



Public Expectations and Nonprofit Sector Realities: A Growing Divide with Disastrous Consequences

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Introduction

It gives me enormous pleasure to have been asked to participate in the *Issues in Philanthropy* lecture series. Georgetown University's Center for the Study of Voluntary Organizations and Service and the Georgetown Public Policy Institute are to be commended for sponsoring this series honoring Waldemar Nielsen. Although I never had the opportunity to meet Mr. Nielsen, I believe that I share a connection with him. His belief that, "The challenge to philanthropy is ... to help generate some fresh ideas and to test some new methods that might provide for both equity and efficiency, humaneness and effectiveness in social programs," resonates deeply with me. Nielsen's words should inspire all of us who believe that a principal role of philanthropy and the nonprofit sector is to improve the lives of people.

It is fitting that Virginia Hodgkinson, the midwife to the modern nonprofit sector, and Pablo Eisenberg, the moral consciousness of the nonprofit sector, guide this lecture series honoring Nielsen's achievements. Virginia and Pablo have both made significant and lasting contributions to the development of our field and together represent a dynamic duo—the Superwoman who has done just about everything in studying and promoting the nonprofit sector and the Batman who is always willing to speak out against hypocrisy and social injustice within the nonprofit sector. I want to thank both of you for your uncompromising leadership and contributions to the sector as well as for your friendship.

Given Georgetown's religious origins, I feel compelled to begin my remarks by making a confession. I stand before you as a practitioner-scholar. I use the term practitioner-scholar to indicate my interest in using real life problems to shape and inform the research questions that are examined by scholars in real time. By real time, I mean that the research is started and completed while the people who are in need of the answers can still make use of the findings. This is not to suggest that there is no role for historical research or conceptual theory, but rather the practitioner in me appreciates the immediate relevance and applicability of policy research. As a result, my remarks today are likely

to be too results oriented for scholars, too scholarly for practitioners and probably too blunt for both groups. For this I apologize and ask for your indulgence.

I want to talk about three things this afternoon. First, I want to make the case for why I think there is a growing disconnect between the public's expectations for nonprofit organizations and the operational realities faced by nonprofit organizations. I believe that this disconnect is not just a problem of image but also a deeper problem of meaning and substance. Second, I want to provide some examples of how the disconnect between public expectations and nonprofit sector realities is starting to have dangerous consequences for our sector. By the nonprofit sector, I am referring to both nonprofit organizations and foundations. Finally, I want to offer a few suggestions about what the nonprofit sector can do to correct this problem before it is too late.

What Image Problem?

Much of what is believed about the nonprofit sector and how we operate can be traced back to the early observations of a visiting Frenchman, Alexis de Tocqueville, in his classic, *Democracy in America*. Tocqueville was interested in understanding the dynamics of America's new democracy. He was fascinated with the propensity of small groups of citizens to come together voluntarily to use their time and money to: 1) provide services for their fellow citizens and 2) peacefully challenge their government by using their guaranteed rights of free speech and the right of assembly.

Over the years, the nonprofit sector has romanticized Tocqueville's observations to present a modern day image of our sector as being comprised of relatively small, volunteer-driven organizations that largely rely on contributions of money, time and goods from individual contributors. It's not that Tocqueville's observations were wrong—it's that our sector has evolved and grown into something far different than what he saw and described during his year-long visit in 1831.

Today's image of the nonprofit sector as largely relying on volunteers or underpaid, hard-working professionals for whom compensation is neither required nor sought because of their unwavering commitment to a particular cause is increasingly untrue and problematic. Based on 1994 data from the Independent Sector, the nonprofit sector represents more than 1 million organizations with annual funds of \$568 billion and employs 9.7 million full- and part-time employees and 5.5 million volunteers as full-time employee equivalents.¹ These paid employees have every right to expect that they will be able to afford a decent place to live, have adequate health insurance and a comfortable retirement. Moreover, many nonprofit organizations are multi-million dollar institutions whose operations require a full-time, highly-trained staff.

Nonprofit hospitals, United Ways, international relief agencies, universities and foundations are among the many types of nonprofit organizations that require full-time employees with high levels of skill, talent and professionalism that cannot be reasonably expected of a part-time volunteer or from a poorly paid workforce. In addition, with the exception of foundations, all of the organizations just mentioned are likely to receive financial support from multiple sources, including: individuals, government contracts, foundation grants and fees for services. These staffing and funding realities mean that some of the largest and best-known nonprofit organizations do not operate in ways that fit the romantic image of the nonprofit sector that is ingrained in the public's consciousness.

Think about this for a moment. The image that the average citizen has of the nonprofit sector is likely to be inaccurate when applying his or her understanding to the largest nonprofit organizations that are the most well known. It's not that some nonprofit organizations don't use volunteers; it's that not all of them do and only a few them rely solely on volunteers. It's not that nonprofit organizations don't receive financial contributions from individuals; it's that many of them also receive substantial financial support from local, state and federal governments, corporations and foundations. It's not that there aren't small nonprofit organizations staffed by committed people who receive modest salaries; there also are large nonprofit institutions that must pay

talented professionals market rate salaries to ensure quality service. It's not that nonprofit organizations don't seek to make a profit when providing their services, it's that an increasing number of nonprofit organizations are making profits through successful for-profit ventures that provide revenue to subsidize their nonprofit activities.

In retrospect, it seems clear that the nonprofit sector always has had something of an identity crisis. Its very name is defined in terms of what it is not rather than what it is. To put it in marketing terms, the nonprofit sector's brand identity is at best confusing, and during times of intense public scrutiny, can reasonably lead the average citizen to believe that the nonprofit organization in question is acting in an inappropriate manner. While the nonprofit sector has matured and evolved over the years, the public's understanding of us has not. The result is often public disappointment, frustration and, occasionally, anger. The irony in this is that the nonprofit sector must shoulder much of the blame for this lack of clarity about who we are, how we operate and our real value to American society.

Unlike other sectors, the nonprofit sector has done little to help evolve the public's understanding of its operations and role in American society. By comparison, the average citizen can easily differentiate between the characteristics of a major corporation and a small business and what can be expected from each. Moreover, a scandal involving one company or small business seldom impugns the reputation of all for-profit companies, even those that mirror the offending organization in size, complexity and product distribution. The current Enron scandal may be the exception that proves the rule. By contrast, every issue or concern raised about any nonprofit organization seems to be used against all nonprofit organizations. Any breakage, spillage or theft that would be accepted as the normal cost of doing routine business for a for-profit or government agency is considered unacceptable for a nonprofit and proof of the entire sector's ineptitude.

In the last 22 years, the nonprofit sector has done a remarkable job of cataloguing both the variety of nonprofit organizations (the national taxonomy) and the universality of charitable giving and volunteering,

across ages, income levels and racial and ethnic groups. These were important contributions and necessary first steps. Unfortunately, this research, albeit unintentionally, helped to reinforce a romanticized view of nonprofit organizations. The effort to document the widespread support of nonprofit organizations through the voluntary contributions of time and money has led many to erroneously believe that such contributions are the only sources of support for nonprofit organizations.

What Substance Problem?

Compounding the nonprofit sector's image problem is an even larger challenge of meaning and substance. By substance, I mean the question of why the nonprofit sector does what it does. It is both ironic and profoundly disappointing that we have forgotten why Tocqueville was so fascinated with the nonprofit sector in the first place. He was interested in our sector's unique and active participation in the democratic process. While we have focused on Tocqueville's description of how we look, we have forgotten his intense fascination about who we are and what we do. At its core, the nonprofit sector is about the capacity of citizens to come together to improve the lives of people and to influence government at all levels to act in ways that support their views. As Tocqueville understood:

Governments, therefore, should not be the only active powers; associations ought, in democratic nations, to stand in lieu of those powerful private individuals whom the equality of conditions has swept away. As soon as several of the inhabitants of the United States have taken up an opinion or a feeling which they wish to promote in the world, they look out for mutual assistance; and as soon as they have found one another out, they combine. From that moment they are no longer isolated men, but a power seen from afar, whose actions serve for an example and whose language is listened to.²

The challenge for our various national and local membership organizations is that not all nonprofit organizations share the same

view on what government should do. It is this diversity of strongly held views engaged in active debate that preserves our democracy. By whatever name is used: the nonprofit sector, the independent sector, the third sector, the nongovernmental sector, the social sector or public benefit corporations, our sector is starting to lose touch with the American people. The fact that we can't agree on what to call ourselves underscores a larger problem that we aren't sure what we stand for and as a result no one else knows what we stand for. The questions that loom before us as a sector are: who are we and what do we stand for?

The nonprofit sector's inability to consistently and uniformly answer these questions is why I believe that we are increasingly failing the public's expectations about the larger meaning and substance of our work. Our lack of clarity is, in part, why for-profit entities see profit signs in doing charitable work. The most obvious example is the entry of financial institutions such as Fidelity and Vanguard into philanthropy by offering donor advised funds without any intention of meeting Nielsen's challenge "to test some new methods that might provide for both equity and efficiency, humaneness and effectiveness in social programs."

At their best, nonprofit organizations and the foundations that support them are social change agents. Our representative national and local nonprofit membership organizations must expand their horizons beyond their perennial focus on the narrow issues of greater tax deductibility for the charitable contributions of non-itemizers, the rollover of individual retirement accounts for charitable purposes or whether the excise tax for private foundations is decreased. These are important issues that should be addressed. However, efforts to prime the pump to create greater resources should not be confused as a substitute for sustained and meaningful discussions on how to bring about a more just society.

By almost exclusively pursuing issues of expanding the available charitable resources, the nonprofit sector is failing in its larger purpose to actively and energetically engage in the democratic process of setting social priorities and allocating resources. Rather than hiding out on the

great issues of our day - universal health insurance, persistent poverty, the lack of affordable housing and AIDS - the nonprofit sector should be at the forefront of these discussions. I applaud the Independent Sector's courage for taking on the estate tax issue and the Council on Foundations for creating the Ylvasaker award to encourage foundations to engage in public policy. What the nonprofit sector needs is for these efforts to become the norm rather than the exception and for foundations to fulfill their role of providing risk capital.

I recognize that these comments will strike some as controversial. They are not intended to be. They are based on my belief that while foundations and nonprofit organizations will disagree on strategies and approaches, as a sector, we are important actors in the civil discourse about how our government responds to social injustice and disadvantage at the national and local levels. For me, this is the higher purpose of nonprofit organizations within our society. Unfortunately, our sector's increasing timidity about actively engaging in the political process on social issues has begun to hurt us. Foundations are so unwilling to fund advocacy by nonprofit organizations that many have guidelines prohibiting such support. This trend has become so troubling that the Alliance for Justice and the Council on Foundations have been actively engaged in efforts to re-educate foundations about the ways they can legally and appropriately engage in public policy.³

More disturbing is that in recent years; several congressional leaders have introduced bills that would have severely curtailed the ability of nonprofit organizations and foundations to actively participate in the democratic process under the mistaken view that they have no legitimate role in the public policy decision-making process. Such legislation, if passed, would have enormous negative consequences for our democracy.

Ideally, the public should view the nonprofit sector as the place where people gather to actively promote their views of improving the quality of life for all. In this context, foundations provide nonprofit organizations with the investment capital, along with other sources of support, to carry out their activities. Certainly, nonprofit organizations

are more credible than either government or business in raising tough social issues and bringing citizens with opposing views together to articulate a common strategy. Who disagrees that it is the responsibility of every citizen to vote and that every valid vote should be counted? Who argues that every child shouldn't have access to health care or a quality education? What challenges our society is how to achieve these goals. The nonprofit sector should actively assert its important voice in shaping the answers to these questions.

And yet, our sector doesn't appear headed in this direction. We leave the most challenging and difficult questions of poverty and social justice to a precious handful of individual nonprofit organizations and foundations that have neither the collective clout, funding nor diversity of opinion to be effective in helping to shape public opinion and fashion a political compromise. Will this be a hard and difficult road? Will it require nonprofit organizations and foundations to accept that public criticism is a necessary and expected burden when trying to make a difference? Is it necessary that we undertake this journey without delay? Yes, yes and yes! We would do well to remember John Gardner's example, a giant in the nonprofit sector, who Pablo Eisenberg recently observed "did not shy away from causes in which he believed, however unpopular."⁴ What is at stake is nothing less than the soul of the nonprofit sector, the preservation of a well functioning democracy and the continuing opportunity to improve the lives of people.

Public Policy Consequences

The disconnect between public expectations and nonprofit sector realities around both image and substance has started to erode the public's confidence in our sector. I want to examine three cases in which the activities of nonprofit organizations created problems for them, in part, because they were not meeting public expectations. The examples are Minnesota Public Radio, the Allina Health Care system and the response of nonprofits to the September 11, 2001 terrorist attacks.

An ongoing reality for nonprofit organizations is the need to develop new sources of revenue. Foundation support is always short-lived and there are limits to relying on individual contributions to support a nonprofit organization's operations. To become more self-sufficient, many nonprofit organizations have developed for-profit subsidiaries to provide revenue for the nonprofit organization's operations. The case of Minnesota Public Radio (MPR) is instructive of how success in developing alternative funding sources can threaten a nonprofit's image with the general public. In 1981, MPR established Rivertown Trading Company after an estimated 20,000 listeners ordered Powdermilk Biscuits from an advertisement that aired on Garrison Keillor's Prairie Home Companion. In 1986, Rivertown Trading Company separated from MPR for the purpose of earning revenue to support the nonprofit through a catalogue business. It would grow to have 400 employees and 1,500 seasonal workers. In 1987, Greenspring Co. was established as the for-profit umbrella company for several subsidiary companies and, by 1998, was the nation's 50th largest catalogue company. Between 1987 and 1998, Greenspring Co. contributed about \$4 million per year to MPR, representing 17 percent of MPR's annual income of \$24 million.

The president and vice president of MPR also served as president and vice president of Greenspring Co. While the compensation was disclosed for the nonprofit executives, it initially was not disclosed for the for-profit executives. The CEO received a nonprofit salary of \$69,200 and the subsequently disclosed for-profit salary was \$429,155. Between 1997 and 1998, Minnesota's attorney general investigated the compensation structures of MPR and Greenspring Co. and found no wrongdoing.⁵

In March 1998, Rivertown Trading was sold to the Dayton Hudson Co. (Target Corporation) for \$120 million. The CEO received \$2.6 million; the vice president \$1.4 million and other for-profit employees received a total of \$7.3 million. A total of \$90 million was added to MPR's endowment. The remaining money, after paying \$10 million in outstanding obligations, was used by the parent for-profit company.⁶

Rather than cheers that MPR had become more self-sufficient, MPR encountered a public relations nightmare because they were not behaving how Minnesotans perceived a nonprofit should act. MPR was criticized because its executives received compensation (as is typical in for-profit transactions) as a result of the sale and because all of the proceeds from the sale did not go to MPR. As nonprofit organizations seek to develop revenues from for-profit ventures to subsidize their activities, it is essential that the public understand the appropriateness of such activities and that state attorney generals charged with oversight help to clarify rather than to obscure which laws apply.

Until a year ago, the Allina Health system in Minnesota was a \$2.6 billion nonprofit conglomerate consisting of over 19 hospitals, 48 clinics, 4 nursing homes and also operated imaging, ambulatory, surgery, mental health and transportation systems. Minnesota's attorney general undertook a review of Allina activities to determine if the company was in compliance with Minnesota's laws for nonprofit organizations regarding conflicts of interest between subsidiaries, executive compensation, consulting expenses, travel, entertainment and administrative expenses. Specifically, Minnesota law prohibits nonprofit organizations from providing private gain to individuals.

The attorney general's report found that Allina essentially operated as a for-profit business although it was organized as a nonprofit.⁷ The report details excessive executive compensation, tens of millions of dollars per year in consulting expenses, tens of millions of dollars per year in lavish travel and entertainment for executives and their families and well above average administrative expenses. Without ever alleging that Allina had engaged in any wrongdoing, the attorney general was able to secure an agreement with Allina that forced it into two separate entities, required the resignation of its board and allowed the attorney general to select the board of trustees for the two new entities. The attorney general was successful in making the public case that Allina was a nonprofit organization that had forgotten what it meant to be a nonprofit organization.

The United States was forever changed on September 11, 2001. What we didn't know as we watched the World Trade Centers' Towers collapse, the Pentagon burn and airplane wreckage in Pennsylvania was that the events that would follow would result in a loss of public confidence in the nonprofit sector. The loss in public confidence is due, in part, to concerns raised about the legitimacy of overhead expenses, executive compensation and organizational efficiency in the distribution of resources, each of which can be traced back to romanticized views about the nonprofit sector. These concerns, which led to Congressional hearings, stem from the disconnect between the public's belief about how nonprofit organizations should operate and the reality of how nonprofit organizations actually operate. It must be noted that the events of September 11th were unprecedented and my comments are intended to help us reflect on the lessons learned from this experience.

Almost from the beginning, the media and the public began the drumbeat about whether all monies donated would reach the individuals affected by the attack. The idea that there would be no legitimate overhead expenses in staffing, coordinating, monitoring and disbursing monies in connection to the September 11th attacks was absurd. And yet, faced with the enormous pressure of public expectations, many of the nonprofit organizations directly involved in the relief efforts felt obliged to say that every dollar contributed would go to victims of the attack. This required many of the nonprofit organizations, for example the September 11th Fund, to separately fundraise to cover legitimate and appropriate overhead expenses. In testimony before the Subcommittee on Oversight of the House Committee on Ways and Means, Joshua Gotbaum, CEO of the September 11th Fund, stated, "... every dollar raised by the September 11th Fund goes directly to grants to meet the needs of victims, their families and affected communities. We have raised all of the Fund's administrative costs separately."⁸ Rather than taking advantage of a teachable moment, we reinforced the public's misunderstanding that nonprofit activity doesn't cost anything and can be carried out for free.

It should have been expected that the media and the public would be interested in the compensation of nonprofit executives. After all, we have created the expectation that nonprofit executives should volunteer their time rather than receive compensation commensurate with their talent and skills. However, it was surprising that even the hero of New York, the now knighted former mayor Rudolf Giuliani, has come under criticism for the salaries that will be paid to employees of the Twin Towers Fund.

The Twin Towers Fund was established by Giuliani to help the families of rescue workers, especially police officers and firefighters, who died in the World Trade Center attacks. Notwithstanding that Fund officials took the pledge that all overhead expenses would be raised separately and that overhead administrative expenses are projected to be less than 1 percent, or \$2.25 million of the \$150 million that has been raised to date, the salaries are the target of continuing public criticism.⁹ In addition, representatives of some of the victims' families have objected to removing city oversight of the Fund to a private nonprofit charity over concerns about financial accountability.

Finally, there has been ongoing public criticism about the perceived lack of efficiency among the various relief agencies and emergency funds in assisting the victims of September 11th. Families of the victims have complained that it has been difficult for them to receive funds because of the lack of coordination among funding sources and the limited information of volunteers who are assisting them.

The Red Cross' Liberty Fund received substantial criticism for its decision, which it later reversed, to use \$264 million of the monies raised to create a permanent fund that could be used in the event of future terrorists acts. In testimony at the Congressional hearings, New York's attorney general threatened legal action against the Red Cross on the basis of consumer protection laws and charitable giving regulations if it did not expend all of its monies on the September 11th disaster. He went on to say that the Red Cross' actions amounted to a violation of the public trust. I would note that Minnesota's attorney general raised

similar questions in 1998 about monies raised by the Red Cross in connection with flood relief.¹⁰

The Red Cross also faced criticism about the blood donations collected from 50,000 people that had to be destroyed because they were not needed. These and other concerns led to the resignation of the Red Cross' president, Bernadine Healy. Some observers have suggested that no small part of Dr. Healy's problem was her effort "to run the Red Cross as a bottom-line business with donors reduced to consumers, Red Cross workers as middle managers and the attendant press to cover their triumphs."¹¹

These events presented another lost opportunity to teach the public that nonprofit organizations operate differently from government agencies. We do rely on volunteers, especially during emergencies. And, we do not have the existing infrastructure to easily coordinate services. The unfortunate part of all of this is that rather than viewing the nonprofit sector as heroes that were able to quickly mobilize during an unprecedented emergency, many Americans now have negative perceptions of the nonprofit sector's capabilities and intentions. It also does not help that several of the organizations that have assumed leadership in responding to the tragedy have publicly stated that they are no longer accepting contributions when there are still people in need as a result of the tragedy.¹²

Conclusion

The nonprofit sector is at a critical crossroads. We have an image problem that masks an even larger problem of purpose and meaning. Others are inaccurately defining us and, if this is not corrected, it will continue to undermine the public's trust and confidence in our sector and, possibly, the participatory nature of our democracy. What should we be doing?

- We need to acknowledge forthrightly the magnitude of the problem. Nonprofit and foundation membership organizations at both the national and local levels need to coordinate their efforts to present an accurate picture of the operational realities of the nonprofit sector.
- We need to respond quickly and aggressively to every media inaccuracy, misrepresentation or misunderstanding of the nonprofit sector, whenever it occurs.
- We need public policy research that underscores the variety and differences among nonprofit organizations so that we may forever debunk the one-size fits all romanticized view of the nonprofit sector that now exists.
- We need to actively engage with the state attorney generals about the changing nature of nonprofit organizations and what laws should apply to which activities.
- Most importantly, we must affirm, at every opportunity, that the larger purpose of nonprofit organizations and foundations is to be social change agents. We must balance narrow self-interest with the larger purpose of fulfilling the common good. This will be difficult, require us to take risks, and will not be universally accepted within or outside of the nonprofit sector.

We cannot allow the divide between public expectations and nonprofit sector realities to grow any larger. The time for the nonprofit sector to act is now.

Endnotes

¹ Alan J. Abramson and Lester M. Salamon, "The Federal Budget and the Nonprofit Sector: FY 1996 and FY 1997." A report prepared for Independent Sector (www.independentsector.org/programs/research/almanac_overview.html).

² Alexis De Tocqueville, Democracy In America (New York: Alfred A. Knopf, 1994, Volume II), p. 109.

³ See: B. Holly Schadler, The Connection: Strategies for Creating and Operating 501(c)(3)s, 501(c)(4)s, and PACs, The (Washington, DC: Alliance for Justice, 1998); Council on Foundations, Report of the Public Policy Task Force for the Council on Foundations, (Washington, DC: Council on Foundations, 1999).

⁴ Pablo Eisenberg, "Remembering John Gardner, an Idealist Who Knew How to Lead," The Chronicle of Philanthropy, March 7, 2002, p. 44.

⁵ Noel Holston, "MPR Executive Pay," Star Tribune, January 30, 1998.

⁶ Melissa Levy, "Dayton Hudson to Buy Rivertown Trading," Star Tribune, March 24, 1998.

⁷ Minnesota Attorney General's Compliance Review Audit Summary Allina/Medica, Minnesota State Attorney General's Office, Released September 24, 2001.

⁸ Statement of Joshua Gotbaum, Chief Executive Officer, September 11th Fund, New York, New York. Testimony Before the Subcommittee on Ways and Means. Hearing on Response by Charitable Organizations to the Recent Terrorist Attacks, November 8, 2001.

⁹ David Barton and David M. Herszenhorn, "Officer, Widows Oppose Control of Twin Towers Fund by Giuliani," New York Times, February 21, 2002 and David Barton and David M. Herszenhorn, "Giuliani to Give Money Quickly in Shift on Twin Towers Charity," New York Times, February 27, 2002.

¹⁰ Grant Williams, "Turmoil at the Red Cross," The Chronicle of Philanthropy, November 1, 2001, p. 71.

¹¹ "Who Brought Benadine Healy Down?," New York Times, Final, Section 6, p. 4, column 3, Letter to the Editor.

¹² Ian Wilhelm, "Half of \$2 Billion Raised for September 11 Given Away; Other Recovery Updates," The Chronicle of Philanthropy, March 7, 2002, p. 15.