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Change Capital Investments: One Tool for Moving to Abundance

By Meghan McDermott

The Long Arm of Crisis: Undercapitalization Means Uncertainty

When the front wave of the economic crisis came into national focus in 2008 it wasn't clear how long the crash would last or how much damage it would do. It wasn't clear, as it is now, how the downturn would fundamentally change the ways in which the independent nonprofit sector and its philanthropic partners regard each other's value and purpose. Conditions continue to be hard for nonprofit organizations. According to "Diminishing Dollars,"[1] a joint 2011 report from The Foundation Center and the Cricket Island Foundation, smaller foundations with less than $50 million in assets expect grant-making expenditures to be nearly 30% less in 2015 than in 2008. And even as assets begin to rise again for some of the bigger foundations, giving remains static or low[2] with the largest source of all charitable donations in 2011 coming from individuals (73%) versus foundations (14%).[3]

This situation has been particularly devastating for youth groups operating at the intersection of community arts and social justice, which have experienced severe drops in funds for both arts-related and youth-organizing work over the last five years. A recent field scan conducted by the Funders Collaborative on Youth Organizing (F.C.Y.O.) noted that over 40% of respondents to their national survey reported a decrease in foundation support, revealing "a potential threat to the growth of the field and the health of the communities that groups support." Importantly, funds that continue to be granted are described as "more issue-focused, shorter-term, and more restrictive."[4] And reflecting the dire state of the arts, the Nonprofit Finance Fund's 2013 "State of the Field Survey" reports that the sector "remains divided between the 'haves' and 'have nots': 60% of arts organizations reported three months or less of cash on hand. While 20% added to reserve funds in 2012, an equal number drew down already limited liquidity."[5] Compounding these trends, the National Committee for Responsive Philanthropy's (N.C.R.P.) Niki Jagpal and Kevin Laskowski's recent report titled "The Philanthropic Landscape" reveals that "general operating support continues to remain relatively scarce among the nation's largest grantmakers, which overwhelmingly favor project grants and other forms of restricted support."[6]

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[1] Gould, S. (2011). *Diminishing Dollars: The Impact of the 2008 Financial Crisis on the Field of Social Justice Philanthropy*. Foundation Center, NY: 1. http://foundationcenter.org/gainknowledge/research/pdf/diminishing_dollars2011.pdf

[2] Gose, B. and Carew Grovum, E. "Caution is the Watchword as Big Foundations Keep a Rein on Giving Despite Growing Assets" in The Chronicle of Philanthropy *(*March 24, 2013). http://philanthropy.com/section/Foundation-Survey/424

[3] http://www.nptrust.org/philanthropic-resources/charitable-giving-statistics

[4] Braxton, E., Buford, W., and Marasigan, L. *2013 National Field Scan: The State of the Field of Youth Organizing*. Funders' Collaborative on Youth Organizing, NY: 4. www.fcyo.org/media/docs/7343_FCYO-11-01.pdf

[5] http://nonprofitfinancefund.org/files/images/2013_arts_survey_results_summary.pdf

[6] Jagpal, N. and Laskowski, K. (May 2013). The Philanthropic Landscape: The State of General Operating Support 2011

Although the numbers are stark, it appears funders have grown tired of hearing about the problem of "sustainability." Instead, market-based solutions hold the philanthropic gaze—despite such solutions being difficult for social-justice nonprofits to implement. Meanwhile, stabilizing long-haul resources for organizational infrastructure are rarely discussed. The outcome? Ironically, a widespread "investment" in unsustainability and undercapitalization, or what Ann Goggins Gregory and Don Howard classify as the "nonprofit starvation cycle,"[7] which "starts with funders' unrealistic expectations about how much running a nonprofit costs, and results in nonprofits' misrepresenting their costs while skimping on vital systems."

Simply, the nonprofit field must move beyond its chronic state of financial stress. A major change is necessary, one that understands that **a key to nonprofit fiscal health is a grantee-donor relationship based on trust, mutual accountability, and a genuine commitment to a grantee's success over the long haul**. What is needed is a shift in the philanthropic framework, one that may be counterintuitive to current discourse, but offers a clear, measurable, and tested way to plan for stability and impact. This framework is called "change capital."

To illustrate the potential of this process in a real-world context, Global Action Project (G.A.P.), an award-winning social-justice media-arts organization working with youth, decided to document its work to craft a sustainable business plan. G.A.P. knows it is not alone in its struggle to stay viable against a rapidly changing philanthropic landscape. It recognizes that public space for candidly discussing planning for survival is potentially hazardous for nonprofits in need of help. The understandable and well-reasoned fear is that funders will turn away. G.A.P.'s audience for this sharing consists of its colleagues in the field: small, social justice-oriented arts nonprofits and grassroots organizing groups that have experienced disinvestment or even had to consider shutting their doors. G.A.P.'s goal for sharing is to help these organizations plan for sustainability on their own terms and empower them to ask their funder allies for what they truly need: accountability to the relationship, resources to plan, and targeted investments of "change capital" to support efforts to achieve long-term financial viability.

According to Teresa Basilio and Jesse Ehrensaft-Hawley, G.A.P.'s co-directors, "we want to share how this kind of funding can be used to fight for a future of abundance instead of one defined by scarcity." While the timeline for a turnaround is not quick or guaranteed, "we hope that change capital can be seen as a way to reset expectations between grant-making and grant-seeking partners and addresses the core issue of chronic undercapitalization."

Change Capital: A Tested Tool

What is change capital? According to the Nonprofit Finance Fund, it is one-time, upfront funding that allows an organization to change and adapt its business model in line with its core values and its capacity to generate reliable, recurring revenue. While general operating support "pays for organizations to do what they already do" and is a form of flexible revenue that helps to keep the lights on, change capital is an investment in broader organizational change that will strengthen its future prospects by supporting: 1) improvements in the efficiency or quality of programs or operations, or 2) growth, downsizing or other adjustments to the size and scope of an organization."[8]

The first national deployment of change capital for the arts sector was developed, documented, and shared through the Nonprofit Finance Fund's (N.F.F.) $15 million Leading for the Future Initiative, supported by the Doris Duke Charitable Foundation. As a result of N.F.F.'s work and a series of capitalization workshops sponsored by Grantmakers in the Arts, change capital has emerged as a promising approach to helping "arts organizations adapt their programming,

[7] Goggins Gregory, A. and Howard, D. (Fall 2009). "The Nonprofit Starvation Cycle." Stanford Social Innovation Review. http://www.ssireview.org/articles/entry/the_nonprofit_starvation_cycle

[8] Thomas, R. and Christopher, R. with Sidford, H. (2011). "Case for Change Capital in the Arts: Building Vibrant and Viable Cultural Organizations." Nonprofit Finance Fund, NY: 10. http://nonprofitfinancefund.org/case-change-capital-arts

operations and finances to thrive in a changed and changing economic and cultural landscape."[9] Change capital is challenging to raise. It requires donors to rethink expectations and behave more like long-term investors but ultimately "supports organizations in changing what they are capable of doing."[10] As N.F.F. describes it, "Change capital is an investment in the alignment of an organization's fixed costs to its reliable, recurring revenue. It is spent down with the explicit expectation that it will lead to improved recurring net revenue (i.e., surplus) to sustain delivery of programs once the capital is fully spent."[11]

Change capital is about planning forward. And while many organizations need recovery and change capital to stabilize themselves after significant reversals (including, but not limited to, changes in funder priorities), change capital can allow for the full revision of a nonprofit business model based on terms that are defined by mission and constituency, as well as realistic expectations of revenue. These revisions don't happen all at once, but over the course of a few years, an organization can change its fiscal course and capitalization structure.

Instead of nonprofits reacting to potentially ill-advised market-based solutions like "just charge a fee" or "monetize your products" with *ad hoc* income-generation strategies, asking for change capital is requesting a demonstrated commitment to the purpose of an organization and its ability to advance its mission over the long-term: it is asking for funds to plan a better and more realistic future. Organizations that scramble too quickly to implement untested revenue-generating activities—without capacity, technical assistance, or the chance to develop internal expertise—find themselves dangerously stretched, sometimes to the point of collapse. When small nonprofits launch new revenue strategies, they are in effect launching a new business. Clear statistics are hard to come by, but many for-profit entrepreneurs generally accept that most new ventures fail, and of those that succeed, it can take up to three years to demonstrate an initial return.

For nonprofits dedicated to arts and social change, there's not much to actually "monetize" and certainly not at the level required to ensure the bulk of operating costs. Even grassroots fundraising, which can be deeply value-aligned as a member or community-led empowerment strategy, rarely accounts for an organization's whole operating budget or compensate for extreme or sudden loss of institutional support. Diverse income streams are key to financial health, but **too many nonprofits are in a daily struggle for survival that pulls energy, time and resources towards maintaining financial security and away from achieving their mission.** Something is very wrong. In contrast, funders who make change capital investments provide organizations with the means to pause and assess, responsibly plan and test, and then take a calculated and informed risk rather than piecemeal or untested strategies for getting resources in the door. According to Philip Rosenbloom, manager of advisory services for New York at N.F.F., "It is not feasible to expect new income streams to quickly and successfully materialize without support for planning and implementation. That support is change capital."

It's not rocket science. If nonprofits and funders committed to work together—nonprofits pursuing sustainability in their business models and funders making change capital investments to support that process—it could precipitate a sea change in the field: stronger organizations, improved accountability, and funders and grantees achieving their goals.

How to Jump Start a Turn-Around

For over 22 years, Global Action Project has worked with young people to engage them in producing powerful media for change. In that time, youth have produced hundreds of videos that have reached diverse audiences, won international and domestic acclaim, and effected change through their leadership and artistry. Yet despite its history and stature in the field, in 2011,

[9] http://nonprofitfinancefund.org/CRF/Change-Capital

[10] Thomas, R. (Fall 2013). Capitalization, for Art's Sake! In the GIA Reader, Vol 24, No 3. http://www.giarts.org/article/capitalization-art%E2%80%99s-sake

[11] http://nonprofitfinancefund.org/CRF/Change-Capital

G.A.P. faced a budget crisis with the elimination of funding from a foundation that had supported its media-arts programming for nearly a decade. This foundation was not the only one moving away from the youth-media and youth-organizing fields; G.A.P. and other youth media groups observed a steady erosion of funding for youth leadership programs and initiatives promoting civic engagement and social change by young people and communities most affected by injustice. Like many of its social justice grassroots colleagues, especially those engaged in the arts, G.A.P. had seen a precipitous drop in income since 2008—nearly 50% in over four years—and had struggled to identify reliable funding. The recession had left the group depleted. It was time to consider alternative scenarios for the future of the organization with board and staff, including the serious consideration of closing its doors. G.A.P. was experiencing firsthand how drops and shifts in nonprofit funding have adverse short- and long-term effects on the "cultural ecosystem, particularly for the smaller, newer, edgier, parts of that system and the artists groups serving…least advantaged communities."[12] The changing landscape made it imperative that G.A.P. adapt and evolve its structure to remain viable and eventually thrive.

As a community, G.A.P. saw it was time to evaluate its financial resilience by better understanding its options. It devised a comprehensive planning process that included concurrent tracks: 1) convening dialogues with colleagues and allies in the field to share ideas, 2) a SWOT analysis (an assessment of strengths, weaknesses, opportunities, threats) with *pro bono* help from the Taproot Foundation, 3) pointed conversations with crucial long-term funders, and 4) extensive financial analysis with the Nonprofit Finance Fund. Then the board and staff engaged in a series of "best- to worst-case" planning sessions. "We designed a process to confront this moment—so everyone was invested in the outcome," describes Robert Winn, G.A.P.'s board chair. Working closely with N.F.F.'s Rosenbloom to complete a financial assessment spanning nearly a decade's worth of income and expense patterns, G.A.P. set its balance sheet in the context of the changing funding climate. This step helped G.A.P. understand more clearly how it had dealt with a cumulative drop in unrestricted dollars, and what continuing those behaviors was likely to do. This analysis informed the scenario planning, which included the prospect of sun-setting.

G.A.P. rallied against closure by making even deeper budget cuts and adjustments—it moved to a smaller office, significantly cut health benefits, continued multiple staff furloughs, and delayed its programs by three months in order to make space for comprehensive planning time. As Teresa Basilio reflected, "Rather than applying short-term tactics like band-aids, we wanted headspace to plan for a turn-around." Rosenbloom explains, "The process of an organization turning around is not about replicating what other people have done. It's learning which options are realistically adaptable for you since every organization has different sets of needs, reputations, networks and identity." From this vantage point, explains Dare Dukes, G.A.P.'s Director of Development and Communications, "G.A.P. saw the opportunity of change capital as an unconventional but useful ask to make in the service of articulating our larger sustainability vision in line with our social justice values. This vision not only recognized sustainability as money, but really as the potential to redesign our organizational structure, the opportunity to implement new models and practices, and not have to abandon our mission in order to chase new dollars."

G.A.P.'s conversations with crucial long-term funders were especially important. G.A.P. solicited constructive criticism and discussed why it was taking the change capital approach, explaining its view that earned income strategies carry incredible risk, and that ventures of any kind must net income. With ambitious goals and a blueprint for planning, G.A.P. approached a long-time funder. The foundation award G.A.P. a $75,000 grant to use the change capital approach to outline and implement a structure for long-term organizational sustainability, including identifying new revenue streams (e.g., fee-for-service trainings, video sales, grassroots fundraising, more robust individual giving systems) to decrease reliance on foundations. To build its internal capacity to focus on net income, G.A.P. worked with N.F.F. to:

[12] Sidford, H. (2011). "Fusing Arts, Culture and Social Change: High Impact Strategies for Philanthropy." National Committee for Responsive Philanthropy, Washington, DC: pp1. www.giarts.org/article/fusing-arts-culture-and-social-change

- assess any venture's feasibility to provide net income, not just meet expenses;
- evaluate any strategy's fit with G.A.P.'s mission and key organizational strengths; and
- secure funds to cover early losses and one-time upfront implementation costs.

G.A.P. also worked internally to ensure that criteria guiding its financial direction were truly reflective of its social justice values. The idea of generating profit, and how G.A.P. would do it "challenged us," Basilio explains, "to think about new income strategies as a long-term commitment to our infrastructure. We had to critically look at the fundamental tensions of being able to do social justice work while responsibly holding—*owning*—the language and lens of a 'business model.' That was really hard for us."

G.A.P. turned to long-respected allies for models, such as the Highlander Research and Education Center. Dukes recalls, "We had to have, and continue to have, conversations about offering what we can for free versus charging what we think it's worth, and what we need to net in order to remain sustainable. Talking with key movement spaces like Highlander helped us think about it differently, that it's about defining guidelines for our fee structure (free, sliding scale, underwritten, etc.) in ways that support our work with the groups that matter most to our mission." As a social justice organization, G.A.P. was well aware of the financial fragility of movement struggles and the difficulty of needing to amass dollars from a range of funders in order to stop turning to institutional support at the same level. **"We have to create stability on our own terms,"** reflects Ehrensaft-Hawley.

G.A.P. drafted questions to answer through the change capital process. If it could have a diverse income portfolio, what would it be comprised of and what would it take to make it real? How could young people take leadership in grassroots fundraising and what would joint creative project partnerships look like? Critically important to G.A.P.'s sustainability vision was intentionally expanding its organizational relationships with communities, individuals and major donors connected to G.A.P.'s mission, and scaling its capacity-building trainings to advance culturally-based social-justice work with new opportunities to integrate creative strategies into social movement and campaign struggles.

But G.A.P.'s operating deficits between 2010-12 from reductions in foundation dollars had significantly eroded its balance sheet, with operating revenue declining almost 40%, so that even extreme cuts had not allowed G.A.P. to reliably cover costs. Now as part of its planning, "G.A.P. had to achieve an operating model that reliably allowed it to cover its full cost of business and build a balance sheet that provides the unrestricted financial resources that help you deal with uncertainty down the line," explains Rosenbloom. And while replenishing net assets could be accomplished through generating annual operating surpluses or by receiving one-time infusions of capital, or both, those options were going to take time to cultivate, underscoring the key challenges of projecting how long it will take to realize the full revenue potential of a new model and getting capital to cover costs during a ramp-up period.

A working committee of key staff and board members examined a range of economic forecasts to see if any of them would lead to sustainability. They included: 1) a review of G.A.P.'s national training institute for youth organizers, which historically had been fully underwritten and free for participants; as well as a restructured fee-for-service version, 2) school collaborations, 3) a new grassroots fundraising structure led by youth, 4) a major donor drive, and 5) space and program collaborations with mission-aligned community partners. Using a decision matrix generated by N.F.F., G.A.P. surfaced assumptions about its capacities to carry out any one of the strategies and then honed the list to a set of realistic activities. Dukes explains, "We identified ways to generate net income that were drawn from things we wanted to continue doing, on past successful efforts, and areas of new learning and risk that we wanted to take."

Over the planning period, G.A.P. staff met to talk through and quantify answers to the decision matrix by responding to prompts about structural variables, alignment with mission, and ongoing yearly and start-up costs. It also addressed where money might come from, how much demand there was for its programs and trainings, how reliable the revenue would be, and how much net income it could really count on. "We had to plan around the resources we already had in place versus the capacity we needed to bring in and at what cost. From there, we revised, modified down, and revised again, recognizing that each tactic had pros and cons, but some would be far more manageable and effective at netting income over time," says Basilio. "The critical realization was how long it would take for any option to not only meet the budget but provide us with net income. The ground work for any of these strategies to succeed would require building infrastructure—people, knowledge and capacity—over the long haul."

Moving Forward

Today, G.A.P. is purposefully moving forward. With N.F.F., it is building out its assessment with detailed projections for each strategy. As Dukes explains, "Our next stage of work is to determine what the implementation steps and trigger points are for getting funding to jump in or jump out of a given approach—low bar of investment versus a must-have amount—or we pull the plug on that strategy." Understanding that the full impact of change-capital dollars will only be visible over time and with a series of investments, Ehrensaft-Hawley agrees, "The big hurdle is understanding how to project over years of implementation and identify a return, how to assess we've gotten enough income to make it worthwhile. It's going to be slower in the first year of simply breaking even versus netting dollars." The line that G.A.P. walks here illustrates the reality of living within a tight margin of risk while striving to adapt to changing circumstances, as well as the need to build a surplus thoughtfully and with care.

Dukes reflects: "Like any large strategic question that an organization is exploring, it's really hard to wrest staff away from daily pressures to address the sustainability process in a way that we need to. So far, we are doing a good job managing and maintaining this conversation over years—with high stakes, and while we had a leadership transition—and keeping a clear-headed commitment moving forward. But one of the benefits of this process, among others, is that G.A.P. staff members are much more engaged in our organizational sustainability in a deep and articulate way. It's not an easy thought experiment to go outside normal boxes of how funding works in the nonprofit universe and convince funders why change capital as a tool to support planning for sustainability works and can be effective. The biggest challenge is to change the way we think about how philanthropy can and should work." Adding to that, Ehrensaft-Hawley notes, "Requesting change-capital dollars is asking a foundation to practice differently and consider an investment that can and should lead to an organization's creation of a self-perpetuating income stream."

The process has kept G.A.P. focused, inoculating the organization against over-reaction and coercion into merger as a strategy for survival. Basilio notes, "We have had the opportunity to do this on our own terms—deliberative, informed, and at a pace we can manage. Change capital was the tool we needed to shift our possibilities." The coming year will be pivotal for G.A.P. as it seeks solutions to unprecedented challenges. As Board Chair Robert Winn reflects, "With two decades of social-justice arts learning and practices to build on, we will continue to make dynamic media-arts programming for cultural organizers, youth, communities, and emerging leaders our core purpose. The change-capital tool has helped us set the groundwork for the next stage of growth so we can secure that vibrant future."

The Check List: Guiding Questions for Organizations & Grantmakers Seeking Long-term Sustainability

To help organizations plan for security, philanthropy should consider harnessing the power of the change capital tool, which is funding that is extra-ordinary, of limited duration, and flexible. Funds are meant to support periods when the organization is experiencing volatility or is at a critical moment of development—including moments of growth or moment of downsizing or re-organization. During these periods, organizations must take risks and have room in their budgets for trial and error. As a result, change capital can, on occasion, cover planned temporary operating deficits.

As G.A.P.'s story illustrates, change capital offers financial flexibility, but more than that, reflects a deeper accountability between grantees and funders, one that has the potential to break the starvation cycle and move the field to abundance. To assess readiness to apply the change capital tool, review these criteria:

For Grantmakers:

- Have you received repeated requests for technical assistance or capacity building dollars for structural or infrastructure improvements?
- Have you been frustrated that technical assistance grants for planning, preparing and implementing organizational downsizing or growth have not resulted in the desired change?
- Do you want to see organizations develop long-term plans for sustainability and security?
- Have you seen the balance sheets of organizations deteriorate as they launch new programs without adequate capital to cover the full costs?
- When funding issue campaigns and mobilizations, have you funded opportunities to build long-term infrastructure in these short-term projects?

For Organizations:

- Have you received or requested short-term technical assistance grants for making significant organizational and structural shifts and seen modest or unsatisfactory results?
- Are project grants not covering the full costs of conducting programs and leading to a regular or increasing budget shortfall?
- Have you considered new organizational structures or scenarios, including sun-setting?
- Have you been encouraged by funders or determined with board, staff and constituents to create new revenue streams without appropriate funding support, information and strategy on how to achieve this?
- Do you measure the success of efforts for long-term sustainability?

If you answered yes to any of these questions, explore applying a change-capital lens to efforts for organizational development. To learn more about change capital, please visit:

http://nonprofitfinancefund.org/CRF/Change-Capital

Further Reading and Suggested Links

Managing in the New Economic Reality.
www.nonprofitquarterly.org/management/20770-managing-in-the-new-economicreality.html

UnderDeveloped: A National Study of Challenges Facing Nonprofit Fundraising.
http://www.compasspoint.org/underdeveloped

No More Free Rides: Foundations Need to Increase General Operating Support Now.
http://pndblog.typepad.com/pndblog/2012/11/foundations-need-to-increase-general-operating-support.html

Foundations Must Get Serious About Multi-Year Grantmaking.
http://www.ssireview.org/blog/entry/foundations_must_get_serious_about_multi-year_grantmaking

Three Ways to Boost Core Support.
http://www.ssireview.org/blog/entry/three_ways_to_boost_core_support

Funding social movements: the New World Foundation Perspective.
http://www.edgefunders.org/wpcontent/uploads/2012/01/NewWorldFoundationFSM1.pdf

The Art of Adding Value: Variety New York's High Touch, High Impact Philanthropic Model.
http://varietyny.org/wp-content/uploads/2013/02/VarietyPaper_Feb2013_FINAL_pages.pdf

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ABOUT GLOBAL ACTION PROJECT

Founded in 1991, Global Action Project works with young people most affected by injustice to build the knowledge, tools, and relationships needed to create media for community power, cultural expression, and political change.

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