Giving Them the Business

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When the dot-com boom exploded, Brad Zumwalt counted himself one lucky guy. Months earlier, just as Internet-stock mania was peaking, the Calgary software entrepreneur sold the visual-content company he co-owned for a cool $30 million, leaving him with plenty of money while he sat out a year-long non-complete clause.

Zumwalt, thought, is not the kind of guy who'll sit still for long. Now 37, the affable father of four bristles with the physical and mental energy that drives him to get things done immediately. So he was eager to find something big to do right away, and his Seattle-based mentor, Paul Brainerd, the father of desktop publishing, had this great idea, which evolved into a 1,500-partner organization called Social Venture Partners (SVP): Why not invest in a non-profit the way a venture capitalist pounces on a little innovative company? Pick an innovative social service carefully. Shower it with money and management expertise. Build up its organizational backbone so it can deliver. Monitor the results – in this case, the social return for the investment. And hold it accountable. This, according to Brainerd, would be a new style of philanthropy. It would be effective charity, a marked contrast to old style giving in which wealthy donors keep their distance and seldom measure bang for buck.

"If only they ran non-profits like a small business," Zumwalt agreed at the time, "the world would be a better place."

The concept he bought into, however, did not originate with Brainerd. Rather, it was launched by three U.S. academics, Christine Letts, William Ryan and Allen Grossman, in a 1997 article in Harvard Business Review. They argued that the classic arm's-length relationship between foundation and charities is a recipe for failure. Although non-profits start with high hopes and vision, they founder because they lack the organizational clout to deliver. Instead, the HBR authors continued, foundations should study how venture capitalists select and nurture young organizations and hold them accountable for results.

The article sparked a wave of interest, especially among young newly rich dot-comers, first in the U.S. and later in Canada, who were attracted by the idea of maximizing their charitable dollars by keeping close tabs on the operations and by offering non-profit managers plenty of coaching. One notable early practitioner was Jeff Skoll, the Canadian-born, San Francisco-based architect of the online auction house eBay Inc. who donated US$300 million to fund innovative social enterprises. Another was Mario Morino, the chairman of Venture Philanthropy Partners, who poured US$4 million into the organization, which has US$30 million in assets. On his side of the border, thought, you can count the venture philanthropy funds on one hand. Among them: Zumwalt; the Tides Canada Foundation, $18 million organization that links donors with grassroots groups seeking to improve the social fabric and the environment; and Toronto's Bill Young, who set up a $10 million fund to help little companies that endeavour to make a buck while employing supposed economic outcasts.

It wasn't long before the U.S. media ran stories about this new breed of big-dollar giver, who was dubbed the venture philanthropist. The fuss must have amused the people who ran such organizations as the Ford Foundation in the U.S. (which gives out US$600 million annually) and the Maytree and McConnell Foundation in Canada ($1.4 million and $11 million respectively), which had been practicing strategic, engaged philanthropy for decades. They knew the strengths of the approach. And its weaknesses, knowledge the full-of-high-hopes venture philanthropists – at least those who still had money after the crash – wouldn't discover until after they encountered a few unexpected surprises on the road to making the world a better place. "After leaving the business. " says Zumwalt, "I thought I would slow down and take a year off doing SVP. The slow easy pace of a non-profit. What a joke! It's just the opposite. Building SVP is easily the hardest thing I have ever done."

It's 7:30 on a dark, rainy Thanksgiving morning, and in about 12 hours Zumwalt will be jetting to France for a few days so he can bike up and down mountain passes with some friends. Tight now, though, he's sitting in a Calgary coffee shop, pumped up and happy to talk about his philanthropic journey of the past couple of years, even if that means giving up time on a holiday morning.

It all started, he says, back in 200 when he, along with his wife, Tanya, and their four kids and his mother-in-law, flew down to Seattle for lunch. Their mission: Talk to Brainerd, founder of Aldus Corp., about SVP. Zumwalt loved the concept – an organization with an entrepreneurial spirit that engages with a charity, educates its members about philanthropy and demands measurable results. After lunch he told his wife he wanted to start an SVP chapter in Calgary on his year off.

"That's great," said Tanya. "That's 100% great. But let's wait three years. We've got a little baby here. Why don't we just wait?"

"If we don't do this now," replied Zumwalt, "it will never happen."

So it happened. "I'm impatient, I guess," says Zumwalt now. "It was a huge sacrifice to lay on the family." Then he admits, "I had grossly underestimated how hard it would be, how accountable we would be."

Once committed, the couple acted decisively. They donated $250,000 over four years to start SVP's new Calgary organization and found 30 couples who agreed to invest $5,000 each per year – probably the biggest philanthropic donation any of them had ever made. In 2001, the group picked their first charities. Their strategy: Don't monkey with the mission. Instead, build strong organizations that can fill the gap left by shrinking government help for social services.

One of SVP's choices was Calgary Community Support for Young Parents (CCSYP), a tiny group that at the time was run by an articulate local dynamo named Pamela Scott. CCSYP helps very poor parents raise their kids, and Zumwalt was psyched: " When I started in this, I was going nuts. I was saying we could be doing more. We should be parachuting six people in their and get all this stuff done right away. Finally, Pamela said: 'Brad, enough, right? You guys are driving us crazy. It's great. We're thankful. But really, one thing at a time.'" One of Scott's problems was that she also had to deal with eight funders, each one wanting its own account of the impact of the donation. As well, every donor had to be consulted before any significant change could be made to the organization.

The non-profit world, as Zumwalt quickly learned, played by dramatically different rules. The psychology that drove non-profit leaders, for example, was unfamiliar to him. Small-business entrepreneurs like Zumwalt imagine and abundant world of endless opportunity. Nut the non-profit organizations Zumwalt saw in Calgary, even the one that were doing the most heroic work, had a " mentality of scarcity, " he says. They were so worried about losing the funding the didn't even allow themselves to imagine ambitious possibilities. No wonder. Some employees were 60-hour weeks on 20 hours' salary, which to Zumwalt is a "humbling" amount.

Zumwalt also discovered it wasn't easy to measure the success of a social investment, as he learned while working with an SVP funded agency that aims to help girls avoid the lure of prostitution. Among other things, it runs therapy sessions for girls and their families. When Zumwalt checked the attendance figures, he noticed that only 50% of the girls turned up for the sessions. "Well, this is not effective, " Zumwalt said at the time. "Why are you allowing these girls into the program?" Then another SVP partner with a doctorate in psychology, pointed out that those were precisely the girls that needed the most help: "If the girls were there 100% of the time, they wouldn't need the program." Zumwalt got the message: It's easy to jack up performance figures if you discard the tough cases and take the easy ones, but it doesn't reveal anything about how much good you've done for the money.

Or in the case of Scott's group, he realized, you can measure the number of families served, or whether the kids are reaching development milestones while they're connected to the organization. But could you prove that the actions taken had truly improved children's lives, helping them to become better adults than they might otherwise have been? In order to arrive at a conclusion, one that could end up being highly subjective, much money, effort, time, and manpower would have been spent.

Though social impact remains hard to measure, Zumwalt knows that SVP has definitely improved the organizational strength of the non-profits. While most donors prefer to fund programs rather than administration, venture philanthropists believe that approach is shortsighted. Weak organizations, they argue, can't deliver a powerful social punch; in fact, organizational weakness is typically the reason why they fail to deliver. So what non-profits need is better management – better computer systems, human resource practices, strategic planning, marketing and so on. With that in mind, SVP helped Scott's group improve its human resources practices and computer systems as well as its ability to track data on the young families. They devised exit interviews for staff and volunteers and worked on a business plan for a potential money-making venture. A checklist on organizational strength created by consultants at McKinsey & Co., helped Scott pinpoint her organization's strengths and weaknesses. With Social Venture Partners money she also hired a co-ordinator, leaving Scott time to map out a merger with two other non-profits that was in the works this fall.

Zumwalt "changed the way we did business," says Scott. "We moved from crisis to crisis into a frame of reference that was far more proactive."

While Zumwalt was setting up SVP in Calgary, Bill Young was in Toronto thinking about how to spend the multi-million-dollar windfall he scored when he sold his slice of cousin Bob's company, Red Hat Inc., for tens of millions of dollars a couple of months before the 2000 crash. At 49, Young isn't the type of guy to spend millions on a Porsche, a fancier house or any other trinkets of wealth. In fact, Young, a slight, eager accountant with a Harvard MBA and a fondness for sensible crewneck sweaters, is a little squeamish about his quick and easy riches. So he decided to plough $10 million into a fund to support innovative ideas in the non-profit world. After researching venture philanthropy in the U.S., Young drew up his list of criteria; a breakthrough idea and a visionary leader, commitment to sound business practices, limited dependency on a single funder, such as government, and self-sufficiency after five or so years. What's more, the organization had to measure its results.

You'd think it would be easy to give away money to non-profit innovators. It wasn't. After six months of looking, Young couldn't find a single Canadian non-profit that fit the bill. The problem, as he saw it: They were too addicted to handouts from government. In fact, the non-profits often had to twist their missions to meet the needs of the donors, be they government or foundations. Strategy was dictated by the needs of the donors, not the clients. That didn't sound right to Young, so he switched gears. What about funding social enterprises – businesses that try to make money and serve a social purpose at the same time? That model was booming in Quebec, where in the past five years communities have launched businesses employing 25,000 people. These social enterprises – which might employ people with disabilities, or chronically jobless residents of low-income neighbourhoods – get plenty of money and non-cash help from the Quebec government and private companies. The funders figure it's a cheaper, more effective way to deliver social services than the alternative: welfare and all the problems and costs that go with it.

Ontario's Conservative government wasn't interested in that model, so Young tried a different route. He set out to find social enterprises that could operate a real business. They had to give otherwise unemployable people real jobs in a real workplace – and give them plenty of support so they could stick with it. At the same time, the enterprises had to break even – or come close to it – after paying the extra bills for training and counselling employees. Any company that could meet that standard would be rewarded with an impressive prize - $1 million funding over several years, plus plenty of advice from Young's organization on the business plan, marketing and sales, prices and other issues.

The hunt began. One contender was Toronto's Eva's Phoenix, which was setting up a print shop to employ some of the homeless youth living in its pleasant-looking shelter inside a converted warehouse. The print shop, in a tiny room with a few computers and two small printing presses, employs tens kids a year who make flyers, cards and other two-colour printed materials. It has registered impressive social results: most of the nine graduates in 2003 have found jobs or have returned to school. But it's losing money: expenses of$200,000 far outweigh gross revenues, expected to be $50,000 this year. Why? Because half the expenses pay for special training and counselling, such as teaching the kinds to turn up on time, says social enterprise co-ordinator Andrew McDonald. The print shop gets money from the United Way, Royal Bank and Ottawa to make up the shortfall.

"I think it's great," says Young, "but they're not trying to run it as a real business." Breaking even, however, is not an option, says Macdonald. The print shop would have to cut the number of employees, which would defeat the purpose of its existence.

Young eventually found what he was looking for in London, Ont., where a remarkable woman named Gwen Charles is rescuing unemployable people – and herself. Charles was a Manitoba politician and the mother of four until she crashed, falling into depression and ending up on welfare in Ontario. Her psychiatrist linked her up to a local psychiatric hospital that used to operate a little business employing patients. The hospital didn't want to run it any more, so Charles took charge. The company, Pivotal Services of London, has carved out a niche making custom packaging for leading Canadian manufacturers. It employs over 60 people – everyone from psychiatric patients to people living on the riverbank. Pivotal employees, who earn $6.85 per hour, are expected to be productive and have a positive work attitude. They have to turn up on time, barring a tough night outdoors. In return, they get training, counselling and other help.

The employees do a good job says Charles. "The best thing you can do for somebody is give him an opportunity and trust." Last year, Pivotal grossed $1.4 million and registered a net loss of $114,000, which is pretty good when you consider the extra cost of counselling. Apart from a $200,000 investment that was designed to help boost management, Young's group helped Pivotal define its core business and devise a pricing strategy. It's paid off – half of the employees each year leave to take better-paying jobs, and this year Pivotal won a Drucker award for non-profit innovation in Canada.

Young thinks Canada should encourage the creation of more social enterprises like Pivotal. But we don't. The key roadblock: Canadian law on charities. The law, and its interpretation by bureaucrats, makes it very hard for social enterprises, especially those that aspire to break even, let alone make a surplus, to pitch for money by offering a tax break to donors.

"We have a charitable regime that's out of date and behind the times," says Tim Draimin, executive director of Tides Canada Foundation, which supports community organizations across the country. "Compared with the United Kingdom, the United States and Australia, we're way behind in flexible ways charities can act to create new initiatives," he says. Charities have to play by very specific rules in order to give donors a tax break. You can, for instance, get a tax break for giving money to a charity that trains the homeless. But if you want to give money to a business that employs them – and counsels them on the job – you're probably out of luck.

Young choose his words carefully when asked about the rules on charities: "It should be easier," he says. Despite all the roadblocks, however, Young is still optimistic about supporting organizations that seek to break even or make money, and employ the unemployable at the same time. Over the past two years, he's found a handful and given them approximately $500,000. "it's going to be long journey," he says. "When you try to combine the difficulties of running a business with the insistence on employing people that others deem to be unemployable, it's tougher to succeed than it was to get rich in the late 1990s. But it's a way more satisfying challenge."

The complexities of Canada's charity law, and the pitfalls of doing business in the non-profit world, seem a long way off to the 30- and 40-something business types meeting in Social Venture Partners' Calgary Office on the 29th floor of a downtown office tower. In another time they would have been called Yupppies. But these nine SVP partners – two of whom have completed gruelling Ironman races – don't exactly fit that me-myself-and-I image. They're eager to learn how to give away their money in the most effective way, and on this bitter Tuesday night they begin five months of weekly meetings to chose one charity out of 73 applicants. The winner will get up to $40,000 per year for three to five years, plus management help from SVP. Tonight is dubbed Get Smart - a chance to learn about the issues affecting kids, SVP's focus. They help themselves to noodles and meat sauce on takeout plates, and get to work.

SVP's program manager, Cammie Kaulback, stands at the white board and asks the question: "So what are the pressing issues?" Silence. Then the SVP partners start drawing up a list, which Kaulback writes on the board: Nutrition, poverty, literacy, drugs … They're not experts, but it's a start. SVP, after all, is trying to create a new generation of philanthropists who give away management expertise along with time. The lengthy due diligence process will change them, predicts one attendee, a VP of operations for a software company and Ironman veteran named Shawn Ovenden. Once the SVPers team meet people like Pamela Scott and see what families with no money have to contend with, goes the theory, they'll never turn back.

It is ironic, isn't it? The venture philanthropists thought they could teach the non-profits a thing or two about how to run a business, even a social business. But as it turned out, the social workers in the trenches taught them something, too – about real life in the lanes and homes that are located a long way from the executive suite.