



## **FUNDING THEM TO FISH: The Case for Supporting the Earned Income Activities of Nonprofits**

### **Introduction**

Why are increasing numbers of grantmakers supporting the earned income efforts of nonprofit organizations?

To answer this question, the Social Enterprise Alliance reached out to more than 100 funders across North America, including those it convened at Sundance Village\* in May of 2003 to discuss the subject of “social enterprise” – that is, the income-producing activities and business ventures of nonprofits designed to sustain charitable missions.

The numbers of nonprofit organizations interested in starting new or advancing existing revenue generating activities is astounding by any indicator. Program (“earned”) revenue now represents the single largest source of income for nonprofit corporations according to the IRS. At the same time, if nonprofit organizations are to achieve genuine success in the arena of social enterprise, a more informed and purposeful partnership with the funding community will be required.

It is important to emphasize that this “case” is built upon the experience of funders who are already supporting nonprofits that pursue social enterprise. We share their insights with you in the hope that you, too, will consider funding grantees toward a more financially sustainable future.

### **What are the primary reasons for providing support to earned income projects?**

Here is what we heard. Among the principal motivators for funding earned income projects were:

1. To maximize philanthropic investments
2. To build nonprofit capacity
3. To increase public awareness of the organization; boosting its standing
4. To keep jobs in depressed markets
5. To provide a platform for sharing “best practices” across sectors

*“The Meyer Foundation is committed to strengthening organizations, not just supporting programs. Earned income initiatives strengthen organizations by providing income streams that aren’t subject to the caprices of private and public funders. They also help organizations acquire new capacities and skills that further their social missions.”*

### Maximizing philanthropic investments

The most frequent rationale offered by grantmakers for funding the social enterprise activities of nonprofit organizations was financial – a full half of all respondents. Eighty three percent of the funders specifically mentioned that they were interested in promoting the sustainability and self-sufficiency of their grantees by helping them diversify their income base. Others noted that earned income:

- Creates a source of unrestricted dollars, or “working capital”, that can underwrite innovation – a category of funding difficult to obtain through other means
- Helps to supplant the need for grant dollars even in enterprises that are not completely self-sufficient
- Leverages private sector funds, maximizing the impact of philanthropic dollars, and
- Increases the overall management and business capacity of the organization.

### Capacity Building

While the emphasis upon nonprofit capacity building has grown steadily over the past several years, only recently has the relationship between “capacity” and success at earned income activities become more broadly recognized and understood. It comes as no real surprise to funders to learn that successfully enterprising nonprofits are also better able to demonstrate their overall effectiveness and efficiency.

*“Our funding has primarily been in helping agencies develop the capacity for incorporating social enterprise methods in looking at opportunities. We are committed to assisting agencies in building capacity and become more self-reliant, partially to help them become less dependent upon our continuing funding for programs, and also to help them be able to generate funding to expand services.”*

More than one third of the funders noted the value of earned income efforts in building organizational capacity. They believe social enterprise:

- Results in good social outcomes and the ability to better articulate those outcomes
- Promotes innovation within the organization in support of its charitable mission
- Develops business planning discipline which positively effects the entire organization including:
  - A better understanding of the market forces at work in their communities including increased awareness of their competitive positioning
  - A better understanding of the real cost of delivering programs
  - Better coordination between the program planning and financial departments of the organization
  - Enhancement of marketing and communications efforts

*“Ben & Jerry’s continues to partner with nonprofits to develop PartnerShops because we see it as a great opportunity to help nonprofits achieve mission related goals, generate income, and enhance their reputation and increase their visibility. It’s a sensible way for us to leverage our core competencies (making and selling great ice cream) to help support nonprofits that are working to address social problems.”*

### Types of Earned-Income Activities Supported by Your Peers

Not surprisingly, the largest single category of earned income activity funded by grantmakers was Fee for Service initiatives. Nonprofits most commonly gain comfort and experience with earned income efforts through the introduction or expansion of fee for service or other tuition-based programs.

However, funders also report support for a broad array of enterprise efforts, including:

- Service businesses
- Retail operations
- Manufacturing
- Wholesale assembly
- Software products
- Consulting
- Rental housing
- Agri-business
- Real estate development
- Restaurants and catering
- Packaging
- Home Repair

Growing numbers of grantmakers interested in entering this “funding space” for the first time are doing so through generic technical assistance or capacity building grants. Some are underwriting the development of business plans for grantees and supporting their participation in entrepreneurial training processes. Others have sponsored their grantees to attend the Gathering of the Social Enterprise Alliance and buy memberships for grantees in the organization. Still others have directed funding through an intermediary with experience vetting social enterprise opportunities. Such support allows even those foundations without the internal capacity to analyze the viability of nonprofit business ventures to utilize or build upon the expertise of others to further earned income goals.

Finally, in the words of funders not yet engaged, social enterprise is:

“A logical and likely fundamental part of our interest in supporting the long-term sustainability of nonprofit organizations.”

“An area with much potential and an untapped concept in building capacity.”

“A way to help an organization to diversify and sustain revenue streams, build organization and community capacity on a number of levels.”

\* The Sundance event was conducted with the generous support of the UPS Foundation and in partnership with Grantmakers for Effective Organizations.

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## Social Enterprise Alliance Standard Lexicon\*

**Social Enterprise:** Any earned-income business or strategy undertaken by a nonprofit for the purpose of generating revenue in support of the nonprofit's social mission.

**Earned Income:** Payments received in direct exchange for a product, service or privilege. [Earned income for a nonprofit includes such elements as tuition and fees for service, commercial products or services, government contracts, consulting fees, membership dues (when dues purchase tangible benefits), sale of intellectual property, agreement to use the nonprofit's identity, property rentals, etc. Earned income does not include such sources as corporate, foundation or government grants or subsidies, contributions from individuals, or in-kind donation of products or services.]

**Financial Sustainability:** The extent to which a nonprofit is able to pursue its mission indefinitely through any or all of the following: earned income, charitable contributions and public sector subsidies.

**Self-sufficiency:** The extent to which a nonprofit is able to pursue its mission indefinitely through earned income alone without relying in whole or in part on charitable contributions or public sector subsidies.

**Double Bottom Line:** The definitive benchmark for a social purpose business venture – the simultaneous creation of both a financial and social return on investment.

**Triple Bottom Line:** A business venture's simultaneous pursuit of beneficial outcomes along three dimensions: economic, social and environmental.

**Financial Return on Investment:** ROI – an index of financial profitability that measures the net result of operations as a percentage of funds invested; an indicator of business success.

**Social Return on Investment:** SROI – the non-financial outcomes created by a social enterprise, measured in terms of the nonprofit's mission, e.g. people served or jobs created, average salaries paid, amount of transfer payments eliminated, etc.

**Social Entrepreneurship:** The art of persistently and creatively leveraging resources to capitalize upon marketplace opportunities in order to achieve sustainable social change.

**Social Purpose Business:** A discrete division, subsidiary or related corporation of a nonprofit or a for-profit company that deliberately pursues financial and social returns within a specific industry segment in the commercial marketplace.

**Earned Income Strategies:** Attempts to capitalize on the earned income potential of a program or other organizational asset (property, intellectual capital, reputation, etc.) in order to cover part or all of the program's costs or to offset a portion of the organization's overall expenses.

**Unrelated Business Income:** Earned income derived from the sale of products or services that are not directly related to the charitable purpose of a nonprofit organization. Such revenues may be subject to federal tax and, at significant levels in proportion to total nonprofit income, may jeopardize the tax-exempt status of a nonprofit corporation.

**Venture (or "Engaged") Philanthropy:** The application by donors of principles traditionally associated with venture capitalists to improve the capacity or performance of a nonprofit organization or social enterprise. Engaged philanthropy practices typically involve a combination of funding and expertise, more direct engagement with leadership, long-term funding relationships (three to six years), performance monitoring, and an exit strategy.

\* Lexicon developed in cooperation with Jerr Boschee, Institute for Social Entrepreneurs.

The Social Enterprise Alliance is a 501(c)3 organization. It is our mission to build stronger, more effective nonprofit organizations by mobilizing a community of practitioners and investors to advance earned income strategies. For more information contact Beth Bubis @ [beth@se-alliance.org](mailto:beth@se-alliance.org) or visit our website at: [www.se-alliance.org](http://www.se-alliance.org).