes and compliance structures, nonprofit organizations need systematic information about how they operate in practice. How often do employees perceive and report ethical concerns? How are their concerns addressed? Are they familiar with codified rules and confident that whistle-blowers will be protected from retaliation? Do they feel able to deliver bad news without reprisals?

Promote Effective Financial Management. Another step that nonprofits can take to foster ethical behavior and promote public trust is to use resources in a socially responsible way. In response to reports of bloated overhead, excessive compensation, and financial mismanagement, watchdog groups like Charity Navigator have begun rating nonprofits on the percentage of funds that go to administration rather than program expenditures. Although this rating structure responds to real concerns, it reinforces the wrong performance measure, distorts organizational priorities, and encourages disingenuous accounting practices. Groups with low administrative costs may not have the scale necessary for social impact. The crucial question that donors and funders should consider in directing their resources is the relative cost-effectiveness of the organization. Yet according to a 2001 study by Princeton Survey Research Associates, only 6 percent of Americans say that whether a program "makes a difference" is what they most want to know when making charitable decisions. Two-thirds expect the bulk of their donations to fund current programs and almost half expect *all* of their donations to do so. Such expectations encourage charities to provide short-term direct aid at the expense of building long-term institutional capacity.

Moreover, the line these donors draw between "overhead" and "cause" is fundamentally flawed. As Dan Pallotta notes in *Uncharitable*, "the distinction is a distortion." All donations are going to the cause, and "the fact that [a dollar] is not going to the needy now obscures the value it will produce down the road" by investing in infrastructure or fundraising capacity. Penalizing charities for such investments warps organizational priorities. It also encourages "aggressive program accounting," which allocates fundraising, management, and advertising expenses to program rather than administrative categories. Studies of more than 300,000 tax returns of charitable organizations find widespread violation of standard accounting practices and tax regulations, including classification of accounting fees and proposal writing expenses as program expenditures.[32]

To address these issues, nonprofit organizations need better institutional oversight, greater public education, and more transparent and inclusive performance measures. Ensuring common standards for accounting and developing better rating systems for organizational effectiveness should be a priority.

Institutionalize an Ethical Culture. In its *National Nonprofit Ethics Survey*, the Ethics Resource Center categorizes an organization as having a strong ethical culture when top management leads with integrity, supervisors reinforce ethical conduct, peers display a commitment to ethics, and the organization integrates its values in day-to-day decision making. In organizations with strong ethical cultures, employees report far less misconduct, feel less pressure to compromise ethical commitments, and are less likely to experience retaliation for whistle-blowing.[33] This survey is consistent with other research, which underscores the importance of factoring ethical concerns into all organizational activities, including resource allocation, strategic planning, personnel and compensation decisions, performance evaluations, auditing, communications, and public relations.

Often the most critical determinant of workplace culture is ethical leadership. Employees take cues about appropriate behavior from those at the top. Day-to-day decisions that mesh poorly with professed values send a powerful signal. No organizational mission statement or ceremonial platitudes can counter the impact of seeing leaders withhold crucial information, play favorites with promotion, stifle dissent, or pursue their own self-interest at the organization's expense.

Leaders face a host of issues where the moral course of action is by no means self-evident. Values may be in conflict, facts may be contested or incomplete, and realistic options may be limited. Yet although there may be no unarguably right answers, some will be more right than others—that is, more informed by available evidence, more consistent with widely accepted principles, and more responsive to all the interests at issue. Where there is no consensus about ethically appropriate conduct, leaders should strive for a decision-making process that is transparent and responsive to competing stakeholder interests.

Nonprofit executives and board members also should be willing to ask uncomfortable questions: Not just "Is it legal?" but also "Is it fair?" "Is it honest?" "Does it advance societal interests or pose unreasonable risks?" and "How would it feel to defend the decision on the evening news?" Not only do leaders need to ask those questions of themselves, they also need to invite unwelcome answers from others. To counter self-serving biases and organizational pressures, people in positions of power should actively solicit diverse perspectives and dissenting views. Every leader's internal moral compass needs to be checked against external reference points.

Some three decades ago, in commenting on the performance of Nixon administration officials during the Watergate investigation, then-Supreme Court Chief Justice Warren Burger concluded that "apart from the morality, I don't see what they did wrong." [34] That comment has eerie echoes in the current financial crisis, as leaders of failed institutions repeatedly claim that none of their missteps were actually illegal. Our global economy is paying an enormous price for that moral myopia, and we cannot afford its replication in the nonprofit sphere. ■

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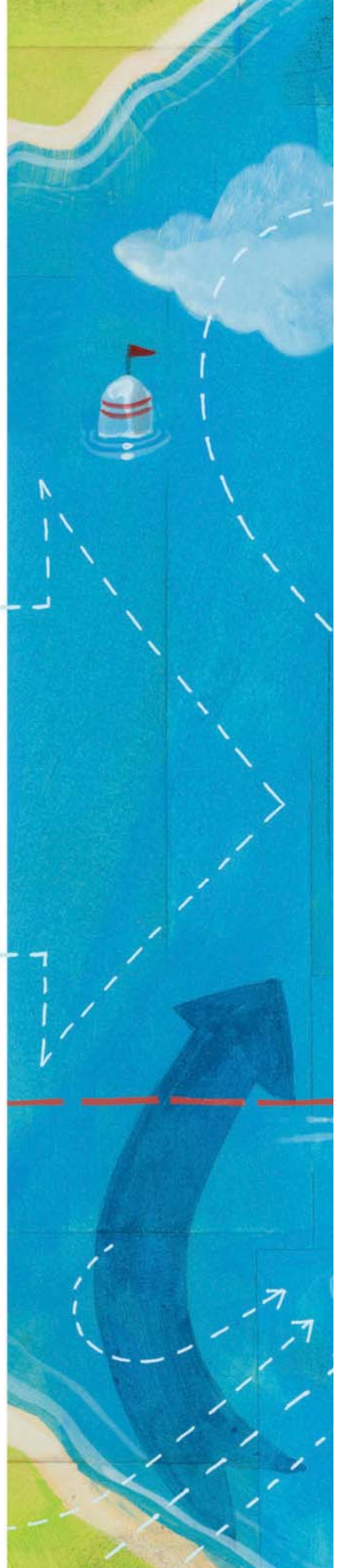
The prevailing governance model is fundamentally adversarial, pitting board members in a never-ending struggle with executives. This model may ensure that the legal requirements of oversight and compliance are met, but it does little to advance the organization's goals. The authors propose a new and more effective framework, one where board members and executives work together to advance the organization's mission.

Mission→Driven Governance

By Raymond Fisman, Rakesh Khurana, & Edward Martenson | Illustration by Leigh Wells



IN 1931, GERTRUDE Vanderbilt Whitney created the Whitney Museum of American Art in a Greenwich Village brownstone and ran it with a narrow circle of family and friends. It was a downtown alternative to the traditional conception of a museum, offering a venue for provocative contemporary art instead of staid old masters. In the 1970s, the Whitney changed. It moved to a new home on Manhattan's Upper East Side—an iconic Marcel Breuer building where it still resides—and added a number of "outside" directors to the board in an effort to expand its base of support. So began three decades of wrangling over the museum's identity in a division that *The New York Times* has called the "Curse of the Whitney" and a "fault line in the Whitney board … between old and new money." [1]

The division among the Whitney's leadership over the museum's mission is cultural and values-laden, resulting in operational and programmatic choices that have seemed inconsistent or even contradictory. The Whitney has earned a reputation for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"chaotic" [2] governance. Three highly ambitious building expansion plans have been floated with great fanfare, only to be killed before ground was broken. Until the present incumbent, Adam D. Weinberg, the tenure of the Whitney's directors had been getting steadily shorter, and they've been alternately hailed as saviors then blamed for the museum's inability to move forward. Turnover among curators and other staff has also been high. Expenses have grown substantially as the Whitney competes with blockbuster exhibitions and elevated audience amenities in other museums. The collecting policy has shifted from low cost to lavish: The museum once identified artists before their work became highly valued in the marketplace, but it now often enters into bidding wars for the works of modern masters. Underendowed in comparison to its peers, the Whitney loses ground year after year to "more robust" [3] rivals like the Museum of Modern Art and the Solomon R. Guggenheim Museum.

These problems and challenges reflect two largely unarticulated but dialectical views of the Whitney's mission. Gertrude Whitney's vision was essentially forward-looking, dedicated to working artists and to identifying trends in modern American art as they emerged. By contrast, the "professionalized" Whitney that began to evolve in the 1970s is a "real" museum with a historical perspective, with the purpose of illuminating the achievements of modern American art and therefore oriented to the art rather than the artists. Collecting high-priced American masters is a necessity in this latter vision, but selling off earlier acquisitions that had appreciated in price in order to make way for new works would be more consistent with the former. The Whitney Biennial exhibition, the source of the museum's reputation as the tastemaker in modern American art, is a flat-out necessity in Gertrude Whitney's original vision but might be no more than a pleasing embellishment to the other. In one version of the Whitney's mission, expansion of the physical museum is essential in order to present high-impact exhibitions with advanced visitor amenities, and in the other it's an unneeded extravagance.

The inability of boards of directors and nonprofit executives to keep their organizations focused on a clearly articulated mission is a significant and overlooked governance problem.

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Rather than replacing one mission with another, the Whitney has tried to sidestep the debate by combining the two versions in an unsatisfactory synthesis. This has made neither faction happy, with the perhaps predictable result of much high-level discontent within the institution that has all too often been exposed to public view. The unwillingness of the Whitney's leadership to choose between the two competing missions probably was the easiest path—it may not even have been articulated as a choice—but the Whitney has paid, and continues to pay, a steep price for that avoidance. In 2006, *The New Yorker* pointedly wondered "Will the Whitney Museum ever get it right?" [4] In supreme irony, the Whitney has begun to consider abandoning efforts to expand the Breuer building in favor of a new downtown location. If this turns out to be the museum's new location, it could signal a return to its roots. On the other hand, if the new site is used in addition to the uptown space, it could signal the permanent bifurcation of the Whitney's identity.

The governance problems that lie behind the Whitney's troubled history are not unique. They are indicative of widespread shortcomings in the way that organizations of all kinds and sizes are governed. These governance issues do not get the attention they deserve. Instead, scandals such as those at the Smithsonian Institution or American Red Cross get all the media coverage, creating the impression that failures of oversight and compliance should be the primary governance concerns. This diverts attention from remedying governance problems that are more difficult to identify, but that ultimately may result in even greater damage to the organization.

The inability of nonprofit boards and executives to keep their organizations focused on a clearly articulated mission is a significant and overlooked governance problem. The roots of this problem are many and varied. In some cases it is the result of idiosyncratic decisions about direction and growth based on the individual preferences of a top executive, a powerful director, or a big donor. In other cases it is because directors and executives are so protective of their respective roles and responsibilities that they don't talk with one another, or scarcely communicate when they do. In still other cases it is because board members are disengaged, or their energies misspent on efforts that are disconnected from any shared purpose. For each of these problems the result is the same: The organization's progress is held back.

Many directors and executives who are dissatisfied with the state of their organizations' affairs nevertheless resign themselves to the status quo because they don't see how it can be changed. They may believe that solutions require new rules, but new rules are inadequate to treat the performance problems that they encounter most often. They may refuse to see governance as a performance issue because no one likes to be evaluated and board members have the power to avoid it. They may seek simple solutions (with bright-line rules such as the division of labor between the board, which handles policy, and management, which handles implementation) in an area that requires decision makers to integrate many kinds of knowledge into a coherent whole. Or they may have internalized a model of governance that is flawed and out of date.

The existing governance model is fundamentally adversarial, rooted in the paradigm of principal/agent conflict. At its core is an image of governance as a never-ending struggle between "principals" (board members) who guard the organization's resources but have limited information to monitor how these resources are used, and their "agents" (executives) who have insider knowledge and control the information-filtering apparatus of the organization. Many of the concepts and ideas in this traditional model are shaped by a long history of governance failure and organizational pathology. It suffices as a solution to the challenge of meeting legal compliance standards through formal systems, but it utterly fails to show how to create a governance system that supports organizational effectiveness.

We propose a new governance model, one whose effectiveness is measured by the ability of the organization to achieve its mission. This model stands firmly in the line of governance literature that began with a focus on distinct roles and responsibilities for boards and executives,[5] continued with a focus on board organization and board functions,[6] proceeded to focus on the board's role in positioning an organization through mission and strategy,[7] and then concentrated on the search for a more supple interaction between board members and executives.[8] We take this progression to the next logical step by focusing on how to improve the effectiveness of board members and executives in pursuing their common interest in advancing the organization's essential purpose and values.

Perspectives on Governance

Governance has largely been viewed from a legal perspective, emphasizing that the board's function, as overseers of the organization, is to make sure that bad things don't happen. This often results in a boardroom dynamic that looks something like this: "Let's look for what's wrong with proposal x." Accountability and oversight are absolutely necessary in achieving and maintaining public trust and the organization's legitimacy, and are therefore necessary elements of good governance. But there are many examples where governance structures that were adequate from a legal perspective still produced bad outcomes. In fact, it is not unusual to observe the simultaneous presence of poor governance and legally adequate accountability.

There is another way to view governance, however, which is the behavioral perspective. Contrary to the legal perspective, which encourages boards to make sure that bad things don't happen, the behavioral perspective encourages boards to make sure that good things do happen. From the behavioral perspective, the goal of governance is organizational success as defined by the organization's mission (not accountability) and it is preoccupied with performance (not structures and controls). To produce good outcomes people have to work together, taking advantage of individual strengths. Consequently, the ideal relationship is based on trust, not rules. The primary activity of the board is not oversight, which often creates a climate of conservatism and risk aversion; it is group decision making that is robust and open to opportunities. The behavioral perspective often manifests itself in a cooperative dynamic that looks something like this: "If proposal x will make us better, let's figure out a way to do it."

The legal perspective focuses on *control*. The behavioral perspective focuses on *performance*. The key to improving corporate governance is incorporating both approaches in a single framework. (See "Perspectives on Corporate Governance" below.) This is more easily said than done. The legal and behavioral perspectives exist in tension, which helps explain the conflicted feelings board members and executives bring into the boardroom. Board members want to be supportive but can't give the executive a free hand. Executives need help from the directors but sometimes feel that the directors are in the way. These tensions can't be eliminated—they are an inherent part of organizational life—but if both perspectives are embraced, the tensions can be made productive.

True North

To incorporate both perspectives, we propose an updated definition of governance: *Governance is how boards of directors and executives work together to ensure the success of their organization.* If governance is about making good decisions in the pursuit of success, the first order of business is to define success. We believe that success is the ability of an organization to accomplish its mission. Ideally, every decision an organization makes should be completely aligned with its mission—what we call True North—and no decision should be made that deviates from this direction. A Shakespeare festival, for example, would produce *Hamlet* but not David Mamet's *Glengarry Glen Ross*, and a symphony orchestra would perform Beethoven's *Symphony No. 4* and avoid Madonna's *Like a Virgin*.

In reality, few decisions take an organization unswervingly along the ideal path it has chosen. Nearly all decisions involve some deviation from True North. Some decisions involve a conscious compromise that deviates only slightly, whereas other decisions deviate significantly from the organization's mission. Some decisions are nondecisions, or continuations along a path of least resistance, but that nevertheless take the organization off course. All of these decisions, however, move in a direction other than True North. One way to define good governance is the board and executives' ability to keep the organization's actions within an acceptably narrow range around True North.

In our hypothetical Shakespeare festival, management might decide to produce a new play on the grounds that it would then get the inside track on the author's next great adaptation of a classical text. This would be a slight deviation from True North. A more drastic deviation from True North would be a decision to present a program of contemporary performance art in the theater lobby. A

PERSPECTIVES ON CORPORATE GOVERNANCE

	LEGAL PERSPECTIVE	BEHAVIORAL PERSPECTIVE
GOAL	Accountability	Success
PREOCCUPATION	Structures and controls	Performance
MEANS	Relationships based on rules	Relationships based on trust
PRIMARY ACTIVITY	Oversight	Group decision making

still more drastic deviation from True North would be a decision to install gold faucets in the bathrooms, which does nothing to further the mission of the organization. (One might think that "gold faucets" decisions are rare, but they are in fact common. A performing arts center we know of decided to install expensive custom carpet in the lobby, which did little to meet the audience's cultural needs.)

How does an organization know what its True North is? Volumes have been written about how organizations can identify their mission; all of them center on a clear sense of the social benefit the organization exists to provide. The important point for the purposes of this article is that an astonishing number of organizations appear not to know their True North, or to have varying degrees of internal disagreement about it.

Deviating from True North

We are using admittedly stylized examples to illustrate two relatively sophisticated points: The vast majority of decisions involve trade-offs, ones that should be evaluated carefully in relation to the purpose embedded in the mission; and the cost of deviations from True North can be high and even dangerous.

If our hypothetical Shakespeare festival were to devote six weeks of its performance schedule to its new play, that six weeks of time would not be available for a production of, say, *Hamlet*. In this case, the decision involving a direction other than True North crowds out another decision that is closer to True North. All decisions crowd out other paths that might have been taken, and these lost opportunities constitute opportunity costs. Each opportunity cost delays the organization's progress toward fulfillment of its mission.

In one real example, a highly successful museum raised and spent a large amount of money on a parking garage because its market surveys said that visitors were very dissatisfied with the lack of convenient parking. As it turned out, attendance did not increase after the parking garage was built. That's because visitors were ultimately attracted by memorable exhibits, not parking. The museum had to wait five years before conducting another major fundraising campaign to create its next highly praised exhibits. It had used a scarce fundraising opportunity on a project that brought precious little progress in the direction of True North.

On other occasions organizations are lured off course by the promise of large amounts of money. In the 1980s and '90s, for example, many funders made large grants to arts organizations to get them more involved in arts education. The public education system had been responsible for arts education, but these programs were an early casualty of cutbacks in government education funding. Most arts organizations hadn't seen arts education as part of their missions, but they accepted the large grants because it was a lot of money. Many people count this a success story in philanthropy because education is now thoroughly embedded in arts organizations' programs: There is a new True North. Nevertheless, money spent on arts education is money not spent on actor salaries, or new symphonies, or touring into rural areas.

One of the problems organizations encounter when they adopt programs that deviate from their mission in order to secure large donations or grants is that the funds seldom cover the full cost of the program. Consequently, in addition to the initial opportunity cost, organizations often find themselves pulling scarce resources away from projects that are closer to True North to cover a portion of the new activity not covered by the initial grant. Moreover, such grants usually provide support for a limited time, so if the activity continues beyond the grant period (as they generally do) even more resources must be pulled away from core activities. Perversely, the bigger and more extravagant (and hence more tempting) the gift, the greater the hidden cost generally turns out to be in future years. In our unnamed performing arts center with the custom carpet weave, the major donor's gift was insufficient to provide for ongoing upkeep of the building, and artistic programs have been constrained for decades because of the high cost of maintenance. Every time a section of the carpet wears thin, a fresh run of the custom weave is ordered to patch it.

Activities that deviate from True North also tend to create their own special interest constituencies whose goals are aligned with the specific activity rather than with the mission of the organization. The resulting factions work to shift the organization's True North in the direction that interests them the most, pulling resources away from True North as the new activity's constituency seeks more resources to support its own desires. Well-governed organizations learn to look a gift horse in the mouth, at least those gift horses that deviate too drastically from True North.

Five Causes of Deviation

There are five principal reasons why organizations deviate from True North: the organization's mission is unclear or misguided; the decision-making culture is flawed; the leaders are unable to share responsibility; the board's composition or organization is suboptimal; or the leaders lack important information.

1. Unclear or Misguided Mission

A small museum has earned a strong reputation by collecting and exhibiting works that reflect its region's indigenous culture. It accepts a bequest from a local artist who is nationally known for his work in a particular kind of abstraction. The gift includes a collection of artworks and funds to construct a special gallery to put them on permanent exhibition, but it does not include funds for future upkeep of the art or facility. The museum assumes that it will be able to cover these costs through more effective future fundraising.

The decision by the leaders of this small museum to accept this bequest was a sharp departure from True North, clearly at odds with the museum's stated mission, but there was no resistance to the decision internally or externally. On the contrary, the opportunity was seen by many as a "no-brainer." The artist's work was sought after by major museums of national reputation, so for a small museum to receive a collection of his work was quite a coup. But now potential donors and visitors are less sure what the museum stands for. It may be even more difficult in the future to say "no" to other bequests that lie outside the museum's mission. And maintaining the new exhibit requires the museum to draw resources from other activities.

Satisfying the desires of important stakeholders—donors in particular—is an obvious temptation, but risks pulling the organization off course. This temptation is even stronger when the organization does not have a clear direction, allowing individual stakeholders to interpret the mission in self-serving ways, which makes the mission even more diffuse. Lacking clear direction, stakeholders begin to lose energy and disagree about whether the organization is succeeding. Decisions get made by opportunities rather than by conscious planning.

Establishing a clear and focused mission, and using it as the discipline to decide what to do and what not to do, is the most important function of governance. The organization's mission, strategy, top-level policies, and resource allocations should be reviewed regularly and in depth. Every deployment of financial, human, and other resources should be tested against the mission and strategy.

To guard against having an unclear or misguided mission, decision makers should regularly ask themselves questions like these: What is the social benefit gained by the organization's existence? How important is the social benefit? Does the mission have meaning for stakeholders, or is it just boilerplate for grant applications? Do you know the organization's competitive advantage, and who its customers are? Have you ever turned down a big grant (or paid some other substantial price) because it was inconsistent with the organization's mission?

2. Flawed Decision-Making Culture

A small and homogeneous museum board decides to diversify in order to broaden the organization's base of financial support, and it does so quickly without taking time to create a new collective vision. Previously, decisions were made in private unanimity. Subsequently—over an extended period of years—the board exhibited factional discord over major decisions, often in public.

One reason why a precisely articulated mission is important is that it automatically tests whether the values that decision makers bring to the table are consistent. Decision makers are unlikely to join an organization—or be invited to do so—if they aren't in tune with the organization's existing direction, but if the existing direction is unclear, how is anyone to know? The inevitable result is a flawed decision-making culture, in which making decisions becomes ever more difficult, factions take shortcuts simply to get things done, and others end up feeling disenfranchised—making decisions still more difficult.

Governance is group decision making. *How* a decision is made can have a profound impact on *what* decision is made. A strong culture helps governance be decisive, but if the culture is too strong it can freeze out useful perspectives. In a weak culture, the organization's direction may need to be argued afresh in the face of even the most innocuous decision. Factions are common, and the longer they remain the more they dig in their heels. Some members of the group feel marginalized or ignored, and often resort to hidden agendas and covert channels of communication to get their way. Under these circumstances, decision making can be neither efficient nor robust.

The ideal decision-making culture is one that welcomes divergent perspectives. People are unified by common purpose and value the organization in similar ways, but they are able to disagree about means and methods without rancor. Disagreements strengthen the group rather than undermining it. A critical element of a healthy decision-making culture is a fabric of relationships based on trust.

To guard against having a flawed decision-making culture, decision makers should regularly ask themselves questions like these: Do people in the group value the same things? Is there consensus about the criteria for judging success? Do we spend time creating good processes? Are decisions made openly and for explicit reasons, or behind closed doors for motives that aren't always clear? Is disagreement useful, or is it dangerous? Are decisions made in small groups and then rubber-stamped, or does every vote count?

3. Inability to Share Responsibility

An executive director of a performing arts center initiates a number of highly visible activities that seem to constitute a change of the organization's strategy, but never explicitly discusses the new direction with the board. Board discord inevitably follows, but it emerges in relation to the specific initiatives and never gets to the deeper issue of the relationship. The executive director frames the decision on every initiative as a vote of confidence. Board members feel manipulated and ineffectual.

Mistrust or lack of respect between an organization's top executive and its board members often leads to conflict and paralysis, a common governance dysfunction. A board of directors delegates substantial elements of its powers to the executive and retains other powers to be exercised collectively. The responsibilities delegated to the executive inevitably overlap with the retained powers of the board, and the executive acts both individually and as a member of the decision-making group. It follows that the working relationship between directors and the executive is a pivotal factor in the quality of their decisions.

In the most effectively governed organizations, relationships of trust permit directors and executives to share responsibilities without undermining their formal roles and responsibilities. Influence flows from expertise, not from positions, in different ways and at different times. Organizations should be less concerned with protecting respective roles and more focused on maximizing the impact of their human resources. No organization should fail to put available knowledge and skills to good use simply because they reside in the board rather than in the staff, or vice versa. Implementation roles for board members are inevitable, as are substantive policy roles for executives.

The board should look to the executive to exercise leadership and provide expertise that board members lack. The executive should respect the board's fiduciary responsibility and be willing to defer to board members in areas where they have greater expertise. Respect is necessary, and the lack of it may indicate the need for a change in attitudes if not in personnel.

Clarity in roles and responsibilities is good practice, but if a low level of trust requires roles to be respected religiously, the organization cannot take advantage of individual strengths nor compensate for individual limitations.

To guard against the problem of poor sharing of responsibility by board members and executives, decision makers should regularly ask themselves questions like these: Do the board and the executive have clear roles and responsibilities? Do they have to guard those roles and responsibilities from each other, or can they share tasks according to skills and experience? Do directors regard the executive as a leader or as an employee?

4. Suboptimal Board

The board of a ballet company with a long and distinguished history is composed of members and friends of the generous founding family. Because of the company's past success, many patrons feel a high degree of loyalty and ownership, but their views are not represented in the company's governance. The company is regarded as out of touch by many of its patrons.

One of the primary reasons that organizations veer off course is that their boards do not have the right people on them or the board's responsibilities have not been sufficiently defined. In both instances, the board's ability to make good decisions is handicapped. Without a properly composed board and effective system of operation, the nonprofit's stakeholders will not be fully represented when important decisions are made.

Too often, boards represent a narrow range of views. Instead, the board should represent a range of stakeholder perspectives (all united around the organization's mission) and a diversity of views about how the organization pursues its mission. This creates a productive tension among board members and between the board and the organization's top executive.

Boards have a tendency to grow large and unwieldy to accommodate fundraising needs rather than governance concerns. Curiously, the need for diverse perspectives often seems easier to overlook in organizations with very large boards. Major decisions, including such primary board responsibilities as hiring and evaluating the chief executive, must not be made entirely in committees. This practice excludes many potentially useful viewpoints and leaves many individual directors feeling left out and disengaged. Board roles and responsibilities should be clearly defined in writing, in what amounts to a job description.

To guard against the problem of suboptimal board composition and organization, decision makers should regularly ask themselves questions like these: Are important decisions made by a few individuals and rubber-stamped by the group? Are directors drawn from a variety of backgrounds, or do fundraising and social considerations dominate appointment decisions, often leading to the addition of new members much like those already on the board? Is there a strategic process for reviewing the board's composition in relation to the organization's changing needs for skills and stakeholder perspectives? Does the board include a number of potential future leaders to choose among?

5. Incomplete Information

A community performing arts center is committed to keeping its ticket prices low so that people with low incomes can afford to attend. The managers of the center had not conducted audience research because attendance had been consistently high. When the center needed to raise revenues, it conducted an audience survey, and much to the surprise of the staff and board, the survey revealed that most of their patrons came from high-income households. Because decision makers lacked this critical information, they had not raised ticket prices, depriving the organization of money that could have fueled faster progress in fulfilling its mission.

Otherwise well-functioning boards can go off course when decision makers fail to collect and disseminate data effectively, resulting in the lack of necessary information to guide decisions. Among the reasons that decision makers give for not systematically collecting data are cost, level of difficulty, and the inevitable imperfection of information. Yet many organizations don't bother to collect facts and figures that are easily available at little cost or effort.

Decision makers often prefer not to have objective data, because this information might contradict the decisions they are inclined to make. This is a natural human inclination, and an important role of routine information gathering is to guard against it. Disconfirming data is at least as important as confirming data. Collecting and assessing data also forces the board to think hard about what is an appropriate measure of organizational success.

To guard against the problem of incomplete information, decision makers should regularly ask themselves questions like these: Do we really know our organization's industry, including its traditions and its challenges? Do we really know what our audience, donors, and employees think? What are our legal and economic exposures? Has actual performance matched our plans and aspirations?

New Governance Practices

Organizations that want to steer True North need to evaluate whether their existing governance practices support effective decision making. From our own work with scores of organizations and observation of hundreds of others, we have identified a number of common practices that bear reexamination.

Getting Leaders to Evaluate Their Governance Performance. It is difficult to get executives and board members to evaluate their own performance. An influential leader, usually on the board, must be willing to say, "Maybe we could do better." Once the subject is on the table for discussion, agreement to adopt a governance self-evaluation routine often follows with relative ease. It's even easier to devise a mechanism for self-evaluation. All that is needed is to identify the questions that should be asked in relation to each of the five sources of deviation from True North previously described. But starting this conversation is critically important. An organization that does not work in a systematic way to improve its governance performance is simply not doing its job.

Building Relationships Based on Trust. Robust decision making requires candor and courage, qualities that are difficult for a group to muster in the absence of trust, both among board members and between board members and the executives. Having that trust is one of an organization's greatest strengths. Because trust is easier to fracture than to create, the critical factor in building trust is to avoid any processes or actions that undermine it. The key to this is creating transparent group interactions: valuing bilateral influence (being open to persuasion through active listening); being explicit about the logic of each decision (eschewing private agendas); and being overt in the tactics that are used to reach decisions (eschewing manipulation).[9] In general, if leaders want to build trust, they should give as much attention to making decisions transparently as they do to the decisions themselves.

Distinguishing Governance from Other Tasks. Every nonprofit depends on board members to raise money and perform other implementation tasks in areas where the organization and its staff lack resources or expertise. This provides board members with a hands-on understanding of the organization and also helps to give greater meaning and depth to board members' involvement. Because such responsibilities often are critically important, there is an unfortunate tendency to conflate the board's governance function with its implementation roles, to the detriment of a clear

For the stewards of any type of organization, the first step is figuring out which direction to steer the ship, and then working together to make sure it stays on course.

understanding of the nature and primacy of governance. Fundraising is not governance.

Articulating the Organization's Mission and Strategy. The most important governance decision a board and its executives can make is to articulate clearly the organization's mission and strategy. This decision should be "owned" by the board and executives. Having a clear mission and strategy is a critical factor in motivating donors and employees. The organization's mission and strategy should be the product of painstaking analysis: rigorous, ambitious, precise, visionary, and compelling. Identifying mission and strategy should never be treated as a fundraising exercise. All operating and policy decisions should be tested for alignment with the mission and strategy.

Planning for Leadership Succession. Choosing a chief executive is among the most important of all governance decisions. It is essential to adopt a strategic approach to identifying the leadership qualities and skills that are needed for the organization to succeed in a changing environment. The time to establish an orderly leadership succession process is well before it is needed. (That doesn't mean forming a short list of candidates, adopting a bias toward external or internal candidates, or predetermining factors that would tie the hands of a selection committee.) Adopting a process in advance saves time at the point of succession and gives board members confidence that they are prepared. It is disturbing that so few boards build succession processes into their regular planning agenda. This often means that hasty or idiosyncratic leadership selections are made in an atmosphere of pressure, stress, or crisis.

Making Decisions with the Full Board. The full board is the final decision maker, and no member should be excluded from critical deliberations. Small-group processes not only alienate other members, but also undermine trust and engagement. The board should not be cast in the role of rubber stamp for committee recommendations. On the contrary, the role of committees and other small groups should be defined in ways that reinforce full-group engagement. Board decisions can be made effectively in a group of between 15 and 25 people without the necessity for committees or other small-group breakouts. If a large board is necessary, attention should be paid to maintaining the subsidiary role of committees—the executive committee in particular. Some committees will continue to be necessary, but they can be charged with defining alternatives rather than making recommendations. The size of the board should be driven by decision-making considerations, not by fundraising.

Creating Systematic Flows of Information. Informed decision makers make better decisions, and a systematic approach to education and information gathering helps to ensure that important knowledge is not overlooked. An orientation program for new board members and executives can help with this, getting them up to speed on the industry and the organization's mission and strategy. It can also inculcate a sense of the organization's culture. Educational components should be incorporated into each meeting agenda in order to deepen the decision makers' knowledge and instill the habit of organizational learning. Few organizations have systematic information-gathering routines, and as a result they risk making unnecessary errors. The lack of updated environmental analysis and program evaluation should be as unthinkable as not having current financial statements.

Not Just for Nonprofits

Although we have written this article using examples from arts organizations and with nonprofit leaders as our primary audience, we believe that our theory of governance performance is applicable to all types of organizations. In fact, for-profits and government entities may derive greater benefit than nonprofits in adopting a less adversarial view of governance. Nonprofits are at least mission driven by their very nature, so it should be more natural for nonprofit leaders to focus on the organization's mission. By contrast, the missions of for-profits often get subsumed by the profit motive that reduces board-executive relationships to pecuniary concerns. The obvious irony is that by focusing on a mission the for-profit organization may very well end up having greater financial success to boot.[10] For the stewards of any type of organization, the first step is figuring out which direction to steer the ship, and then working together to make sure it stays on course. ■

This article is based on a paper prepared for a National Arts Strategies seminar.

Notes

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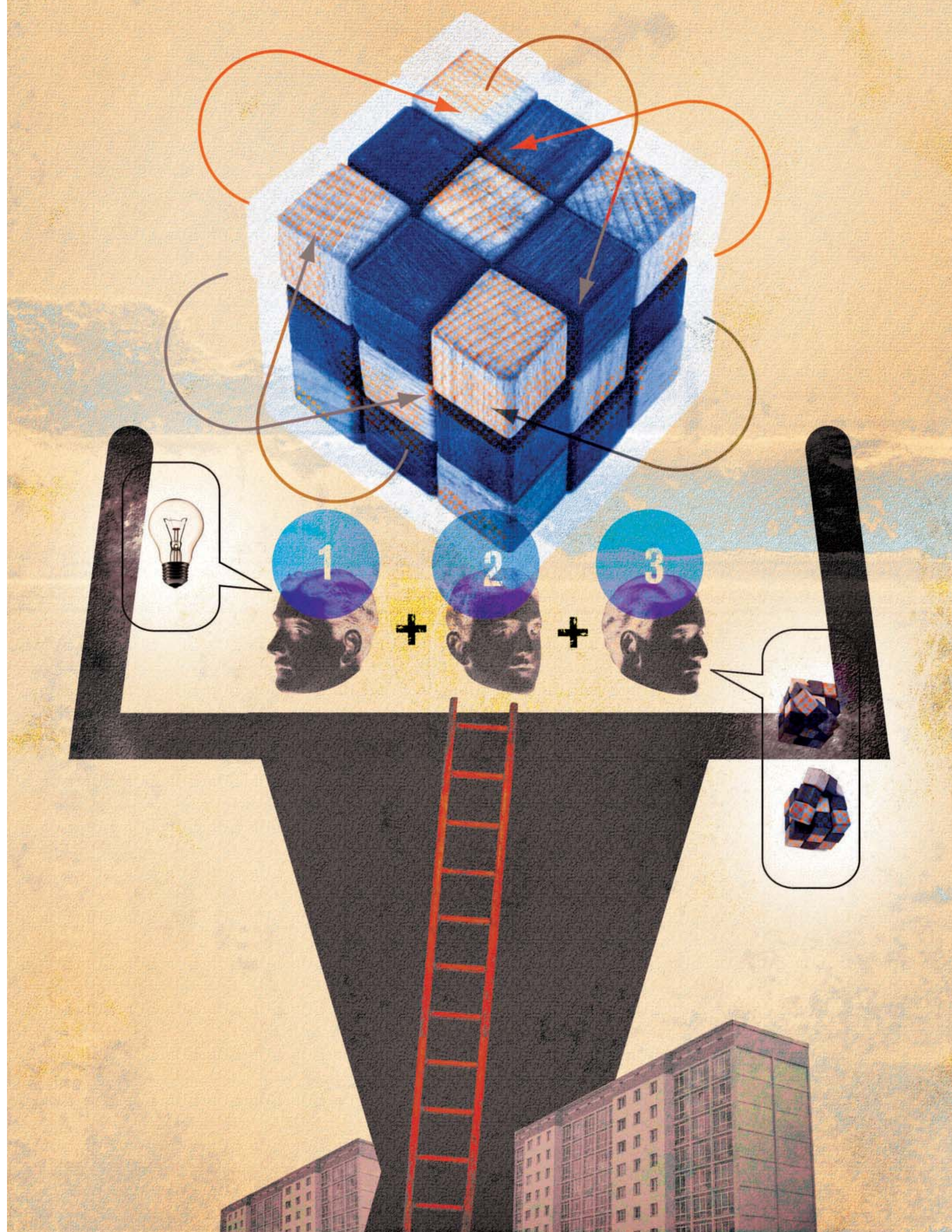
Platforms for Collaboration

By Satish Nambisan | Illustration by Stuart Bradford

Some of the brightest ideas for social change grow in the spaces between organizations and sectors. Yet few organizations have systems that make collaboration happen. To foster innovation, organizations need to develop places where they can come together and work creatively—that is, platforms for collaboration. In this article, a management expert identifies three kinds of collaboration platforms—exploration, experimentation, and execution—and then outlines what organizations can do to put these platforms to work for them.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The Rockefeller Foundation had a simple question: How can you turn a solar-powered flashlight into an all-purpose room light? For parts of the world that lack access to regular electricity, the answer to this question could save lives in hospitals, educate children after dusk, and power cottage industries after the crops are harvested.

Yet no one knew the answer. And so the Rockefeller Foundation paired up with InnoCentive to ask 160,000 independent inventors worldwide how they might transform the flashlight. The inventors were part of a Web-based network of "solvers" that InnoCentive, a privately held company, has established. InnoCentive is an innovation intermediary—an organization that brokers relationships between those with questions and those who might have the answers.[1] Organizations with specific technical problems pose their problems on the InnoCentive Web site and offer the solvers large financial rewards for the best solutions. An electrical engineer in New Zealand named Russell McMahon ultimately came up with a flashlight that enhanced the solar battery and LEDs to create a much stronger light.

Meanwhile, north of the border, the Toronto Transit Commission (TTC) was struggling with an overtaxed infrastructure and highly dissatisfied customers. Its 1997-vintage Web site had not been updated for 10 years and had become too cluttered and too corporate-looking for riders to plan trips or find schedules. And its subway cars were not designed to carry their current loads of riders.

Like the Rockefeller Foundation, TTC took its problems to the people. It organized a unique one-day event called Toronto Transit Camp, to which it invited ordinary riders, transit activists, and technology geeks. Attendees then enumerated TTC's problems and suggested creative solutions to them. At the end of the camp, TTC walked away with plans to overhaul its operations—from simplifying the Web site to streamline trip planning, to redesigning subway cars to offer more standing room during rush hour, as well as poles that short people can reach, storage for backpacks, and outlets for computers. The event was so successful that TTC has expanded the collaborative problem-solving exercise into a full-fledged program called Metronauts, which works with several nonprofits and agencies to improve all forms of transportation in the Greater Toronto and Hamilton area.

As these two examples show, social innovation increasingly requires collaboration among diverse networks of nonprofits, government agencies, corporations, and private citizens. These networks promise a wider range of ideas, better use of resources, and faster solutions than do traditional, monolithic entities. (For more on networks for innovation, see "The Networked Nonprofit" in the spring 2008 issue of the *Stanford Social Innovation Review*.) Moreover, in areas such as energy, environment, disaster management, health care, and education, the issues often cross sectoral and organizational boundaries. In the future, much social innovation is likely to happen not within individual sectors, but in the spaces between the different sectors. (For more on cross-sector solutions to social and environmental problems, see "Rediscovering Social Innovation" in the fall 2008 issue of the *Stanford Social Innovation Review*.)

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Yet collaboration demands particular sets of practices and systems—what I call *platforms*. My research over the past few years has revealed three different kinds of collaboration platforms that organizations need for social innovation: *exploration platforms*, *experimentation platforms*, and *execution platforms*. (See "Three Types of Collaboration Platforms" on page 47 for descriptions of the different platforms.) Partners use exploration platforms to define what the problem is; they use experimentation platforms to test possible solutions to the problem; and they use execution platforms to disseminate the solutions.

As is evident, these platforms support different phases of problem solving. Moreover, establishing and participating in each type of platform requires different types of organizational resources and capabilities. To be effective partners in social innovation, organizations need a deeper understanding of these three platforms so that they may develop the necessary skills and resources. This is especially true for nonprofits and government agencies, which are usually the lead partners in most social innovation collaborations.

Exploration: What's the Problem?

Most social issues or problems are multipart puzzles. But when pieces of the puzzle—however minor those pieces may be—are missing, partners may not understand what, exactly, the problem is. Exploration platforms bring together diverse stakeholders so that they may frame problems fully and accurately. Once the partners develop a shared definition of the problem, they can start working on solutions.

For example, the Maryland-based All Hazards Consortium (AHC) is a nonprofit organization that was formed in 2003 to help coordinate the region's disaster management efforts. It organizes an annual event, the All Hazards Forum (AHF), to bring together Mid-Atlantic government agencies, private corporations, nonprofits, universities, and research institutions to identify problems and solutions in the broad areas of disaster management and emergency preparedness. Over the past three years, this exploration platform has helped AHC's members develop shared definitions of problems in several areas, including evacuation planning, infrastructure protection, food security coordination, and regional cyber security.

Consider the evacuation of special-needs populations, a critical issue in emergency management. People with special needs composed about 25 percent to 30 percent of those affected by hurricanes Katrina and Rita. In both instances, government and nonprofit aid agencies had difficulty serving this population.

To coordinate their own efforts, attendees of the 2007 AHF explored their protocols and practices for evacuating people with special needs. Their discussions uncovered two problems. First, the attendees had different notions of what counts as a disability or special need—a disagreement that leads to much confusion during disasters.

For example, although government entities such as the Federal Emergency Management Agency consider people who do not own cars and people with limited English proficiency as having special needs, the American Red Cross does not. AHC partners agreed to develop a common definition of special-needs populations for all aid agencies, both public and private.

Three Types of Collaboration Platforms

	EXPLORATION	EXPERIMENTATION	EXECUTION
Objective	■ Define core problems ■ Connect with problem solvers	■ Develop solution prototypes ■ Test prototypes in near-real-world contexts	■ Build and disseminate solution templates ■ Help adopters adapt to system-wide changes
Role of Lead Organization	■ Build a diverse coalition of stakeholders ■ Give stakeholders numerous and varied forums to air their concerns ■ Identify potential problem solvers	■ Integrate ideas from diverse stakeholders ■ Offer neutral environments for deep testing of solutions	■ Facilitate the collaborative development and diffusion of solution templates ■ Provide resources that adopters can use to manage the "ripple effects" that follow implementation
Desired Outcomes	■ Shared definition of the problem ■ List of potential solutions	■ Assessments of possible solutions ■ Solution recommendations	■ Solution templates ■ Implementation standards ■ Rapid adoption of the social innovation

The forum's attendees also discovered that they had different ideas about what kind of emergency shelter people with special needs should have. After extensive discussion, they agreed that these populations need a shelter with slightly more services, monitoring, and medical care than a general-population shelter, but fewer services than a hospital. The attendees also developed standard procedures for locating and transporting people with special needs.

At this AHF, as at all forums, AHC did not set the agenda. Instead, forum members first attended panel sessions that were dedicated to various topics. At these sessions, members identified which problems they would tackle. Once members identified a problem, they explored it in more detail at separate technical sessions and workshops, which involved only the relevant stakeholders. AHC then distributed these workshops' outputs—white papers and detailed problem statements—through online and offline channels.

Minnesota's Citizens League has likewise developed a powerful exploration platform. In early 2007, the St. Paul-based nonprofit launched its Students Speak Out (SSO) project to find out more about students' day-to-day issues. The project was part of a larger initiative called Minnesota's 150th Anniversary Project (MAP 150), which encourages all citizens to be coproducers of the public good. The MAP 150 initiative offers a set of Web-based tools that allow citizens to collaborate in solving problems in several policy areas, including property tax, senior services, and public school education.

The users of SSO quickly zeroed in on one student problem: bullying. What had started out as a simple Web-based forum for students turned into a venue for parents, journalists, education researchers, school board members, legislators, and city government officials—including the mayor of Minneapolis—to discuss the growing problem of bullying in schools. The conversations occurred both online and offline. For example, on the Web site students swapped stories about bullying and debated what allows bullying to happen, and educators at a teacher training program met with students to discuss strategies for reducing bullying. The Minnesota legislative committee on education likewise invited SSO participants to present findings from their online discussions.

Gradually, a much clearer picture of the bullying problem emerged—one to which all the different stakeholders could relate. For instance, students' discussions revealed a broader range of bullying acts, including teasing, insults, physical bullying, cyber bullying, and even bullying by teachers. The students also uncovered that behavior considered to be bullying in one school or grade level is sometimes perceived as acceptable behavior in another school or grade level. Meanwhile, teachers noted that there are many factors that lead to bullying, and many of them are well beyond their (or the school's) jurisdiction. The exploration platform also revealed that contrary to teachers' widespread beliefs, students who are bullied often do not want their teachers to do anything about it. Instead, they just want someone to listen to them and be present when needed.

The Citizens League captured this formulation of the problem in an issue brief and a white paper. These served as the foundation for discussions on potential solutions, including school reforms and legislative actions. The early success of the Minnesota SSO project led to the launch of a similar initiative in Milwaukee in 2008.

Both AHC and the Citizens League followed the same general guidelines in creating their exploration platforms. Neither nonprofit controlled the discussion agenda. Instead, both offered neutral environments for diverse stakeholders to explore each other's perspectives and to develop a common definition of their main problems.

Also, both organizations gave their partners many forums for discussion. People often need to talk many times to reach a consensus about the nature of their shared challenges. In the case of AHC, participants first identified problems during the annual AHF, and then refined their conception of the problems during technical workshops and regional forums. The Citizens League likewise combined the SSO Web site with offline events such as student workshops, student video contests, and an annual convention. The number and variety of venues allow participants to build on each other's ideas.

Finally, both organizations connected their partners to solutions. AHC did so indirectly by inviting private companies to its workshops and annual trade shows, because these companies produce the technologies (wireless telecommunication networks, software, hazardous materials removal systems, etc.) on which disaster management organizations rely. The SSO more directly involved problem solvers by involving the Minneapolis city government, which subsequently incorporated the students' feedback in its policies, including those to reduce youth violence.

Experimentation: What's the Solution?

Businesses routinely put their innovations through a rigorous process of technical and market testing before they introduce them to the market.[2] Yet most nonprofits and government agencies skip experimentation. Consequently, many social innovations go more or less directly from idea to implementation. Yet as social innovations cross boundaries and increase in complexity, experimentation will become the cornerstone of effective problem solving.

Experimentation platforms give organizations a neutral environment for building and testing solutions in simulated or "near- real-world" contexts. A good example of such an experimentation platform is the Experience Labs, run by the Providence, R.I.-based nonprofit Business Innovation Factory (BIF). BIF's purpose is to serve as "an R&D center for transformative social innovations," according to the organization's mission statement. To this end, Experience Labs offer nonprofit and public organizations access to a safer, more manageable environment to test new ideas before implementation.

In a recent project, for example, several nonprofits, private corporations, and other partners are working with BIF to design the trauma bay of the future. Trauma bays are that part of hospital emergency rooms where the most seriously injured people receive treatment. Unfortunately, many trauma bays suffer from incoherent physical design, leading to delays and inefficiencies.

Over the summer of 2007, the Experience Labs team first observed and interviewed people who use trauma bays. The team then generated a number of ideas to reconfigure and optimize the space. For example, the storage systems in trauma bays are rather disorganized. Medical supplies are often stacked on shelves or stored in drawers without regard to how they are used in a typical day. In the new design, the shelving and patient gurneys are color-coded to make it easier for doctors and nurses to find supplies. Further, the gurneys are designed to carry medical information along with patients, preventing dangerous mix-ups.

The Experience Labs team then developed full-scale mock-ups of its design ideas using borrowed furnishings from Rhode Island Hospital, shaped foam, poster-sized photos, and hand sketches. Team members role-played different scenarios in the trauma bay prototype, analyzing the business case for the different design ideas from the standpoints of equipment suppliers, hospital administrators, architects, and medical practitioners. Through this process of repeated prototyping and testing, the team plans to develop a national standard for trauma bay design.

Similar experimentation platforms are evolving in other domains. For example, Philadelphia-based University City Science Center is a nonprofit that helps area universities and public research institutes turn their findings into profitable companies. Providing office space and fully equipped laboratories for life science and technology entrepreneurs, the research park has incubated more than 400 companies. It has also helped other multi-sector groups develop similar facilities in Bangkok; Kyoto, Japan; Oxford, England; and Sydney, Australia.

BIF and the Science Center share features that other experimentation platforms should emulate. Both combine input from diverse partners to create prototype solutions. For example, BIF brings together design ideas from researchers at Brown University, industrial designers at the Item Group (a private company), and practicing physicians at the Rhode Island Hospital and the University Emergency Medicine Foundation. Likewise, the Science Center convenes entrepreneurs from the greater Philadelphia region, academic scientists from area universities such as the University of Pennsylvania and Temple University, emerging life science companies, and established businesses.

Both platforms also define a common set of success metrics that help different partners rapidly generate and test new solutions. For instance, in BIF's trauma bay project, a common metric is the time it takes doctors to find medical supplies in the trauma bay. Likewise, entrepreneurs at the Science Center work to develop metrics that appeal to scientists, businesspeople, local and regional economic development agencies, and investors.

Finally, experimentation platforms should provide neutral environments for deep tests of alternative solutions. Neutral environments are not biased in favor of any particular stakeholders, so the data that they generate are valid and informative for all potential adopters. For example, BIF is a nonprofit entity with no direct ties to either the supply side (hospital equipment manufacturers, industrial designers, etc.) or the demand side (physicians, hospitals, etc.) of the innovations it is developing.

Deep tests, meanwhile, are comprehensive enough to unearth all the implementation challenges that each solution poses. In the case of the BIF trauma bay project, mock-ups of the design ideas are detailed enough to clarify the ideas' value to physicians and nurses in the trauma bay as well as to validate their economic viability to hospital administrators and medical suppliers. The Science Center likewise supports extensive testing of the ideas it incubates.

Execution: Giving the Solution Away

Once collaborators have defined their problems and identified their solutions, they can use execution platforms to roll out their findings. The most effective execution platforms build and distribute solution templates. Templates capture the core elements of a solution, but can be easily customized to fit different contexts. They also help partners coordinate their efforts. (For an example of an execution template, see "Art Mimics Art" on page 61 of this issue.)

Consider the School Support Organizations that the New York City Department of Education recently launched. This initiative created several networks of schools, businesses, and nonprofits, which schools can join to learn about innovative curricula and operations strategies. For example, the nonprofit Academy for Educational Development (AED) leads a network that disseminates proven-effective educational practices for young adolescents. The City University of New York (CUNY) heads another network that specializes in college preparation. Yet another School Support Organization convenes networks of 15 to 20 schools of all age levels to share best practices in evidence-based arts and technology programs.

Basic Ingredients for Collaboration Platforms

INGREDIENTS	ORGANIZATIONS MUST BE ABLE TO:
A Network-centric perspective	■ Play supporting roles, rather than controlling the innovation processes ■ Adapt to the potentially conflicting goals of other partners ■ Embrace nontraditional partners ■ Leverage network resources and facilitate two-way flow of ideas and solutions
Modular or plug-and-play expertise	■ Deploy specialized expertise in diverse contexts both quickly and cost-effectively ■ Integrate expertise with that of partners
A portfolio of success metrics	■ Agree on measures that reflect all stakeholders' concerns ■ Define project goals in ways that subsume organization-specific goals

Other public sector agencies are likewise launching execution platforms. For example, the London-based Technology Strategy Board, a quasi-governmental organization, recently launched a public-private collaboration to implement technology-based social innovations such as efficient transport systems, environmentally sustainable buildings, and assisted living for chronically ill people. The initiative plans to bring together business organizations, government procurement agencies, university researchers, and scientists.

Successful execution platforms diffuse both well-researched solution templates and the knowledge needed to apply them. Many of the School Support Organizations, for instance, offer call centers, learning communities, on-site visits, and retreats. As part of its Middle Start program targeted at middle schools, for instance, AED conducts workshops and study sessions for schools, as well as school site coaching for principals and other school officials. Such forums help network members learn from one another, promoting faster adoption and adaptation of the solution templates.

Adopting new solutions often creates ripple effects within and outside organizations. And so a final task for execution platforms is to help their members manage these system-wide changes. For example, schools that join School Support Organizations in New York must often overhaul their operations so that they can make continuous, data-driven improvements. These changes include redefining performance goals, measuring gaps in student learning, and redesigning curricula. Organizations such as AED help individual schools identify and execute these changes, as well as coordinate their efforts with external stakeholders.

Sharing the Platform

The three types of collaboration platforms—exploration, experimentation, and execution—are important vehicles for social innovation, particularly in areas where the agendas of public agencies, nonprofits, and businesses overlap. To participate in these platforms, however, organizations must cultivate the following three sets of capabilities. (See "Basic Ingredients for Collaborative Platforms" on page 48.)

A network perspective. Organizations must look beyond their own boundaries to leverage external resources for ideas. Adopting this network perspective forces them not only to consider how their agendas fit with broader social problems, but also to develop the skills for collaborating with diverse partners.

To be good network members, partners should play a championing role, rather than seeking to control the activities in the collaboration platform. For example, AHC did not direct its partners toward any particular problem. Rather, it supported dialogue that would lead to the discovery of relevant problems. This ability to "let go" and allow the innovation process to unfold organically is important for the long-term success of the collaboration platform.

Part of that letting go is embracing nontraditional partners, who often harbor unique perspectives and therefore can offer creative solutions. The Toronto Transit Camp, for instance, reaches out to commuters with no technical expertise. Likewise, the nonprofit Rockefeller Foundation readily employs the for-profit InnoCentive. Forging alliances between these strange bedfellows requires all partners to understand each other's incentives and business models.

At the same time, however, platform partners must subsume their individual agendas to the larger goals of the platform. For example, in the AHC case, private companies such as IBM Corp., Lockheed Martin Corp., and Northrop Grumman Corp. are allowed to weigh in on specific problems. Yet many of these companies also possess technologies and services that could potentially address some of these problems. Because these corporations have a vested interest in shaping the problem definitions, AHC has established norms and procedures to check these corporate interests. Meanwhile, the companies have to adapt their private goals to participate in the collaboration platform.

To leverage network resources, partners may also need to adapt some of their existing practices. For example, the schools participating in the School Support Organization network had to build more flexibility in their internal structures and decision-making processes to adopt the best practices offered in their networks.

Plug-and-play capabilities. As organizations and sectors collaborate to solve social problems, they must become both more specialized and more flexible—in other words, more modular. Platform partners will have to package their expertise so that they can quickly and cost-effectively deploy it in very different contexts. They must also know how their expertise can complement that of their partners.

For instance, InnoCentive has honed its ability to conduct idea contests to generate ideas across a wide variety of problems. At the same time, the company has also learned to consider the domain knowledge, funding, and intellectual property policies of its partners. With these parameters in mind, it tailors its contests to the problem and partners in play. Similarly, BIF can apply its design expertise to develop, test, and evaluate a wide range of innovations, using the unique strengths of its project partners.

A portfolio of success metrics. Rather than focusing on narrow organization- or sector-specific indicators, platform members must measure success in ways that appeal to all partners. One way to do this is for the project to develop larger goals that subsume the goals of its individual partners.

In the trauma bay project, for instance, BIF must weigh hospital administrators' concerns about cost and regulatory considerations, medical suppliers' concerns about market size, and doctors' concerns about patients' survival. At the same time, though, BIF set a broader, longer-range goal: to set the national standards for trauma bay design. This far-reaching goal not only reflects the organization-specific goals of its partners, but also gives the group a target to pursue together.

Collaboration platforms can help dismantle the long-held barriers between government, business, and nonprofit sectors. They can also speed the cross-fertilization of innovative ideas and solutions throughout the sectors. The ability of nonprofits and government agencies to establish and participate in such collaboration platforms will likely decide their success in solving the complex social problems that we currently face. ■

Notes

1 For more on the different types of innovation intermediaries, see Satish Nambisan and Mohanbir Sawhney, "A Buyer's Guide to the Innovation Bazaar," *Harvard Business Review*, June 2007.

2 For more on experimentation, see Thomas H. Davenport, "How to Design Smart Business Experiments," *Harvard Business Review*, February 2009.

The Hidden Costs of Cause Marketing

By Angela M. Eikenberry | Illustration by John Hersey

From pink ribbons to Product Red, cause marketing adroitly serves two masters, earning profits for corporations while raising funds for charities. Yet the short-term benefits of cause marketing—also known as consumption philanthropy—belie its long-term costs. These hidden costs include individualizing solutions to collective problems; replacing virtuous action with mindless buying; and hiding how markets create many social problems in the first place. Consumption philanthropy is therefore unsuited to create real social change.

I do my main charity work once a week—at the grocery store. Like some of you, this week I bought organic yogurt that not only is healthier for my family and the Earth, but also supports nonprofit environmental and educational organizations. I also picked up snack bars that promote peace (no kidding!) and salad dressing that funds various (unnamed) charities across the country. For all of this hard work, I rewarded myself with some Endangered Species Chocolate, which helps "support species, habitat, and humanity," according to the company's Web site. Delicious.

All of these purchases are examples of what my colleague Patricia Mooney Nickel of Victoria University and I call *consumption philanthropy*.[1] Also known in the business world as cause-related marketing or cause marketing, consumption philanthropy pairs the support of a charitable cause with the purchase or promotion of a service or product. (See “Flavors of Consumption Philanthropy” on page 53 for a description of the types of cause marketing.)

One example is the Product Red campaign, which California politician Robert Shriver has led and U2 lead singer Bono has promoted since its launch in 2006. By purchasing select Product Red-branded items from companies like Gap Inc., Apple Inc., Dell Inc., and Starbucks Corp., consumers can also support nonprofits like the Global Fund to Fight AIDS, Tuberculosis, and Malaria. The most well-known among the Red products, the Red iPod, costs $199, with $10 of that amount going to the Global Fund. So far, Red and its corporate partners have contributed more than $59 million to charity.

Consumption philanthropy seems like the ideal solution to many of the problems our society faces today. It allows charities to raise much-needed funds and to educate consumers. It helps corporations increase their profits, bolster their reputations, and distinguish their brands. And it lets consumers feel that they are making a difference in the world. On the surface, all seems rosy.

Yet lurking beneath this rosy surface are some disturbing consequences of combining consumption and philanthropy. I do not mean the often-cited risks of cause marketing, which include misalignment between the charity and the corporate sponsor, wasted resources, customer cynicism, or tainted images of charity. Most critiques of consumption philanthropy focus on these pesky problems of execution without questioning its basic underlying assumption—that consumption philanthropy, if done well, would do good for all.

I disagree with this assumption. Consumption philanthropy individualizes solutions to collective social problems, distracting our attention and resources away from the neediest causes, the most effective interventions, and the act of critical questioning itself. It devalues the moral core of philanthropy by making virtuous action easy and thoughtless. And it obscures the links between markets—their firms, products, and services—and the negative impacts they can have on human well-being. For these reasons, consumption philanthropy compromises the potential for charity to better society.

Short-Term Fix

Strategies that combine consumption with philanthropy have skyrocketed in the last two decades. Among corporate sponsors, cause-marketing expenditures went from almost zero in 1983 to an estimated $1.3 billion in 2006, according to IEG Inc., a Chicago-based firm that tracks cause-related activities in the United States. At the same time, consumers increasingly demand that companies practice philanthropy and social responsibility. A 2004 Cone/Roper report found that 86 percent of American respondents were “very or somewhat likely to switch from one brand to another that is about the same in price and quality, if the other brand is associated with a cause.”

As a growing body of research attests, consumption philanthropy does offer short-term benefits. Many corporations that sign on for cause-marketing campaigns enjoy higher sales and wider publicity for their products and services, improve their image with consumers, expand their markets, and boost employee morale. For example, cosmetics giant Avon Products Inc. says that cause marketing on behalf of early breast cancer detection and research has improved its relationships not only with its predominantly female customer base, but also with its predominantly female sales force.[2]

Meanwhile, charities gain legitimacy in the marketplace because they are seen “as viable partners in commercial ventures and not just as beggars pandering for the corporate dollar,” write Australian marketing professors Michael Jay Polonsky and Greg Wood in their review of cause-related marketing.[3] Through cause-marketing campaigns, charities also generate revenues, attract volunteers, raise awareness of their cause, and receive extensive publicity. For instance, the Susan G. Komen Breast Cancer Foundation’s partnership with Yoplait—Save Lids to Save Lives—has raised millions of dollars for the foundation while also increasing public awareness of breast cancer (and strengthening Yoplait’s brand image).

Consumers also seem to win from participating in cause marketing. They get additional information about a charity or cause, as well as a convenient way to spend their disposable income on charitable causes. For example, consumers who were planning to buy chicken noodle soup or cereal anyway can choose to buy the “pink” Campbell’s chicken noodle soup or “pink” Cheerios to meet their needs, while also providing funds for breast cancer research.

Lone Rangers

Yet the long-term effects of consumption philanthropy are troubling. The first of these effects is that consumption philanthropy—which usually takes place as individual market transactions—distracts its participants from collective solutions to collective problems. This distraction steers people’s attention and collective resources away from the neediest causes, the most effective interventions, and the act of critical questioning itself.

The growth of consumption philanthropy reflects many people’s confidence in the power of the market (that is, the institutions, systems, and places where buyers and sellers exchange things) to deal with all sorts of social problems. That confidence stems from the ideology of neoliberal economics, which prevailed worldwide—at least before the current economic collapse. This ideology “views all aspects of human society as a kind of market,” note management scholars Brenda Zimmerman and Raymond Dart.[4] For instance, in his 2005 book, *The Fortune at the Bottom of the Pyramid: Eradicating Poverty Through Profits*, University of Michigan management professor C.K. Prahalad portrays the world’s poorest people as an untapped market niche whose salvation will come when they are fully integrated into the market. Likewise, in response to the 9/11 terrorist attacks, President Bush told Americans that our best, most patriotic recourse was to go shopping.

But one problem with relying on consumers to right the world’s wrongs is that most consumers are not very interested in or capable of righting the world’s wrongs. The primary goal of people in marketplaces is to make choices that fulfill their self-interested, individual material needs and desires. In this capacity, they generally have little impetus to consider “the public” or “the public good.” Caught up in the transactions of buying and selling, they have little opportunity to question the fundamental principles of corporate organization. And unlike citizens who share in the collective authority, responsibility,

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Flavors of Consumption Philanthropy

Transactional. This is the most widespread model of consumption philanthropy. For each unit of product or service a corporation sells, it contributes a portion of the proceeds to a social cause. Two examples are the pink products campaign that the Susan G. Komen Breast Cancer Foundation organizes and the Product Red campaign that Robert Shriver and Bono back. Through them, consumers can buy a product while also supporting breast cancer research or the HIV/AIDS, malaria, and tuberculosis battle in Africa. Both campaigns partner with multinational corporations in the United States and elsewhere.

Promotion-Based. Corporations promote a cause and make charitable contributions. The donations are not necessarily tied to business transactions and not necessarily monetary, but do promote both the cause and the corporation. An example is the partnership between the Anti-Defamation League and Barnes & Noble. Their Close the Book on Hate initiative provides instructional materials and lectures to promote racial and cultural tolerance.

Licensing. A charity such as the World Wildlife Fund licenses the use of its name and logo to a company such as Visa. The company then donates a percentage of every transaction associated with the logo to the charity.

and dignity of public life, individual consumers have little reason to wonder how larger political-economic structures might create social problems in the first place.

Recent research indeed shows that when money enters the picture, people's more charitable impulses often fall by the wayside. University of Toronto management professor Sanford DeVoe and his colleagues, for example, have shown in laboratory experiments that participants are less likely to volunteer for a charity after calculating how much money they earn per hour than they are after merely reporting their annual salary. Putting a price tag on time, it seems, makes people less willing to give their time away "for free." [5] (For more information, see "The Stingy Hour" in the winter 2008 issue of the *Stanford Social Innovation Review*.)

The research evidence also shows that individualized consumer approaches to philanthropy actually shift giving away from more collective approaches. Professors Karen Flaherty, currently at Oklahoma State University, and William Diamond of the University of Massachusetts Amherst found in a 1999 study that cause-marketing campaigns hinder future donations to charities because consumers think that their purchases *are* donations.[6] So when the plate passes for charitable contributions, respondents to cause-marketing campaigns feel that they've already given. Likewise, findings published in 2004 in the *Journal of Marketing* suggest that consumers who support socially responsible companies believe that they have already done their philanthropic share.[7]

Consistent with these findings, Zimmerman and Dart tell the story of a person who attended a book sale held by a nonprofit organization. The person bought a hot dog, a drink, and a couple of books at the event. When the nonprofit asked for donations, the attendee demurred, thinking that the purchases were a sufficient contribution to the organization.

Another less favorable implication of consumption philanthropy's reliance on the purchasing decisions of individual consumers is that it may disadvantage less attractive but nonetheless worthy causes. Consider the many pink ribbon campaigns for breast cancer, for instance. Since 1991, when the first pink ribbon was handed out at the Susan G. Komen Foundation's Race for the Cure, pink ribbons and products have flourished. Today, the Komen Foundation raises about $30 million a year through 130 corporate partnerships.

The sheer volume of pink products seems to lead many consumers to believe that breast cancer is the most pressing health problem facing women today. Yet the most recent (2004) data from the U.S. Centers for Disease Control and Prevention show that the leading cause of death among women in the United States is heart disease, not breast cancer. And although cancer is the leading cause of death for women ages 35-64, breast cancer is not the most common form of cancer among women (skin cancer is), nor is it the leading cause of death among women diagnosed with cancer (lung cancer holds this distinction). Because of the success of cause marketing for breast cancer, however, breast cancer-related organizations receive attention that is disproportionate to the scope of the disease.

As consumption philanthropy becomes ubiquitous, some observers worry that it may, in the long run, have exactly the opposite of its intended effect and will desensitize the public to social ills while decreasing other forms of philanthropic action. Accordingly, Matthew Berglind of Northwestern University and Cheryl Nakata of the University of Illinois at Chicago write in a 2005 *Business Horizons* article: "It is not difficult to imagine cause-related marketing campaigns interjecting themselves into the millions of purchase transactions that take place each day. In response, people may simply tune out and say 'no' because they cannot process each and every request, or because they believe they have already donated enough." [8]

Easy Virtue

One of the redeeming aspects of consumption philanthropy is that it makes philanthropy simple and convenient. As I do every weekend at the grocery store, shoppers can protect the Earth, promote world peace, and fund a network of otherwise unnamed charities without deviating from their routines in the least. In this way, consumption philanthropy can contribute to a more compassionate marketplace.

The other side of this easy virtue, however, is that it is *too* easy. Consumption philanthropy does not allow people to exercise their moral core. Philanthropy originated in the Greek ideal of *philanthropos* or "love of humankind." According to Aristotle's *Nicomachean Ethics*, philanthropy allows people to enact the all-important virtues of generosity, benevolence, kindness, compassion, justice, and reciprocity. Enacting these virtues, in turn, allows people to develop their character, cultivate their human potential, and strengthen their moral fiber.

Can consumption philanthropy achieve these same ends? Probably not. When people link their charitable donations to their preexisting consumption decisions, they need not exercise a deeper sense of moral responsibility. They need not take any extra steps (beyond, say, choosing a different brand of yogurt) or make any additional sacrifices. Instead, they need only to pursue their shopping needs and wants. Indeed, the consumer-philanthropist may even enjoy a cost savings for her seemingly virtuous effort. As a recent Project Red advertisement put it: "30 percent off for you, 5 percent to fight AIDS in Africa." One could argue that consumption philanthropy—especially if there is a charitable surcharge—represents effort, and the choice to buy a "socially responsible" product represents intention, but there is very little sacrifice, if any, required. And so consumption philanthropy becomes divorced from the experience of duty.

Perhaps a more disturbing feature of consumption philanthropy is that consumers need not be aware of the supposed beneficiary of their actions. The morality of philanthropy comes from acting for other people, according to scholars Warren Smith and Matthew Higgins.[9] Acting for other people, in turn, requires figuring out what they really need.

Yet consumption philanthropy sidesteps both this requirement and, more generally, contact with people in need. For example, a person who uses a charity-licensed credit card to pay for an expensive meal, and thereby sends a percentage of his purchase to a cause that fights hunger, may no longer feel obligated to find out who is hungry or why they are hungry. Without this knowledge, he may feel less empathy for poor people, and therefore less compelled to change the conditions that caused their plight.

More broadly, in the absence of people's active and effortful moral engagement, corporations and their profit-driven needs set the tone for acceptable ways of being philanthropic. As a result, people's genuine benevolent sentiments are co-opted for profit, and their care is reduced to a market transaction.

Market Blindness

A third long-term negative consequence of consumption philanthropy is that it obscures the ways that markets produce some of the very problems—physical, social, and environmental—that philanthropy attempts to redress. In *Pink Ribbons, Inc.,* Samantha King describes the paradox of some pink ribbon products: labels on the outside that promote breast cancer awareness and research, but chemicals on the inside that cause the disease in the first place. (See the spring 2007 *Stanford Social Innovation Review* for a review of this book.) So consumers buy, say, a $6 SpongeBob Pink Pants toy to help fight cancer, not realizing that this product—a frivolous item—also likely creates the toxins and other environmental hazards that help cause cancer.

Consumption philanthropy seldom calls on consumers to question the labor that went into the creation of these products. Do these allegedly responsible corporations pay their workers a living wage? Do they create safe working conditions? Do they make fair contracts? Product Red may be donating money to fight disease in Africa, but it isn't doing enough to protect the workers who make its products, says Bristol, U.K.-based nonprofit Labour Behind the Label. Although Product Red partner Gap has worked diligently over the years to improve its ethical practices and image, for instance, the apparel company still runs afoul of both international regulations and activists: Two years ago, London's *Observer* found children making Gap clothing in sweatshops in India. Cause-marketing items may be no worse than ordinary products, but they appear to be no better, either.

Finally, consumption philanthropy rarely questions the act of consuming or the environmental havoc that more and more products wreak. Did the energy used to create that Endangered Species Chocolate bar destroy another acre of rain forest, and therefore hasten the endangerment of yet another species and the warming of the planet? Was that SpongeBob Pink Pants toy really worth the petroleum—and the environmental degradation that came with extracting, refining, and transforming it—that went into it? Rather than raising these questions about our purchases and their consequences, consumption philanthropy encourages people to buy more by making them feel better about it.

In short, consumption philanthropy lulls people into a false sense of doing good through their purchases, even as they are potentially doing harm through their purchases. Indeed, in many cases, consumption philanthropists are exacerbating the very harms they wish to reduce. At the same time, consumption philanthropy feeds the systems and institutions that contribute to many social problems in the first place.

Meanwhile, because consumption and philanthropy have become one and the same, the distance from which one would critique consumption and the market, and imagine alternatives, is eliminated. Philanthropy becomes depoliticized, stripped of its critical, social change potential. The result is that consumption philanthropy stabilizes, more than changes, the system (the market) that some would argue led to the poverty, disease, and environmental destruction philanthropists hope to eradicate. Consumption philanthropy is thus not about change, but about business as usual.

Profit-Free Philanthropy

I cannot offer the solution to the problems of consumption philanthropy. But I hope at least to offer a starting point for dialogue about unexamined assumptions and the political nature of philanthropy. What are our assumptions and expectations of philanthropy? Should philanthropy create social change? If so, what type of change?

If we are concerned about solving societal problems, reinvigorating the moral core of philanthropy, and making markets protect—or at least not harm—human well-being, a market approach cannot be an appropriate avenue for philanthropy. The most benevolent philanthropic agenda would not be infused with consumption. Instead, it would give voice to those who suffer. This may be the best way to create social change.

Why amplify the voices of those who suffer? As we have seen in movements for workers' rights, African-Americans' civil rights, and women's and gender rights in the United States, when the aggrieved speak and the more powerful listen, policies, political processes, and public perceptions can change. Social movements are one of the principal ways in which "collectivities can give voice to their grievances and concerns about the rights, welfare, and well-being of *themselves* and others." [10] And social movements—such as the American Revolution and the abolition of slavery—have brought about some of the most significant developments and changes in human history.

For philanthropy to give voice to those who suffer, it needs to support grassroots social movements. Since at least the 1950s, a small but persistent group of foundations and donors has practiced social change philanthropy through its unfettered support of nonprofit groups and grassroots associations. These nonprofit organizations and grassroots associations, in turn, support the movements that give voice to the marginalized. This is in line with Tracy Gary's challenge to donors, in *Inspired Philanthropy*, to practice a philanthropy that "has a role in changing the inequities of society" by joining donor interests and experiences with needs in the community. The National Committee for Responsive Philanthropy likewise calls on foundations to dedicate at least 25 percent of their grant dollars to advocacy, organizing, and civic engagement that promotes equity, opportunity, and justice.

Boston-based Haymarket People's Fund is committed to this vision of philanthropy. Founded in 1974, the fund supports groups that are working in the areas of racism, workers' rights, women's and gender rights, housing and homelessness, and environment and health issues. Its mission is explicitly to "strengthen the movement for social justice" by supporting "grassroots organizations that address the root causes of injustice," and its democratic funding practices transform the typically hierarchical relations between donors and recipients.

Other nonprofit organizations and philanthropic institutions could focus on cultivating more meaningful and diverse relationships with donors, rather than on raising funds through consumption. Through a more regular and deeper relationship with donors, these organizations and institutions can encourage philanthropists to pay attention to how their philanthropy fits into the larger movement to serve the public good. This will allow them to revive the moral core of their philanthropic acts, as well as to engage in political discourse about what role philanthropy should play in society.

To this end, fundraising experts Kay Sprinkel Grace and Alan Wendroff suggest that fundraisers move away from a *transactional* model of giving, whose emphasis is on cultivating donors of major gifts, and toward a *transformational* model of giving, whose "focus is on the impact of the gift and the renewing relationship, not just on the transaction." [11]

Changing philanthropy to give greater voice to those who suffer also means changing the current focus in corporate philanthropy. Rather than tying charity to profits, corporations should focus on their own responsibility to their employees (through means such as fair wages and healthy, satisfying work conditions), the environment (through means such as greener and more sustainable practices), and the global society (through means such as Fair Trade practices and loyalty to communities of operation). Corporations might also join other foundations and donors in funding grassroots efforts to improve communities. These alliances would be strategic partnerships not for profits, but for change from the bottom up.

Though many corporations will find it difficult to be socially responsible on all these dimensions, a few are already doing well on most of them. Two examples are Google Inc. and Whole Foods Market Inc. Google is well-known for its supportive and holistic labor practices: The company pays its employees well, gives them time to explore new projects and creative endeavors, and offers them amenities ranging from on-site roller hockey rinks to free food 24 hours a day. Google also values diversity. Likewise, the Google Foundation supports anti-poverty, alternative energy, and environmental efforts. Whole Foods is the largest corporation to purchase renewable energy credits and promotes the use of nonpolluting electricity sources. Several of its stores are 100 percent green-powered.

True Benevolence

Consuming more will not solve today's social and environmental problems. Indeed, consumption may very well create more of the kinds of problems that we had hoped philanthropy would fix. Relying on individual consumer choices, consumption philanthropy is unsuited to the scale or complexity of the problems it seeks to fix. Couched in market transactions, it neither acknowledges the voice of the transactions' beneficiaries nor gives philanthropists the satisfaction of mindful virtuous action. And caught in the mechanisms of the market, it obscures the fact that the market caused many of the problems that philanthropy seeks to redress.

For philanthropy to lead to social change—if that is indeed what we hope and expect it to do—I suggest we look to philanthropy as a tool to bring greater voice to those who have suffered or are marginalized, and for those who advocate for bettering society. This is not easy in today's society, although our current economic crisis is increasingly demonstrating the limitations of the market.

The time has come to question our assumptions and then to imagine alternative, more hopeful futures. Surely, genuinely philanthropic benevolence would call not for more consumption, but for the elimination of the conditions that make philanthropy necessary. ■

Notes

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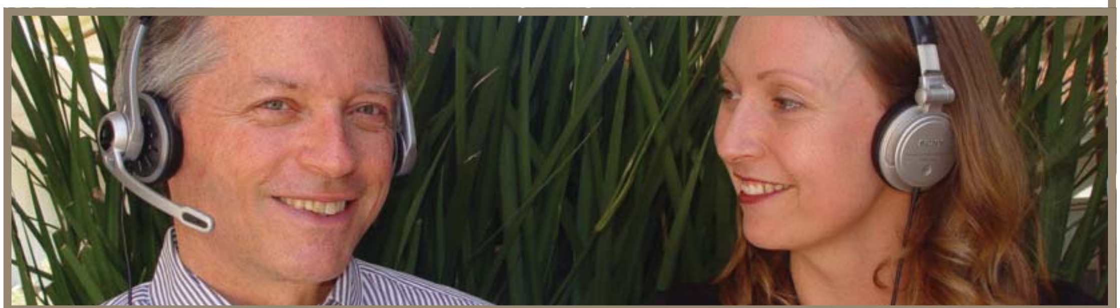

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STANFORD GRADUATE SCHOOL OF BUSINESS

CENTER FOR SOCIAL INNOVATION

By Suzie Boss

Fashionable Twitterers combine clubbing with fundraising for clean drinking water at New York's M2 Ultra Lounge.

PHOTOGRAPH BY MARINA FRAGOSO SENRA

WEB 2.0

Tweets for Change

▶ Work fast. Do good. Invite everybody. Mash up these appealingly simple strategies with a Web 2.0 tool like Twitter, the popular microblogging platform, and you wind up with something called a Twestival.

During the world's first Twestival, on Feb. 12, near-simultaneous fundraisers took place in pubs and clubs in 202 cities around the globe. The buzz began building a couple of weeks earlier, thanks to chatter in the Twitterverse. (For anyone who's managed to miss the latest Internet phenomenon, Twitter allows people to post short updates, called tweets, which others can subscribe to and read.)

Twestival attendees got to meet and greet the real people behind the avatars whose mini-messages they follow. But this was more than socializing. Ticket sales and online donations generated more than $250,000 to support the nonprofit Charity: Water, whose mission is to provide clean drinking water in the developing world.

Twestival organizer Amanda Rose, a Canadian events consultant living in London, volunteered to organize the event on a few weeks' notice to demonstrate the power of microphilanthropy. "I'm not a charity thumper," she insists. "This just seems like the right thing to do." During tough economic times, she adds, "we are going to be reliant on microdonations. I wanted people to give what they could, even if it's only two dollars, and let them see how it adds up."

Picking just the right cause is critical. "It had to be a simple and worthwhile concept," Rose says, "so the Twitter community could get behind it." Clean drinking water turns out to be an ideal concept to convey in 140 characters or less (the maximum length of a tweet). What's more, Charity: Water is a nonprofit "that really understands social media and how to engage this crowd," Rose says. The organization invites donors to post their personal stories about philanthropy on its Web site and uses Google Earth to show the locations of wells it builds in the developing world.

Conversations that start with a few words on Twitter often jump to blogs and YouTube. Rose says this shows the viral power of Web 2.0 tools to connect and engage people. "It's the conversation that gets people."

Instead of taking a top-down approach, Rose favors crowdsourcing. That means engaging local volunteers in every site. "I want to bring huge awareness," she says, "but decentralize it." Her strategy: provide event guidelines to ensure consistency across geographies, then leave the nitty-gritty to locals. Naturally, she arranged to track donations online, giving Twitterers something else to chatter about.

Every Twestival had its own vibe. New Yorkers raised $24,000 while schmoozing in a nightclub. Meanwhile, in Dubai, the tweet-up raised $400 at a beach party. "That reflects the online Zeitgeist," Watson says. "Nobody's experience online is the same as anyone else's."

London's Twestival was a huge draw: 700 tickets sold out in two hours, and donations topped $8,000. Dhaka, Bangladesh, raised almost nothing, but was still a success from the organizer's perspective. "I just wanted them to participate," Rose says. "The next time it happens, the momentum will be huge." ■

GOVERNMENT

White House Digs Innovation

▶ When first lady Michelle Obama helped turn a patch of the South Lawn into a kitchen garden for the White House, sustainable foodies savored the moment—and the overnight attention it brought to their "eat local" movement. Social innovators, meanwhile, spent early spring waiting for the Klieg lights to turn in their direction. "Any day now" was the rolling estimate of when the new President would formally announce creation of the first-ever White House Office of Social Innovation. (At press time it was learned that the office would be headed by Sonal Shah, who previously worked at the global development team of Google.org.)

Even before the announcement, spirits were high among those who have pushed hard for the creation of this new West Wing office. "This could be a very big idea," predicts Vanessa Kirsch, executive director of New Profit Inc. Kirsch is also a founder of America Forward, a coalition of leading social entrepreneurs. During the presidential campaign, America Forward lobbied hard for a White House office that would help scale effective nonprofit programs.

More cause for optimism came in late March with the passage of the Senator Edward M. Kennedy Serve America Act. Passed with broad bipartisan support, the act creates a community solutions fund for replicating proven programs, starting with $50 million in 2010. It also greatly expands opportunities for community service. For social innovators, this means fresh infusions of money and people power for scaling up good ideas.

One of the people who helped establish the new office was Michele Jolin, a former senior fellow at the Center for American Progress. (Jolin first made the case for the new office in "Innovating the White House," published in the spring 2008 issue of the *Stanford Social Innovation Review.*)

Establishing a White House office sends a strong message. "Every President creates special offices around his priorities," Jolin points out. "This is a way to signal that social innovation will have some extra oomph in this administration."

With a home base in the White House, the new office staff will be in a position to convene gatherings, bring together potential partners, and use the bully pulpit to promote social innovation across sectors. At the same time, the office will likely be careful not to create any new bureaucracy that could interfere with community-level innovation. "Government's role is creating a climate so that innovation can happen," Jolin says, "not to put barriers in place."

This emphasis on showcasing innovation and funding what works could enable government to act more like a venture philanthropist, predicts Kirsch. Emphasizing results and competing for resources are hallmarks of social entrepreneurs. "We welcome the chance to compete against metrics," she says. "Tell us what you want to accomplish in government and give us the chance to show you that we can do it more cost-efficiently, or at scale, or in neighborhoods where you didn't think we could succeed. Our dream is that this office is like the little engine that could." ■

HEALTH CARE

Mobilizing Against Fake Drugs

▶ Your child is feverish and hacking, so you rush to the pharmacy to buy some cough syrup. If you're living in the United States or Germany, you trust that the bottle contains exactly what the label describes. But in the developing world, there's a one-in-three chance the medicine you purchase will be fake.

Counterfeit drugs are a big and cruel business across much of Africa. They not only waste consumers' money but put public health at risk. Western tools for authenticating pharmaceuticals—such as chemical testing, nanotechnologies, radio frequency identification, or holograms—rely on labs and technologies that aren't always available in the developing world, where even electricity is unreliable. And even if government regulatory agencies are in place, they lack the resources to match well-funded counterfeiters.

"All these options have failed us," says Ashifi Gogo, a young, Dartmouth College-trained engineer who is a native of Ghana. "They don't work in developing nations." Gogo is the cofounder of mPedigree, a start-up that has devised a method for using mobile phones—ubiquitous in the developing world—to put drug authentication into the hands of consumers.

Here's how the drug authentication system works: At the point of sale, a buyer scratches off a label to reveal a unique numeric code. Using text messaging, the buyer sends this code to an automated hotline, which checks a database and reports back immediately whether the medication is authentic or fake. If it's counterfeit, the buyer can demand a refund on the spot.

Ghanaians can easily find out if the drug they bought is legitimate by texting a scratch-off code and receiving instant authentication.

PHOTOGRAPH BY ASHIFI GOGO

During a trial in Ghana, most consumers had no trouble using scratch-off labels to authenticate pharmacy purchases. The trial also indicated that elderly consumers prefer talking to a hotline operator rather than texting. A survey revealed that nearly half of consumers were unaware of the prevalence of counterfeit drugs on the retail market. Yet the World Health Organization estimates that counterfeit drugs account for 30 percent of the drugs sold in the developing world.

The most promising aspect of mPedigree's model may well be its bottom-up design. "Consumers are the ones who are most invested in drug safety, the ones with the most to lose," says Gogo. Although mPedigree also encourages government enforcement, he adds that "empowering consumers is what this technology is about."

That makes sense to Marv Shepherd, president of the Partnership for Safe Medicines. "We have to get control of this problem. Consumers need to trust that they are getting authentic products. Any deterrent that can be implemented will be helpful to combat 'a global problem that shows no signs of slowing down.'"

Under the mPedigree business model, consumers pay no premium for the assurance of drug safety. Drug companies eager to protect their brands have shown a willingness to cover the costs of texting, redirecting a portion of their marketing budgets to cover SMS fees, Gogo says. Ghana's four telecommunication firms collaborated during the first trial, making the same four-digit access code work across all mobile carriers.

Eventually, Gogo intends to sustain mPedigree's drug safety efforts with a for-profit venture to authenticate other commonly counterfeited goods, such as clothing and entertainment products. "Nobody dies from buying a fake DVD," he says, "but big companies still want to be able to protect their IP [intellectual property]." ■

SOCIAL INVESTING

Hedge Funds for Good

▶ Looking for the silver lining in the current financial mess takes a special breed of optimist. Combine that with a quest to redefine the hedge fund as a force for good and you can start to sound downright quixotic.

Yet that's what the founders of New York-based Uhuru Capital Management have set out to do. The firm will manage a conventional fund of hedge funds, but with an attention to social values. What's more, general partners will direct 25 percent of their profits to help social entrepreneurs scale up efforts in developing markets.

The founders bring solid credentials for both making money and doing good. Peter Kellner, a successful private equity investor, is a protégé of Ashoka founder Bill Drayton and cofounder of Endeavor, a nonprofit that supports high-impact entrepreneurs in emerging markets. And Neal Goldman launched Capital IQ, a financial research firm that was later sold to Standard & Poor's.

The opportunity to put sustainable investing ideas into practice is what attracted Jed Emerson, Uhuru's managing director of integrated performance. After years of talking up blended value theory on the conference circuit, he says, "what we really need are more and deeper examples of practice."

Will wealthy individuals and families warm to Uhuru's approach? Justin Rockefeller (the youngest son of U.S. Sen. John D. "Jay" Rockefeller IV) is one who showed early support, providing start-up capital and family name recognition.

Uhuru isn't sharing financial projections, but no one expects the firm to grow to the size of the multibillion-dollar hedge funds. "That level would not be success for us," Emerson admits. "We're trying to maximize value. We don't believe we would be able to manage funds as effectively," he says, if they mushroomed into the billions.

Uhuru's timing and smaller is better approach may work in its favor. The firm starts at "the current reset point," Emerson points out, with no need to recover losses, a problem plaguing many other hedge funds.

"It's pretty clear we're at an inflection point in the financial system," says Tim Freundlich, a partner at Good Capital and senior vice president at the Calvert Foundation. "Everyone's wondering, how do we come out of this on stronger footing? The commitment up front to sustainability and social responsibility—that's what they're leading with [at Uhuru]. In the hedge fund world? There's been very little of that."

But it's on the back end where Uhuru—Swahili for freedom—may really make an impact. That's where a quarter of general partners' incentive-based management fees will be channeled to the new Uhuru Sustainability Foundation, dedicated to helping social entrepreneurs achieve scale in developing markets. The foundation will keep overhead low by relying on intermediaries such as Ashoka and Endeavor to manage the selection process. "We become an investor in their fund management approach," Emerson explains, "in the same way we would if we were investing in for-profit activity."

Once all the parts are operating, Uhuru will have in place a global network of wealthy investors, hedge fund managers, and social entrepreneurs—groups whose circles seldom overlap. Their shared knowledge will inform how Uhuru makes money and does good. Predicts Freundlich, "That could be a much bigger conversation." ■

Art Mimics Art

Manchester Bidwell Corporation replicates by adapting general strategies to local cultures

By Suzie Boss

More than 1,000 visitors a year tour the nonprofit Manchester Bidwell Corporation (MBC) in Pittsburgh in search of ideas for their own organizations. They get an eyeful. In an after-school program called Manchester Craftsmen's Guild, at-risk teenagers produce stunning ceramics, paintings, and multimedia in studios that rival the best college facilities. In its sister program, Bidwell Training Center, unemployed adults nurture hothouse orchids and cook gourmet meals to prepare for technical careers. Another program brings in world-class jazz musicians to produce Grammy Award-winning recordings.

"No matter where your eye turns, there's something cool going on," says CEO and founder Bill Strickland. "That's quite deliberate."

Strickland, a MacArthur Fellowship (also known as a "genius award") recipient, has spent the last 40 years in the same tough neighborhood where he grew up, honing MBC's model of community change. And his model gets results: reduced high school dropout rates, increased college admissions, and adults placed in jobs that lift their families out of poverty.

Now, Strickland is spreading MBC's lessons far beyond Pittsburgh. Funded in part by a $1 million grant from the Skoll Foundation, MBC has planted offshoots in San Francisco, Cincinnati, and Grand Rapids, Mich., and plans to launch another in Cleveland later this year. In so doing, MBC has refined the art and technology of replication. Central to MBC's replication technique is helping communities tailor the model to their unique needs and preferences, rather than exporting its Pittsburgh formula wholesale. The nonprofit has also nailed down a clear order of operations for developing new sites.

Equipped with proven replication strategies, Strickland has set his sights high. His goal is to launch 100 arts and technology centers in high-poverty urban settings across the United States, and another 100 around the world. That would create the critical mass to "change the conversation" about what education should be, he says.

LOCAL FLAVOR

Strickland's replication strategy used to be showing a slideshow to anyone willing to watch. A charismatic speaker, he inspired plenty of listeners. But the lag between inspiration and action frustrated him. "I didn't know how to shape what we'd learned in Manchester and package it into a concept that could be effectively rolled out on a grand scale," he relates in his autobiography, *Make the Impossible Possible*.

That changed when community leaders in San Francisco asked MBC to help them start their own education center. After several years and more than a few false starts, the doors of the Bayview Hunters Point Center for Arts and Technology (BAYCAT) opened in 2004.

"That's when we started talking about what it would take to [replicate] in a more organized way," explains Georgina Gutierrez. She is vice president of the National Center for Arts & Technology (NCAT), a separate nonprofit dedicated to disseminating MBC's model. With funding from the Skoll Foundation, MBC hired the Bridgespan Group to prepare a replication business plan. "That caused us to step back and ask ourselves, what do we have in Pittsburgh that could be planted like a seed in another city?" she says. The Pittsburgh team also sought advice from friends of the organization, including J. Gregory Dees from Duke University's Fuqua School of Business and James Heskett from Harvard Busi-

Suzie Boss is a journalist from Portland, Ore., who writes about social change and education. She is coauthor of *Reinventing Project-Based Learning: Your Field Guide to Real-World Projects in the Digital Age*.

Students and staff develop photos at the West Michigan Center for Arts and Technology, a Manchester Bidwell spin-off.

PHOTOGRAPH BY MARK THOMAS

ness School. These far-reaching discussions eventually led to the establishment of NCAT in 2007 as a separate nonprofit under the MBC umbrella.

As Strickland and company became more deliberate about replicating, they distilled the Manchester model into four nonnegotiable goals for every new center: (1) A world-class environment for learning; (2) Ambitious arts programming for at-risk youth; (3) Job training for adults, calibrated to the needs of local employers; and (4) A culture that values poor people as assets, not liabilities.

SPREAD SOUND STRATEGIES

Adapt proven techniques to fit communities' needs and strengths

Chart a clear course from idea to implementation

Hire local leaders with both discipline and passion

NCAT then decided to leave the details of how to pursue these goals to each community. Communities fund and operate their centers as independent nonprofits, although all are affiliated with NCAT. As a result, the four existing centers look quite different, though "they all share the same spirit," Strickland says. "You feel very hopeful in any of these spaces."

RULES OF ENGAGEMENT

Strickland hasn't stopped giving his famous slideshow, which opens with the story of how a high school art teacher transformed his own impoverished life. "That's where the interest usually starts," says Dolores Sewchok, interim vice president of NCAT. "Somebody hears Bill speak and gets inspired." To accelerate what happens next, NCAT has developed a formal replication process.

The first phase is cultivation. "This is where we make sure the community really understands what this will take," Gutierrez explains. Typically, interested parties travel to Pittsburgh to see MBC's operations firsthand, and NCAT staff get acquainted with their potential partners.

Moving to the next phase—feasibility—requires potential partners to sign a formal consulting agreement with NCAT at a cost of $150,000. If a new organization is not yet formally in place to manage fundraising and other tasks, a local foundation might serve as the convener. "This is where we find out, are they really ready for this? Is there a need for the kind of programs we can bring," Gutierrez says, "and is there enough focus on those needs to raise the money required for solutions?"

The feasibility phase takes from 12 to 18 months and includes discussions between NCAT staff and about 100 local leaders. This outreach is time-consuming but necessary to ensure that support for the new nonprofit is strong on all sides, including the school district, corporations, government leaders, and existing nonprofits. The dialogues also reassure existing organizations that "we're not coming in to duplicate or compete for funding with programs that already exist," says Lillian Kuri, director of special projects for the Cleveland Foundation, which has been a local convener and major funder of the Cleveland replication. "By spending time on this early," she adds, "you don't get opposition later."

If the feasibility phase ends with a green light, parties move on to a four-year process of planning and implementation, with consulting costs to NCAT of $150,000 annually.

Lee Carter, chairman of the board of the Cincinnati Arts and Technology Center (CATC), says it took his community about two and a half years to establish its program. Now in its fifth year, CATC serves 400 youths annually. Although nearly all of the teenagers in the youth arts program are at risk of school failure when they start, 95 percent graduate from high school on time and 70 percent go on to higher education. Meanwhile, the job training program is mentoring about 100 adults in automotive repair, construction, and health care.

Well-received by the community today, the vision for CATC didn't grab hold in Cincinnati until people understood that they could adapt the program to their own needs. "The word 'replication' was turning people off at first," says Carter. "But the minute we started talking about adapting instead of replicating, the same people who had been critical started saying, 'Oh, that sounds like a good idea.'" CATC, housed in a refurbished warehouse, weights its budget toward youth programming because Cincinnati has other adult job training programs. "We don't need to duplicate that," Carter says. And instead of selling orchids or jazz albums as they do in Pittsburgh, CATC has devised a different income stream: a team of CATC youth artists that paints Cincinnati-themed storefront murals for a grocery chain.

LEADING FROM WITHIN

Each time a city considers joining the NCAT family, the question of leadership comes up. Stories of MBC and its founder are so closely intertwined that people often wonder, "How are we ever going to find our own Bill Strickland?"

Gutierrez has a ready answer. "We're not looking for another Bill Strickland. We're looking for a person who can be disciplined enough to follow someone else's idea," she says. The executive director must also be from the local community. Being an artist isn't required, Sewchok says, but candidates "have to be passionate about helping people who have been left out of other systems."

NCAT is hands-on about guiding the executive director search. "We have a profile," Gutierrez says, "but we have learned that capable directors can come from very different backgrounds." BAYCAT Executive Director Villy Wang, for example, is a seasoned attorney, whereas 27-year-old Luisa Schumacher, the executive director of the West Michigan Center for Arts and Technology in Grand Rapids, has a background in political fundraising, nonprofit marketing, and community relations.

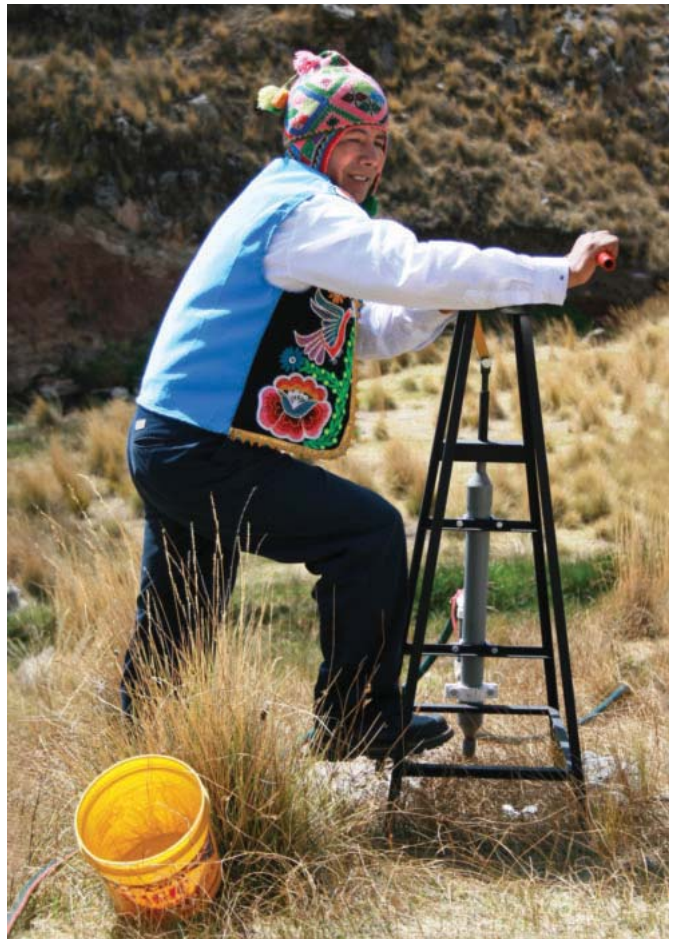
NCAT is also very involved in guiding site selection and board development. "Being able to learn from their expertise has helped speed our decision making," says Kuri. "It's true collaboration. They aren't telling us what to do. We use their expertise to figure things out together. We couldn't do it alone."

Potential new art and technology education centers are now in their early stages in Israel, Rwanda, and Ireland, along with several U.S. cities. "The model may look a little different in these places," Sewchok says, "but our goal will be the same: bring people together, find common ground, and collaborate for the greater good." ■

The Parent of Invention

RAMP nurtures local inventors in India, Peru, and Indonesia

By Aaron Dalton



This RAMP inventor developed a manual pump that farmers use to water crops in the highlands near Cusco, Peru.

PHOTOGRAPH COURTESY OF RAMP PERU

People valued brick houses for their solidity and durability long before the Brothers Grimm wrote down the story of the wise pig who kept the wolf at bay while his brothers had their straw and wood homes blown down. The denizens of Tamil Nadu state in India are no different. Yet the kilns they need to bake enough bricks for a decent home require up to 15 tons of firewood—both an economic and an environmental hardship.

Development experts might have suggested that residents switch to a less resource-intensive building material to sustain the region's booming housing sector. But George Eapen, a local inventor, knew that the brick houses held an unshakable allure. And so instead of trying to change ingrained attitudes, he changed the kiln. His new design bakes bricks with alternative fuels like agricultural waste, thereby reducing pollution and lessening the demand for firewood.

Eapen's idea might have remained just that—a concept stuck on the drawing board. Instead, he received both financial support and mentoring from the Indian branch of the Portland, Ore.-based Lemelson Foundation's Recognition and Mentoring Program (RAMP). With local partners Indian Institute of Technology and Rural Innovations Network, RAMP helps grassroots inventors "create enterprises that meet basic human needs in a sustainable way," according to the organization's Web site. "Life is tough enough for dreamers and innovators," says Eapen. "But if you have to sink in your own money, time, and passion, most give up at some stage for want of even moral support."

Since founding its Indian program in 2004, the Lemelson Foundation has developed two additional RAMPs: one based in Jakarta, Indonesia, and another based in Lima, Peru. The Indian RAMP has supported 37 inventors, the Peruvian RAMP 19 inventors, and the Indonesian RAMP 10 inventors. "In many places, particularly in the developing world, inventors are seen as weird or nutty. They're quite isolated," says Julia Novy-Hildesley, executive director of the Lemelson Foundation. "We seek to elevate the stature of inventors through public prizes, to show that society is validating and supporting innovation and thus encourage more inventors to come forward. That's why the program emphasizes recognition and mentoring in addition to financial assistance."

Aaron Dalton is a New York-based journalist and photographer whose work has appeared in *Wired*, *PC Magazine*, and *Popular Mechanics*. He also authors the blog *1GreenProduct*, where he reviews eco-friendly goods and services.

Local Genius

By definition, inventors everywhere are fated to struggle against the status quo. They rebel against conventional wisdom and overturn comfortable routines. Failure is an inevitable part of the job description. When questioned about the results of his experiments, no less an inventor than Thomas Edison replied: "Results! Why man, I have gotten a lot of results. I know several thousand things that won't work."

Though less famous than Edison, Jerome Lemelson also had a successful career as an inventor, earning more than 600 patents. Lemelson and his family started a foundation to encourage innovation and entrepreneurship. In the United States, the foundation has established centers for the study of innovation and created prizes such as the $500,000 Lemelson-MIT Prize, which "recognizes individuals who translate their ideas into inventions and innovations that improve the world," according to MIT's Web site.

In the 21st century, the foundation is turning its focus toward the developing world. "Jerome Lemelson believed that innovation and creativity were distributed evenly throughout the world, but that in many places, there are barriers that prevent individuals from realizing their creative potential," says Novy-Hildesley. "Our RAMP programs emphasize a strategy of nurturing local innovators, based on the belief that these people often have a better understanding than outsiders of the obstacles and their sociocultural context."

NURTURE NATIVE BRILLIANCE

Support local solutions to local problems

Work with organizations on the ground to identify talent

Give inventors technical, social, and financial support

Trying to airlift inventions from one context and plop them into another is often a recipe for disaster, agrees Jackie Khor, managing director at Imprint Capital Advisors, an organization that advises foundations, families, and individuals on developing mission-driven investment portfolio strategies. Khor previously worked at the Rockefeller Foundation, which is involved with the Rural Innovations Network that partners with RAMP to assist Indian inventors.

"It is logical that the innovations that would be most useful in addressing unmet needs in a particular context would be the ones developed in that context," says Khor. "Solutions need to be context specific, and local innovators are best positioned to understand and take into account climate, culture, and the particular needs of their innovation's local end users."

For instance, outsiders would probably have not been able to decipher the complex web of relationships and transactions that govern the lives of nomadic shepherds in the southern Indian states of Kerala and Tamil Nadu. Yet a local innovator named G.V. Sudarshan saw that shepherds were in dire straits, struggling with shrinking herds, scarce pasture, labor shortages, and sickly lambs. With money and mentoring from RAMP, Sudarshan developed a nutritious sheep feed that uses farm waste products such as corncobs and straw. The feed not only reduces the amount of land the sheep need to forage, but also improves their health.

Sudarshan combined his product with a service innovation, giving the shepherds access to preventive veterinary care and livestock insurance—both previously unheard of in the community. To encourage shepherds to use his pellet feed, he offered both the product and service at his own cost, later recouping his expenses by purchasing the lambs at a discount and then selling them to urban meat processors.

Similarly, on the island of Java in Indonesia, RAMP inventor Ir. Ari Purbayanto developed a machine called the Suritech, which separates the bones and meat of small fish, turning bycatch fish from waste into edible (and profitable) food. And in Peru, an innovator funded by RAMP named Luis Coronado Lira devised a ventilation system to prevent the spoilage of perishable foods, potentially increasing farmer profits and simultaneously giving urban dwellers access to more nutritious options.

Although Lemelson does have a full-time consultant working in India, the foundation works hard to make RAMP programs local and resource-light. In all three locations, the foundation relies on partnerships with local organizations and volunteers, many of them academics, to identify and support grassroots innovators. RAMP inventors receive what the foundation calls "tailored catalytic support"—prototype facilities, marketing experts, and other specialized resources that can make the difference in helping an innovator turn his or her idea into reality. In Chennai, India, RAMP also sponsors an annual awards ceremony where hundreds of inventors can network, share ideas, and build a sense of community. Promising inventors that the awards process identifies are encouraged to apply for formal RAMP support.

SHARING THE SMARTS

Khor also praises RAMP's model of giving inventors both funding and mentoring for entrepreneurship and commercial development. Early-stage venture capital firms have proven this model to be successful for profit-seeking companies. The biggest challenge in a nonprofit context, notes Khor, is to develop appropriate and cost-effective distribution strategies.

That's a problem that RAMP is still trying to solve for Dr. Sathya Jeganathan, a physician in a rural Indian hospital in Tamil Nadu. In the neonatal ward where Jeganathan works, expensive, complicated, and scarce baby warmers often break down, with deadly results for newborns. After a dreadfully cold night contributed to the deaths of six newborns, Jeganathan began working with local craftspeople to invent a reliable, low-cost baby warmer. They devised a simple construction that can be built and maintained entirely with local materials and expertise.

With help from RAMP, Jeganathan developed a working prototype that lowered infant mortality rates in her hospital by approximately 50 percent. RAMP is now trying to help her mass-produce the warmer, as well as to convince the Indian government to purchase and distribute enough of the warmers to replicate Jaganathan's lifesaving results at rural hospitals throughout India.

Novy-Hildesley says that the Lemelson Foundation is exploring the possibility of starting a RAMP program in East Africa. She also notes that RAMPs are considering taking small equity stakes in some of their inventors' projects. That way, if a particular innovation succeeds, the RAMP would have more funds.

Meanwhile, RAMP-supported innovators are hard at work around the world. One inventor in Peru is developing a plant oil-powered cooking stove that will reduce indoor air pollution. Another innovator in India is refining a portable spice powdering machine, which will reduce the distance that Indian villagers would otherwise travel to procure finely powdered chili and coriander.

"Once an idea has gotten off the ground, many foundations and even venture capital (VC) firms are interested in helping, but not many organizations are willing to work at the early high-risk stage," says Novy-Hildesley. "As a foundation dedicated to invention, we feel that this is an important niche. We incubate ideas, help our inventors cultivate relationships, make sure they can negotiate properly with VCs and other traditional investors, and then hand them off when the time is right." ■

Bikestation, a certified B Corporation, is building this bicycle transit center at Union Station in Washington, D.C.

IMAGE COURTESY OF BIKESTATION

Making the B List

The B Corp seal of approval distinguishes truly responsible businesses from mere poseurs

By Jenna Lawrence

Reem Rahim and her brother Ahmed don't always agree. But the two cofounders of Oakland, Calif.-based Numi Tea were both skeptical when the nonprofit B Lab approached them about certifying their business as a B Corporation.

B—"beneficial"—Corporations use "the power of business to solve social and environmental problems," according to B Lab's Web site. Yet Numi Tea had already received organic and Fair Trade certifications, so the Rahims did not understand why they also needed to earn their B Corp bona fides. They questioned whether B Corporation certification was just another marketing fad. And they wondered whether customers would even care that Numi was a B Corp.

But as false claims of social and environmental stewardship increasingly cluttered the corporate landscape, the Rahims sought the B Corp seal of approval. "We were concerned about 'greenwashing,' or attempts by typical companies to portray themselves as something that they are not," says Reem. Although different organizations offered environmental, labor, quality, and governance certifications, no one offered a single, independent, comprehensive standard for a company's overall social and environmental responsibility. As a result, consumers struggled "to tell the difference between good marketing and good company," explains Jay Coen Gilbert, one of the three cofounders of Berwyn, Pa.-based B Lab, which sets the standards for and certifies B Corporations.

To help both consumers and corporations, Gilbert worked with cofounders Bart Houlahan and Andrew Kassoy to form the B Lab in 2006. Since that time, the total number of B Corporations has grown to more than 180, representing 31 industries. "Numi and other B Corporations are not only directly influencing their industries," says Houlahan, "they are also contributing to a broader movement that will change the way business is done."

Graded Course

Businesses that want to earn their certification must first complete the B Survey, a dynamic online assessment tool that measures social and environmental performance. Although the actual questions differ according to the size and type of the company, all versions of the survey assess a company's governance, environmental impact, community outreach, and employee treatment. In total, the survey takes about 60 to 90 minutes to complete. The CEO typically completes the report with assistance from other departments.

To create its survey, the B Lab convened an independent standards advisory committee to comb through existing labor, environmental, and business certifications. Its mission was to glean the best standards and measures across industries, building on the efforts of the Global Reporting Initiative, WiserBusiness, and the Social Venture Network.

The original survey was one-form-fits-all. But after more than 600 entrepreneurs and experts gave their feedback, the committee fashioned an interactive, dynamic format because the original standards were too broad to distinguish B Corporations from their noncertified competitors. For example, financial services firms like San

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Francisco-based Good Capital must answer questions about their lending practices and costs of capital, whereas consumer goods companies like Numi Tea must respond to questions about their suppliers' environmental impact.

After corporations complete the B Survey, the B Lab staff prepare a B Report on the business. Companies that receive a rating above 80 (out of a possible 200) are eligible to become B Corporations. Before proceeding, they must supply evidence for some 20 percent of their survey responses.

BE LIKE B LAB

Create a single certification for both environmental and social responsibility

Offer members enticing benefits and privileges

Align laws with values

To give its certification even more teeth, B Lab audits 20 percent of its member companies every two years. Companies whose audited score falls below 80 have 90 days to clean up their acts. Companies found to have intentionally misrepresented themselves to B Lab face the public revocation of their certification.

Completing the B Survey is simple, yet thought provoking, says Reem. Although Numi Tea scored high on the survey, "we had to take a second look at some of our practices that were not covered by our organic or Fair Trade certifications," says Reem. The survey "pushed us to think more about what we should be doing to be good corporate citizens in our hometown, Oakland."

PROTECTING VALUES

Having passed the B Survey, companies must next change their articles of incorporation to reflect their commitment to social and environmental responsibility. In traditional companies, a board's main responsibility is to maximize financial returns to shareholders. B Corporations, in contrast, change their bylaws so that their boards must also consider the interests of their employees, their communities, and the environment. B Lab helps companies rewrite their bylaws, answering questions and linking them with lawyers. "Adding just a few paragraphs helps the business institutionalize the sustainability and socially responsible values," says Gilbert.

These governance changes not only solidify the company's commitment to people and planet, but also protect the company's values from the whims of new management, new investors, and new owners. Among social entrepreneurs, Unilever's purchase of Ben & Jerry's still serves as a cautionary tale of how easily corporate fiat can undermine social responsibility. "The board was legally required to sell to the highest bidder," says Jonathan Storper, an attorney at Hanson Bridgett, the first law firm to earn B certification. Neither Ben Cohen nor Jerry Greenfield wanted to sell the company, but because it was public, they had no choice. Both cofounders have since expressed concerns that the company has shifted away from its original mission of social responsibility.

"In contrast," says Storper, "the board at a B Corporation has permission to take a long-term view of the company's best interests. They do not have to sell out."

Gilbert concedes that no B Corporation has yet been tested by litigation. In 33 states, businesses are permitted to consider the interests of groups other than shareholders. This is not true in the remaining states, however, including California. In these states, B Corporations cannot yet rewrite their bylaws to conform to B Lab standards, but must commit to changing their bylaws as soon as legally possible.

Storper worries that California's failure to protect B Corporations will drive socially responsible businesses out of the state. "There has been an explosion of mission-driven companies," he says, "but they will leave California if it is not the best place for them to incorporate, and we will lose our position in this growing marketplace." As a result, Storper has joined B Lab and other supporters to lobby the legislature to amend state laws to create a type of corporation that can consider social and environmental purposes as seriously as profits. That legislation will go before the assembly in late 2009.

PRIVILEGES OF MEMBERSHIP

The final steps to becoming a B Corporation are signing a so-called declaration of interdependence and paying an annual licensing fee to B Lab. By signing the declaration, the CEO commits to doing business "as if people and place mattered." And by paying fees based on percentage of sales, B Corporations help run B Lab, maintain the certification standards, conduct audits, support policy efforts, and promote their cause.

Having received their B Corp certification, many companies do not rest on their laurels. "We can't stay comfortable for too long," says Reem. "The ratings inspire healthy competition for us to make our businesses better every year."

The extra effort and pressure of being B, however, seem to increase employee morale. Reem reports that employees rallied around the B certification process. And at Hanson Bridgett, employees were so excited about being certified that they took it upon themselves to organize into committees, says Storper. The green committee, for example, convinced the firm to get rid of bottled water because of the environmental impact of the plastic bottles and the purity of San Francisco tap water.

Another benefit of going B is the tight network of trusted partners. "If I am looking for vendors, whether for office supplies or tea, I look to fellow B Corporations first," says Kevin Jones, founding principal of Good Capital. His company also uses the B Corporation certification to decide where to invest its money. "There is so little commonality among social ventures that we have to evaluate investments on an individual basis," he says. "But if we know it is a B Corporation, we already know a lot about the company and its values."

Certification may not matter that much to consumers, say some B Corporations. For instance, Xavier Hegelson, founder of Better World Books, notes that "customers talk about the free shipping that we offer, not the literacy programs we support or the carbon-neutral footprint we maintain." Nevertheless, he points out, "everyone doubted that consumers would be willing to pay three times as much for organic produce, but now even mainstream customers choose organic." Similarly, B Lab founders are betting that investors, employees, and consumers will eventually go the extra mile to find and patronize B Corporations. ■

The Profit in Nonprofit

Kiva, the first online peer-to-peer microcredit marketplace, is one of the fastest-growing nonprofits in history. But its nonprofit status was not inevitable. Here's why Kiva chose to be a 501(c)(3), what this tax status buys the organization, and how being a nonprofit poses challenges. By Bethany Coates & Garth Saloner

In 2004, Jessica Jackley set out for rural Kenya, Tanzania, and Uganda to perform an impact evaluation for the Village Enterprise Fund (VEF), a San Francisco Bay Area nonprofit that makes modest grants and loans to small businesses in East Africa. A few months later, her husband, Matt Flannery, then a computer programmer at Alviso, Calif.-based TiVo Inc., came to visit her. As the couple traveled around the country interviewing small-business owners, they talked nonstop about the best ways to help Africa's struggling entrepreneurs.

One year earlier, Jackley had heard Muhammad Yunus, the founder of Grameen Bank, give a talk about microfinance. "I reacted with both my head and my heart," she recalls. "My head said: 'Microfinance is effective. It's powerful. It works.' But the most important part was what my heart said. The way he talked about the poor was beautiful, respectful, and dignified. I didn't have feelings of guilt and shame like I did after a lot of nonprofit messaging. Instead, I wanted to be there, listening to people's stories and talking with clients face to face."

Once in East Africa, Flannery and Jackley agreed that they too would facilitate loans rather than donations. After weeks of brainstorming, they soon settled on the basic idea for Kiva. At first, they envisioned a few friends and family members lending money to a handful of entrepreneurs in East Africa. And then eventually, although they weren't sure of the steps along the way, they saw Kiva evolving into a self-regulating online lending marketplace where microfinance institutions (MFIs) could raise loan capital to fund projects for small-business people in developing countries.

Upon their return to the United States, they set up meeting after meeting with contacts in microfinance to discuss, among many other topics, whether the venture should be nonprofit or for-profit. After months of skepticism, disapproval, and rejection from industry insiders, they launched Kiva (which means "unity" or "agreement" in Kiswahili) as a nonprofit. By the end of 2007, Kiva had become one of the fastest-growing nonprofits in history.

Although being a nonprofit presents unique challenges, the organization's 501(c)(3) status has ushered in many unforeseen benefits. Major industry players, such as PayPal Inc. and YouTube Inc., generously bestow goodwill donations on the organization. Some of the best business and Internet talents in Silicon Valley freely funnel their time and energy to Kiva. And both individual and institutional donors help underwrite the costs of the site.

"Although perspectives are rapidly changing, and hybrid social enterprises are cropping up everywhere, people still have a lot of misperceptions about the limitations of being a 501(c)(3)," says Jackley. For the time being, Kiva is content with its nonprofit status. "It's a tax code, not a religion," she says. "We do think like a business wherever it makes sense, and we have tried hard not to get sucked into any sort of false limitations of being a nonprofit."

The Obstacle Course

As Flannery and Jackley first imagined it, Kiva's business plan was quite straightforward: An online platform would allow ordinary people to invest in small and medium enterprises (SMEs) in the developing world. (See "Kiva's Loan Cycle" on page 70 for an overview of how Kiva works.) Users would log on to the Web site to read the personal accounts of Kiva's carefully chosen borrowers and then use their PayPal accounts or credit cards to lend as little as $25 to a borrower. On-the-ground MFIs would then administer the loans to the borrowers. Users would get their money back over the course of a year, with the option of either relending the money or pocketing it. While the loan agreement was in place, users would also receive frequent updates about their borrowers from the MFIs.

Despite the simplicity of their model, Flannery and Jackley ran into a tremendous amount of resistance from microfinance experts. "The criticisms were about both the supply side and the demand side," says Jackley. "On the supply side, critics said that the idea wasn't scalable because of the time and effort needed to vet borrowers and then to post their stories on the Web. And on the demand side, the critics said, for whom is this product intended?" The microloans were neither investments nor donations. "No one knew what to do with this bizarre, in-between product," she says.

Another issue was how much interest (if any) Kiva could charge borrowers and return to lenders. Kiva's founders originally wanted to offer lenders the option of earning interest on their

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loans, both to attract lenders and to transform the usual wealthy donor-poor beneficiary hierarchy into the more egalitarian lender-borrower relationship. Yet returning interest on loans could have turned the loan into a security in the eyes of the Securities and Exchange Commission (SEC). Offering a security to the public would trigger a long list of SEC requirements, including sufficiently collateralizing the loans and investing only in entities that comply with U.S. accounting standards.

Kiva's founders also debated whether to be a nonprofit or a for-profit organization. Establishing Kiva as a nonprofit was the fastest way for the founders to get the site up and running. Yet they could not readily ascertain whether a charitable organization could extend loans rather than donations. They were also unsure what tax implications Kiva and its lenders would face upon the return of the loan principals and, should they charge interest, profits.

Finally, skeptics doubted whether Kiva could actually help lift many people out of poverty. A common theory circulated that, for microfinance to have a significant impact on world poverty, MFIs would need to be integrated into the global economy and to tap into the capital markets. Yet most MFIs did not qualify for commercial-grade investments. Rather, they relied on donations, especially during their early years of operation. Observers questioned how Kiva could find enough appropriate MFIs with a reasonable number of borrowers to help the organization establish a creditworthy track record.

CASE STUDY QUESTIONS:

What benefits do nonprofits enjoy that for-profits do not?

What limitations do nonprofits face that for-profits avoid?

How do social entrepreneurs weather doubts and disappointments in the early stages of their ventures?

JUST DO IT

By December 2004, Flannery and Jackley themselves began to question whether to pursue their idea any further. After so many naysayers and so little progress, they were beginning to feel discouraged, says Jackley. Rather than giving up, though, the founders decided to plunge ahead with the more straightforward plan: become a nonprofit.

After calling 47 law firms, Flannery finally located an attorney who was willing to help establish Kiva as a nonprofit. The founders then worked with Moses Onyango, a pastor they met during Jessica's VEF study, to identify seven Ugandan entrepreneurs who could benefit from small loans.

To avoid potentially running afoul of the SEC, and to focus on the core mission of "connecting people through lending to alleviate poverty," Flannery and Jackley decided that the Kiva Web site did not need to offer interest to lenders. At the same time, the MFI partners who would distribute the loans to local entrepreneurs would still charge prevailing interest rates and earn interest income. In this way, individual lenders, not MFIs, bore the risk of borrowers' defaulting on the loans. Suddenly, MFIs had access to free, flexible, and very forgiving debt capital through a brand-new source—individual lenders around the globe.

In April 2005, the founders e-mailed a description of Kiva, its mission, and the businesspeople it currently sponsored to a list of 300 friends. Within two days, the organization had raised $3,500 and funded all seven enterprises. Kiva had just become the first online peer-to-peer microcredit marketplace.

Onyango used the Kiva Web site as a blogging platform and regularly entered updates and progress reports on the entrepreneurs. His profiles became a reason for lenders to check back on the site, and perhaps to lend again.

By October 2005, the borrowers had repaid the first round of loans. Flannery and Jackley decided to launch officially—"which basically meant having a friend write a press release and removing the word 'beta' from the Web site," says Jackley. Kiva then worked with Onyango to find 50 additional Ugandan entrepreneurs.

For the first few weeks after the press release, the Kiva site was rather quiet. Then,

Kiva users can make loans to this woman-owned carpet-weaving enterprise in Kabul, Afghanistan.

PHOTOGRAPH COURTESY OF KIVA

in mid-November 2005, "something happened," Flannery described in the winter/spring 2007 issue of *Innovations*:

> My day started as usual. I took the Caltrain to work and logged into my computer. I had received nearly 1,000 e-mails to my Kiva address. I checked the database logs and saw that we had raised about $10,000 that morning and that all the loans on the site were sold out. Why? We had been featured on the home page of Daily Kos, one of the world's largest blogs. Over a million people had read about Kiva that day and hundreds were actively discussing it online.

In short order, Flannery quit his job at TiVo and began building Kiva as its CEO. Meanwhile, Jackley pursued her MBA at the Stanford Graduate School of Business. "We thought this could allow us to have the best of all worlds—I would still be able to learn and bring resources and new ideas to Kiva while it was growing, and we could live off of my student loans," says Jackley. "Meanwhile, Matt could build out the site because he was the tech genius."

THE CHARITABLE ADVANTAGE

Although Flannery and Jackley had not raised any real start-up capital, Kiva attracted a passionate, talented, and dedicated crew, fueled by Kiva's mission. The team grew quickly to include heads of partnerships, marketing, technology, and public relations. Many of the 23 full-time employees—most of them in their 20s and 30s—worked pro bono for months. "It was easy to feel ownership of the project," Jackley recalls. "When you know that a big dream relies on you, it's inspiring."

In part because of its nonprofit status, Kiva was also able to leverage hundreds of volunteers and to fill its board with well-known Bay Area executives, including Reid Hoffman, CEO of LinkedIn Corp. and the former executive vice president of PayPal; and Jenny Shilling Stein, executive director of the Draper Richards Foundation. Geoff Davis, who was serving as CEO of Unitus, a nonprofit microfinance accelerator based in Seattle, likewise joined the nonprofit's board.

Kiva also attracted Premal Shah, a six-year PayPal veteran who had recently spent a sabbatical in India working for an MFI. Shah stepped away from founding MicroPlace Inc.—an eBay Inc.-owned for-profit online lending company that had a slightly different yet potentially competitive model of making retail investments in MFIs—to become president of Kiva. Although both MicroPlace and PayPal are eBay companies, Shah was able to broker a deal with PayPal for free payment processing on the Kiva site—in large part because Kiva was a nonprofit. Because Kiva's largest variable cost is processing payments, PayPal's partnership allows Kiva to pass on 100 percent of loans to entrepreneurs. (Kiva launched a full two years before MicroPlace because the former did not take the long and difficult path of meeting the SEC's requirements for offering interest-bearing investments.)

Other big-name partners soon filed in, so that the "Supporters" list on Kiva's Web site now reads like a Who's Who of hip corporate America. YouTube, for example, has donated 120 million free banner ads to Kiva. Google Inc. gives Kiva free AdWords, the company's flagship advertising product. Yahoo Inc. likewise donates search marketing keywords, as well as employee volunteers. Microsoft Corp., Intel Corp., Starbucks Corp., Facebook Inc., and LinkedIn, among many others, likewise donate goods and services to the organization.

Kiva's nonprofit status has yielded more prosaic benefits as well. "Our staff eat well," says Jackley. Kiva's first office was located next door to Blowfish Sushi, a well-loved San Francisco restaurant. Kiva staff members frequently met with donors and board members at Blowfish, and so became familiar faces there. Eventually Kiva and Blowfish brokered a deal for big discounts on meals. "It may not seem like much," says Jackley, "but it actually helped a lot. The team worked long hours and could now meet potential donors next door, without worrying too much about who might pick up the bill."

Being a 501(c)(3) has also made Kiva feel comfortable asking its members to help cover the organization's operating costs, which totaled $5.9 million in 2009, according to Fiona Ramsey, Kiva's director of public relations. Jackley zeroed in on the idea of optional transaction fees at the 2007 Net Impact Conference. She was on a panel with members of two related nonprofits—DonorsChoose.org Inc., which allows people to donate directly to United States classroom projects, and the GlobalGiving Foundation, which facilitates direct donations to a wide range of projects around the world. An audience member asked the panel how each organization covered its costs. Jackley learned that DonorsChoose suggested that users make an optional 15 percent donation in addition to their base donation. GlobalGiving, in contrast, automatically took a 10 percent fee out of users' base donations.

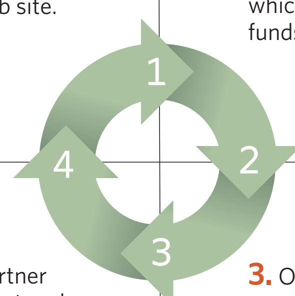
Extracting what she thought was the best of both worlds, Jackley suggested asking users to make an optional 10 percent donation to Kiva, in addition to their base loan to borrowers. A donor who makes a $50 loan to a borrower in Uganda, for example, would be asked to pay an additional $5 transaction fee. Jackley worked with Kiva's staff to implement this idea at the point of purchase online. In 2008, optional transaction fees totaled $2.2 million, says Ramsey, covering some 37 percent of Kiva's operating costs.

For the remainder of its funding, Kiva relies on three other revenue streams: grants, unused Kiva credit (e.g., uncashed Kiva gift

Kiva's Loan Cycle

1. Lender makes loan to business featured on Kiva Web site.

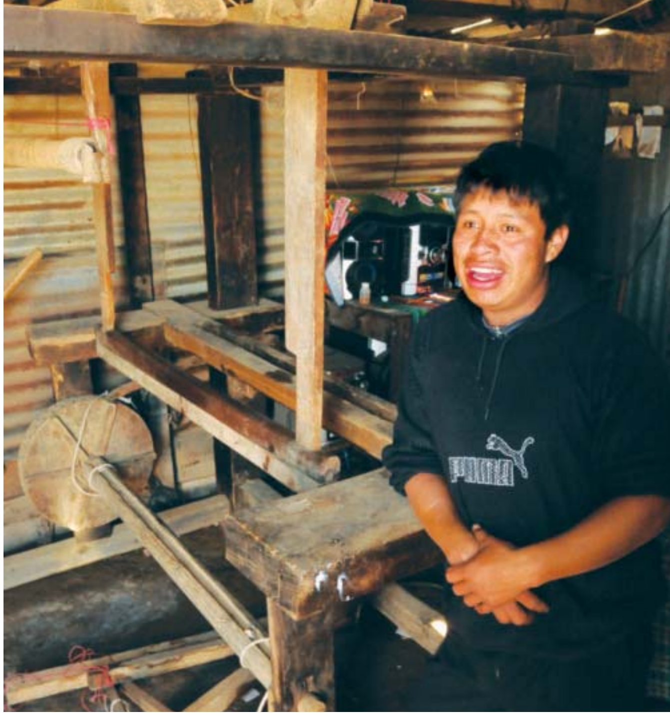
2. Kiva transfers loan to local partner, which then disburses funds to business.



3. Over time, local partner collects loan principal plus interest from the business.

4. Local partner keeps interest and sends principal to Kiva, which then repays lender. Lender may then withdraw or re-lend the money.

Source: Kiva



With demand for his products on this rise, this Guatemalan shoe maker is using his $950 Kiva loan to buy materials.

PHOTOGRAPH BY AUDREY SCOTT

certificates and uncollected loan repayments), and "float"—the interest the nonprofit captures on the capital in its bank accounts. Because Kiva receives loans daily, but distributes the funds to MFIs monthly, its bank accounts earned some $370,820 in float in 2008.

Being a nonprofit also makes Kiva eligible for foundation funding. The organization receives large grants from foundations including Skoll, W.K. Kellogg, and Draper Richards. In 2008, those grants totaled $1,796,000.

THE COSTS OF BEING 501(C)(3)

Although foundation funding has been generous, says Flannery, a major drawback of being a nonprofit is that Kiva has to pass up commercial capital. "Venture capitalists call me up all the time trying to convince me to become for-profit," he says. "I know I could raise a lot of money in a short time." Instead, Kiva must raise its money incrementally, "getting this huge mélange of grants in small, unpredictable pieces."

Flannery indeed considered converting Kiva to a for-profit model. "A couple of years ago, we had trouble capitalizing. I bet that we could raise money from angel investors, so I brought that idea to the board. But the board said no, unanimously, right off the bat."

Over time, Flannery came to agree with the board. "We are building a community based on trust," he says. "We are asking people to concede profit to help a poor person. In turn, Kiva agrees not to profit from people's goodwill. If we did convert to a for-profit model, our users would probably trust us less." Indeed, a 2006 survey showed that 50 percent of Kiva users would not lend on the site if it adopted a for-profit model.

A second possible disadvantage of being a nonprofit is the need to orchestrate the interests of the board, staff, and other stakeholders. "If you're a founder of a for-profit you can just own the business and you don't have to gain the consensus of a large set of people," says Flannery. "The more controlling and entrepreneurial parts of my psyche would like that. But the other side of me is very thankful to be in a community where everyone has buy-in. It's been good for me."

With more stakeholders comes more scrutiny, however—a third cost of being a 501(c)(3). "People hold nonprofits to a high standard," says Flannery. "They scrutinize how you spend every dollar. I'm glad because it makes us stronger. But it can also slow you down," he says. "Everyone knows how much money you make, reads your financials, and questions you all the time."

KIVA TODAY

Since its founding, Kiva has produced a number of compelling results. The site regularly sells out of loans. Most businesses listed on the site are funded within hours. New borrowers are added hourly and potential lenders are urged to check back often to participate.

During times of overwhelming traffic on its Web site, Kiva caps loans at $25 so that more people have a chance to get involved. "Our mission is not to raise money for entrepreneurs at any cost," says Jackley. "Our mission is to connect human beings in a dignified way, through a loan. When push comes to shove, we would rather have more people involved and connected to each other than fewer, especially if the money will come either way."

At this time, the nonprofit has 95 field partners (that is, partner MFIs) in 44 countries around the globe. Average loan repayment rates are above 97 percent, and cumulative loan volume is more than $66 million. Both the number of lenders and the average number of businesses funded by each single lender are steadily increasing.

Kiva has also enjoyed a number of high-profile media successes. President Bill Clinton described the nonprofit in his bestselling book, *Giving*. *New York Times* journalist Nicholas Kristof profiled his experience with Kiva in an editorial piece. Then, in September 2007, Oprah Winfrey featured Kiva on her daytime TV show, thereby attracting an enormous amount of interest from Middle America. Demand was so high on the day the episode aired that it crashed the site.

The Kiva team feels affirmed about the growth of their organization, the positive media attention, and the moving anecdotal evidence of poverty alleviation amongst the entrepreneurs listed on the site. "Instead of sleeping on a reed mat, someone now has a blanket," Jackley notes. "Instead of mud walls, they have concrete. People have mosquito nets and medicine now, where before there were none of these things."

In the future, Kiva wants answers to questions like how many borrowers live on $2 per day now rather than $1, how many can afford to feed their families at least two or three times daily, and how many no longer have to choose between nutrition, schooling, and medication for their children. Yet this plan requires building more technical infrastructure, training MFIs around the world, and even more monitoring and auditing functions—demands that the organization cannot meet at the moment. "But we are planning to in the near future," says Jackley.

Although Kiva can measure its successes in numerous ways, Jackley maintains that the organization's most important impact is on the minds and hearts of the lenders and borrowers who use the Web site. From day one, Kiva's mission has been to connect people through lending. She says that these personal connections are "the most powerful force for change on the planet." ■

Power House

Mitch Cope and his wife, Gina Reichert, own a house on Detroit's north side. The neighborhood is a mix of Polish, Ukrainian, and Bangladeshi families—and quite a few drug dealers.

"People who have been in the neighborhood for a long time talk about how great [it] used to be; you didn't have to lock your doors," says Cope. "Okay, so it's gotten worse. Now what? Let's do something."

Cope and Reichert, who own a contemporary architecture and design store called Design 99, started with a wood-frame, single-family foreclosed house that scrappers had already trashed. The husband and wife team bought the house for $1,900 and are turning it into what Cope calls the "Power House Project."

"Instead of connecting to the grid, we wanted to keep it off the grid and get enough solar and wind turbines and batteries to power this house and the next-door house," Cope says. He thinks he can take the whole place "off the grid" for around $60,000, which he hopes to help cover with grants.

Cope plans to turn the first floor of the house into a neighborhood art center. The second floor will be a bedroom for visiting artists. Cope believes that if he can get artists to visit the neighborhood, then the lure of cheap real estate will keep them there. So far he's convinced about a dozen working artists from around the world to move into the Detroit neighborhood and make the most of a city that many people have given up on. —JENNIFER GUERRA

PHOTOGRAPH COURTESY OF MITCH COPE, DESIGN 99