Social Enterprise and Strategic Philanthropy
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A New Orientation for Not-For-Profit Charities/Businesses

In 2011, an article in *Business Week* detailed the birth of 'philanthrocapitalism,' which advocates that nonprofits change their business behaviors into a capitalist mode that mirrors for-profit industry. To achieve this transformation, new institutions would focus on social investing and entrepreneurship. It went on to say that, this new form of 'venture capital' could support the philanthropic equivalent of stock markets, investment bonds, research houses and nonprofit consultant firms. This form of so called 'social-impact investing' would also encourage private philanthropy and foundations to behave like active investors looking for the social returns of positive outcomes and impacts.

By definition, social entrepreneurs are the innovators seeking to solve social problems through social investing. In 2010, the potential of social entrepreneurship caused the Obama administration to launch a small scale Social Innovation Fund (SIF) that creates partnerships between government, private capital, social entrepreneurs and the public.

Mr. Goldsmith, in his book titled *The Power of Social Innovation*, invites the government to support collaboration between for-profit and nonprofit organizations to deliver what he terms 'disruptive transformative innovation.' A new corporate form of public interest company has emerged called a B-CORP that is a hybrid model that merges parts of a for-profit company and nonprofit organization. Its vision is to create a new mixed segment of the economy that leverages the synergies of for-profit and nonprofit business.

At first glance, investing for financial returns in philanthropy seems contradictory and far-fetched. However, where social good with improved outcomes and cost savings are provable and measurable, it could result in a model that yields both social and financial returns to the investor. For instance, if social investing from individuals, corporations and social impact bonds (SIB) resulted in long-term preventative and corrective programs that saved money, why should not they yield a financial return. Unhealthy lifestyles, criminal recidivism, high school dropouts, unemployment and homelessness are examples of problems that have societal costs and could be addressed with preventive solutions that have definable financial returns on paper. This sounds reasonable, but in our free enterprise system positive 'social results' do not produce a revenue stream even as they are universally applauded. Generally, treatment takes preference to prevention for social problems.

Social Enterprise

The goal of social enterprise and strategic philanthropy is to generate fees and revenue growth through commercialization of nonprofit products and services. This change in orientation is gaining advocates who wish to make funding of nonprofits more reliable and less beholden to outside subsidies and donations. A host of consultants conducts workshops and seminars devoted to this new creed. In these didactic sessions, the lesson plans are very similar to courses taught in American business schools. Here are some of their tenets.

1. Social enterprises should be market-driven and focus on the customer using market research.
2. The boards and directors of nonprofits should proactively think strategically in pursuing acceptable organizational risks in order to reap greater rewards in achieving impact and sustainable growth.
3. Achieving ambitious goals and objectives form the basis for compensation of social entrepreneurs.
4. Staff workers should shoulder greater responsibility for outcomes and ownership of projects.
5. Management should be less forgiving of employees who underperform and receive poor performance reviews.
6. Boards and senior managers should govern and execute programs strategically rather than tactically.
7. Programs and activities that are not profitable or fail to measure up are ‘right-sized,’ reorganized or cut.
8. All processes are under strict control in the light of organizational advancement and return on investment.

Although entrepreneurship and social innovation is quite understandable in this new matrix of strategic philanthropy, how does altruism and standard philanthropy fit in this frame of hard-nosed business and Schumpeter’s ‘creative destruction’ principles?

Many of these new business practices are neither new nor historically foreign to not-for-profit entities. After all, not-for-profit status does not mean ‘for-loss.’ Nonprofits have always relied on fee payments of one sort or another. However, how do you fit mission-driven charities with operations that serve the less fortunate into a social enterprise mold? How can a soup kitchen, homeless shelter, food bank or religious mission become sustainable through fee revenues and morph into entrepreneurial entities? Additionally, if social enterprise closely mirrors for-profit enterprise, what differentiates them and what prevents unfair competitive advantage because one entity enjoys tax exemption while the other does not?

It is remarkable for experts to consider strategic philanthropy and social enterprise as original and transformational. One can argue that most any business produces ‘public good and community benefit’ by providing jobs and helping our communities grow and prosper. Many profitable businesses have little difficulty in qualifying as charities. For instance, any business that employs one or more disabled persons can apply. Among the ranks of charities are fitness centers, bookstores, TV and Radio stations, paper recycling, janitorial services, vending, mowing and lawn services, landscaping, bakeries, snow removal, home health and funeral homes.

One of the most blatant incursions into for-profit territory occurs in nonprofit hospitals that have large fitness centers open to public membership. A for-profit owner of a fitness center who pays property and state taxes would rightly consider this unfair competition from a deep-pocketed hospital system.

Nonprofit boards, executives and pundits justify this leap into social enterprise by citing their need for greater organizational stability and sustainability freed from the caprice, inefficiencies and hassles of private fundraising, public funding and foundation grants. Many venerable nonprofits already pursue business models that closely resemble their for-profit cousins and could operate profitably as for-profit businesses. My visit to the local Goodwill Industries facility convinced me that it is very profitable and could stand on its own without tax-deductions for individuals donating clothing and cars.

The decision to operate as a for-profit going-business usually rests on profitability and potential returns on investment (ROI). The decision to operate as a nonprofit usually rests on a worthy mission that can generate adequate outside public and private funding. However, the nonprofit organization that operates as a social enterprise merges profitable commerce and charitable mission. For many nonprofit employees and volunteers, this new model has created an identity crisis. Most workers for nonprofits link their career pathways to 'giving back', helping others and value systems. This causes dissidence with the pure profit motive and a focus on the bottom line. Especially for those in faith-based organizations, social enterprise distorts the image of self-sacrifice and generosity that coincide with their religious beliefs.

Generally, faith-based organizations are more resistant to social enterprise as their success stems from the generosity and devotion of their parishioners. Religious beliefs determine the mission and congregations can mold the mission to moral stances and human needs free from the encumbrances of commerce.

Examples of Social Enterprise

The Delancy Street Project in San Francisco turns drug addicts and criminals into artisans, first teaching them vocational building skills and then employing them in home-building and rehabbing projects. Mimi Silbert, the director of the Delancey Street Foundation, says, "The very idea of merging mission and money was anathema to me—it smelled. We have never taken any government money for several reasons and we do not rely on donations. People have to earn their own self respect—sitting around waiting for a welfare check is just as bad as the members of a wealthy family waiting for their daddy to die so they can become 'heir' heads."

Visiting nurse associations can qualify either as for-profit or nonprofit enterprises. For instance, the *Visiting Nurse Association of Greater Cincinnati and Northern Kentucky (VNA)* is the only freestanding 501-©-3 tax-exempt organization of over 100 other similar associations. Its stated purpose is to “service the needs of the indigent and those with limited resources” as well as to “educate professionals and the general public in the appropriate use of home care.” In 2007, according to VNA statistics, only 5 percent of the association’s services went to ‘free care’ with 15.5 percent of revenues applied to administrative expense. The VNA has no volunteer program or volunteer coordinator and raises only 3.5 percent of its revenues from private donations. What features qualify this agency as a nonprofit and all the rest as for-profits?

The *Cystic Fibrosis Foundation* raises over 100 million dollars a year to conduct over 100 clinical research studies seeking new remedies for the 30,000 Americans with Cystic Fibrosis. The profits from new discoveries flow back to the Foundation.

Are Hospitals Charities?

Many years ago, a tax-exempt status was granted to a hospital if its services were made available to all in the community (charity care), and it provided additional community or public benefits. However, with the advent of health insurance, Medicare, Medicaid and national wealth creation, there are too few indigents without healthcare insurance to meet this threshold of public good.

Unquestionably, hospitals have their share of uncollected receivables, but these write-offs are more than offset by insurance payments and cost shifting to those who can afford to pay. Most all hospitals have deep pockets, large endowments and robust profit centers, and their operations and administrative functions closely mirror the for-profit business model. A casual glance at the ubiquitous construction sites that dot the hospital campuses is testimony to their profitability.

In 1969, Washington lobbyists representing hospitals managed to persuade lawmakers to delete ‘charity care’ as a specific component for hospitals to qualify for nonprofit status. The new rules allow hospitals to substitute other benefits to the community, such as health fairs, cancer screenings and emergency care. These activities may legitimately form the basis for tax exemption for smaller charities, but are hardly a credible substitute for charity care in a hospital system that receives many million, if not billions, of dollars in revenues annually.

Hospitals have certainly become leaders in social enterprise and strategic philanthropy. Novel specialty clinics, mobile imaging centers, nursing homes and fitness centers are a sampling of services that hospitals concoct to add to the bottom line and brand. In addition, hospitals are feverishly buying up medical practices and hiring physician hospitalists and intensivists to become integrated multispecialty Accountable Care Organizations (ACOs). In addition, this coupled with sophisticated information systems will position them to compete directly with Health Insurance Companies in the provision of population based healthcare coverage.

The benefits that accrue to hospitals as charitable organizations give them considerable wiggle room to operate inefficiently. This corporate welfare trumps market forces and lowers fixed costs enabling underperforming hospitals to remain in business by simply cutting staffing and providing only profitable services.

The American Hospital Association (AHA) should be a relatively apolitical entity, but in reality, the hospital lobby wields enormous influence in Washington. The AHA's $100 million in annual revenues are, in large measure, used to influence public policy that protects the interests of hospitals. To garner support for healthcare reform, it is widely rumored that the Obama administration struck a deal with the hospital lobby to accept some cuts in reimbursement in exchange for the continuation of their tax-exempt status.

Partnerships between For-profit and Nonprofit Enterprise

The involvement of for-profit enterprises in nonprofit causes is growing and no longer considered the soft side of their marketing plans and initiatives. The number and size of corporate sponsorships and joint projects has expanded, as 'cause-related marketing' has become a significant part of public relations. Corporate assistance comes in many other forms including discounted rents, piggyback advertising, computer software, use of conference facilities, staff training, office equipment and marketing. In return, the stamp of approval and overt appreciation from a respected charity can send a message to the community that a company is a good corporate citizen; ergo a good place to work and patronize. As these synergies grow, so do the number of corporate logos that crowd the web pages of nonprofit organizations. This interest in cause related marketing, however, rarely transfers business knowhow and management skills to the operational platforms of nonprofit partners.

As major companies have become more sensitive to their corporate image and public opinion, 'corporate social responsibility' (CSR) has gained traction across all aspects of commerce. CSR is measured through a so-called 'triple bottom-line' in which a company reports not only its financial results but also what it is doing to provide community benefit and also address more global concerns that impact the environment, equality and education. Moreover, corporate America has become the nexus for volunteer projects such as building a house for Habitat for Humanity or a clean-up campaign. Nonprofit board experience for rising corporate executives is frequently used to nurture leadership skills, foster networks of like-minded individuals and build moral fiber.

Not surprisingly, this panoply of 'corporate virtue' is even evaluated by Dow Jones through its indices of socially responsible companies.

Reconciling Mission with Social Enterprise

Clearly social enterprise and strategic philanthropy can increase the capacity and potency of the social sector. The problem arises when an organization does not reconcile its mission with its social enterprise, and become enamored with commerce at the expense of social values.

This leads us finally to the Public Policy Dilemmas that underlie these new directions.

a. What are the boundaries that delineate and differentiate between for-profit and nonprofit organizations?
b. What guidelines identify for-profits that enjoy not-for-profit advantage to the detriment of their competitors?
c. How do regulatory agencies sort out ‘unrelated income’ issues and disqualifying mission creep?