

**Issue #143, September/October 2005****The Revolution Will Not Be Grant Funded**

Philanthropic support is declining and government subsidy is disappearing. Isn't it time for CDCs to break the shackles of foundation support and let the market set them free?

By Michael H. Shuman and Merrian Fuller

For 40 years community development corporations (CDCs) blossomed from the financial nutrients provided by myriad government programs and America's wealthiest foundations. Now that this era of soft money is coming to an end, some CDC managers are filled with dread. We believe the more appropriate response should be one of excitement, because CDCs can – finally – break free from the shackles of the philanthropic plantation.

CDCs now must do what they have helped others to do – to enter the world of community entrepreneurship. There are already numerous examples of creative entrepreneurship in the nonprofit world. Housing Works in New York uses its Used Book Café to generate more than \$2 million annually for its work, which prioritizes advocacy for homeless people with HIV. The organization runs clinics, conducts public policy research, lobbies federal and state officials, even leads sit-ins. It is fearless, aggressive and stunningly effective – and its \$30 million of annual work would be impossible were it not for its vast range of realty, food service, retail and rental companies that help pay the bills.

“What we are about,” says Housing Works president and chief executive officer, Charles King, “is the business of changing the entire paradigm by which not-for-profits operate and generate the capital they need to carry out their mission – a new paradigm based on sustainability and social entrepreneurship.”

We believe that the spread of social entrepreneurship, as a positive alternative to conventional fundraising, offers a fundamentally new strategy for CDCs to expand their power and their voice in the United States.

**Illegitimate Birthright**

Community entrepreneurship could have been the hallmark of CDCs. In the late 1960s politicians on opposite sides of the aisle, including the liberal Wisconsin Senator Gaylord Nelson and the conservative Vermont Senator Winston Prouty, sponsored the Community Self-Determination Act, which would have linked CDCs more directly to their neighborhood bases and encouraged them to expand their work through for-profit subsidiaries. The idea was to form community-based organizations owned by local shareholders, who would use proposed tax advantages to undertake riskier projects with public benefits. These organizations would reward smart investors and smart CDC managers with profits, attract private investors into the War on

Poverty and create a new generation of self-financing, community-based institutions for social change. Of course, it never worked out that way.

CDCs wound up staying in the nonprofit ghetto, and today, four decades later, CDCs can point to a track record that is, at best, mixed. The good news, according to a 1998 report by the National Congress for Community Economic Development (NCCED), is that there are some 3,600 CDCs that have produced, over their collective lifetime, 247,000 private sector jobs and 550,000 units of affordable housing. The bad news is that these data mean that a typical CDC, with a 15-year life according to the survey, had produced 69 jobs and 153 housing units, which isn't very impressive. While one can quibble with these numbers, the indisputable bottom line is that CDCs are a very long way from meeting the employment and housing needs of their own communities.

One significant drag on CDCs' performance, we believe, has been their reliance on foundation and public monies. As nonprofits, successful CDCs cannot easily grow, except through retained earnings and debt, while for-profits can also turn to the stock market. Even well-run nonprofits tend to grow slowly, if at all. Nonprofits also do worse during hard times, as many CDCs will soon discover. Without much in the way of assets to serve as collateral, few nonprofits qualify for significant bridge loans. With a social mandate and misguided board pressure to spend accumulated earnings, most perpetually operate on the brink of bankruptcy.

After reviewing these and other problems facing nonprofits (high staff turnover, poor management, overreaching boards, zealous IRS regulators), one of the leading promoters of entrepreneurial nonprofits, the Roberts Foundation, concedes, "Were there a significant competitive advantage to being a nonprofit engaged in revenue-generating activities, we would have witnessed a marked increase in the number of businesses seeking...to take advantage of the added financial benefit of nonprofit status in the marketplace. In fact, we see just the opposite." Indeed, in an era when many nonprofits have converted into for-profits to become more competitive, it is almost impossible to think of any for-profit that has converted into a nonprofit.

The really bad news is that the absence of financial self-reliance could soon destroy many existing CDCs. The pots of public and philanthropic dough that have long supported CDCs are shrinking in the face of yawning deficits at all levels of government, a proliferation of worthy causes begging for support (the victims of Hurricane Katrina being just the latest competitors), and feelings of exhaustion and boredom by funders who say that 40 years are enough. As Bill Clinton once said about welfare, grants and public money must be viewed as a second chance, not a way of life. Now is the moment when CDCs must rise to the challenge of making it on their own.

### **Mission Warp**

To many CDCs, enlisting the power of entrepreneurship to gain independence puts their mission at risk. The concern is not unwarranted. J. Gregory Dees of the Duke University Fuqua School of Business argues that the entry of the YMCA into the exercise and health club business pulled it away from its original mission to serve at-risk young men and made it an upper-middle-class organization. More than a few entrepreneurial CDCs now build crass shopping malls and sprawling neighborhoods for the middle class. The bottom-line logic of business can lead the

nonprofit enterprises to neglect people without money, including the young, the old, the poor and the sick.

Critics overlook, however, the fact that many of these dangers already swirl around those rattling a tin cup for soft money from wealthy individuals and foundations. Building a philanthropic base of support instead of an entrepreneurial one can cripple an organization's mission and wreck it altogether when the well runs dry. Most CDCs have engaged in a kind of fundraising arms race in which our best leaders focus more time, energy and resources, not on changing the world, but on improving their panhandling prowess to capture just a little more of a philanthropic pie that actually expands very little from year to year. Armies of "development" staff spend as much as a third of an organization's resources, not to advance the poor, but to cultivate wealthy donors. Significant numbers of our colleagues create campaigns, direct-mail pitches, telemarketing scripts, newsletters and other products exclusively to "care and feed" prospects, and frame positions and adopt tactics that will not offend the rich.

A better way for a CDC to preserve its mission, while embracing entrepreneurship, is to keep its revenue generation work as separate as possible from its advocacy and organizing work. Ideally, it should be set up a subsidiary. Put everything that can conceivably be placed on a break-even footing (or better) into the revenue generator and use the proceeds to underwrite everything else through the nonprofit. The subsidiary can be either a for-profit (our preference), a separate nonprofit with a clear revenue-generating mission or even just a department within the CDC with a strong measure of autonomy. In all these models, the mission-oriented nonprofit essentially becomes an investor, leaving actual operations of the enterprise in more business-oriented hands.

Pioneer Human Services is a CDC based in Seattle that assists a wide range of at-risk populations, including the unemployed, the homeless, ex-convicts and alcoholics and addicts. The organization serves 6,500 people a year and generates nearly all its \$55 million budget through a web of ambitious subsidiary nonprofit businesses: cafes and a central kitchen facility for institutional customers, aerospace and sheet-metal industries, a construction company, food warehouses, a real estate management group and consulting services for other nonprofits. Most of the jobs in these businesses are awarded to its at-risk clients, allowing it to further its mission to integrate clients back into society.

Nonprofits other than CDCs have also embraced this strategy. The Rocky Mountain Institute, a leading promoter of alternative energy technology in Snowmass, Colorado, is an example. E-Source, begun as a project within the nonprofit in 1986, provides in-depth analysis of services, markets and technologies relating to energy efficiency and renewable energy production. In 1992 RMI secured a program-related investment from the MacArthur Foundation to move the work into a for-profit subsidiary. By 1998 it was generating about \$400,000 for the parent nonprofit, but RMI decided it could do even better under new management, so it sold the company to Pearson PLC in Britain for \$8 million. Today, RMI assists and benefits from other for-profit spinoffs, such as Hypercar, Inc., which aims to create a lightweight body architecture to improve the efficiency of the entire U.S. automobile fleet.

These kinds of subsidiaries, of course, are not without risks. A cautionary tale comes from the Milwaukee YWCA, where the director, Julia Taylor, had distinguished herself as a model

entrepreneur. Between 1986, when she began her tenure, and 2002 she had developed a variety of for-profit businesses, including a computer software company and a plastics factory, to expand the organization's budget nearly a hundredfold. The collapse of these subsidiaries in 2003 left the YWCA saddled with millions of dollars of debt. Taylor herself was one of only two board members overseeing the computer software company, and paid herself stock options (which were ultimately worthless).

Minnesota Public Radio's (MPR) sale of its mail-order catalogue business to Dayton Hudson Corporation for \$120 million was also controversial. The deal was executed by the Greenspring Company, a for-profit subsidiary whose executives – including MPR's president, William Kling – are expected to pocket \$7.3 million each.

What made Taylor's and Kling's actions ethically problematic was not that they acted entrepreneurially but that each kept one hand in the nonprofit while putting the other in the pocket of the for-profit. CDCs must operate at arm's length from related revenue generators, with different management, staff, activities and cultures. And the enrichment of any person within the nonprofit must remain strictly prohibited. But the examples above also suggest how CDCs, if they are careful about how they structure the relationship, can use subsidiaries to become more financially independent without drifting from their mission.

### **Anti-poverty Businesses**

Sooner or later, the concept of CDCs and of socially responsible businesses should become indistinguishable. Truly responsible businesses will be owned by all members of a community (rich and poor), hire locally, expand local skills, comport with local labor and environmental standards, produce goods and services that meet urgent local needs and become allies of social justice movements. What better way to help the poor than to transform them into captains, worker-bees, shareholders and customers of community-friendly business?

By some reckonings, we're now on the third generation of socially responsible businesses. The first generation comprised Fortune 500 companies that tried to improve their social performance, often in small ways with large public relations budgets, like American Express's Share Our Strength campaign. Many executives in these companies continue to share best practices through Business for Social Responsibility (BSR), which got started in 1992.

The second generation represents small and medium-size businesses whose proprietors are more eager to align themselves and their companies with progressive causes, and whose CEOs collaborate through organizations like the Social Venture Network (SVN). We applaud the Body Shops, the Ben & Jerry's and the Benetton's of the world, each of which manufactures decent products, comports (however imperfectly) with reasonably responsible labor and environmental standards and has snippets of political education in its advertising. The importance of the millions given by these kinds of companies – Newman's Own, for example, has donated more than \$150 million to charities, including many progressive causes – should not be underestimated. But at the end of the day, the core products of each, whether cosmetics or ice cream, are pretty ho-hum, and they are not linked to any particular community.

What has impressed us most is the growing number of local businesspeople who not only “walk the talk” of social justice in the small details of their operations and products but also tout the virtues of local ownership. This third generation is now being led by the Business Alliance for Local Living Economies (BALLE) and by the American Independent Business Alliance (AMIBA). Both emerged in recent years as grassroots alternatives to BSR and SVN and have mushroomed into three dozen chapters with several thousand affiliated small businesses, including local CDCs. Each promotes local ownership of the economy, pushes for new public policies that remove the tilts in the playing field that currently favor badly behaved big business and increasingly promotes social justice and neighborhood revitalization.

One of the founders of BALLE is Judy Wicks, whose White Dog Café in Philadelphia is as much a community organizing center as a restaurant. Radical speakers from around the country provide a steady stream of lectures. An adjacent store sells “fair trade” products and will soon be introducing a line of locally made clothing. The White Dog itself embodies principles of social justice and environmental stewardship by paying all employees a living wage, insisting on humanely raised meats and eggs, using locally grown ingredients and running on wind electricity. Twenty percent of profits from the restaurant go to the White Dog Café Foundation, carrying on the café’s mission through nonprofit activities.

### **Next Steps**

If foundations and donors had never existed and professional panhandling had been outlawed, CDCs would have been forced to create and run new enterprises or new networks of local businesses, and our movement would be considerably healthier than it is today. Progressives have become the classic twentysomething kid still living at home, expecting an allowance from the deep-pocket parents for a few basic chores, while agreeing, as a condition for the chump change, to obey someone else’s rules on social change. It’s time to grow up and strike out on our own.

Here’s a challenge to CDC managers (one we take seriously ourselves): Let’s try to wean ourselves from the charity habit, say by 3 percent per year. Think about just one piece of your agenda that could be framed as a revenue generator, dream about it a little, develop a business plan and give it a try. If you lack the skills, skip your next fundraising class and instead attend one of thousands of entrepreneurship programs around the country. Or hire someone who might start the entrepreneurial subsidiary of your nonprofit.

The fateful decision nearly half a century ago to make CDCs nonprofit was rooted in the beliefs that the poor were unbankable, that affordable housing was unprofitable and that poor communities made lousy markets for new business – all embarrassingly paternalistic and incorrect assumptions that have been demolished by the work of thousands of socially responsible entrepreneurs. There may be progressive causes that cannot be fought in self-financing ways, but the focal points of CDCs – to provide affordable housing, neighborhood revitalization, and new business and entrepreneurship opportunities – are fortunately not among them.

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Local Living Economies. This article was adapted from “Profits for Justice,” which first appeared in The Nation, January 24, 2005.

#### Resources

Social Venture Network

[www.svn.org](http://www.svn.org)

Business Alliance for Local Living Economies

[www.livingeconomies.org](http://www.livingeconomies.org)

American Independent Business Alliance

[www.amiba.net](http://www.amiba.net)

“What If Everyone Had a Job?” by Richard Taub. Shelterforce, September/October 1996,

[www.nhi.org/online/issues/89/everyon\\_job.html](http://www.nhi.org/online/issues/89/everyon_job.html)