

Merging Mission and Money: A Board Member's Guide to Social Entrepreneurship

By Jerr Boschee

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THE CHALLENGE

“Social workers ... are raised by experience and training to distrust money, business and capitalism. We develop a mind-set that views money as evil. Grow up.”

Jed Emerson (from The New Social Entrepreneurs)

“Too many nonprofit organizations are financially stagnant, raising and distributing funds the same way they have for decades A nonprofit that is run for profit sounds like a contradiction in terms. But it doesn't have to be.

Bill Shore (from Revolution of the Heart)

The nonprofit sector today is peopled by millions of talented, compassionate men and women dedicating their lives to helping others. One of every seven American workers is employed by the sector.

During the past 30 years, as social problems exploded, these men and women have been heroes. They've met one challenge after another, soldiers in a trench warfare unseen by most of their fellow citizens. They are the living embodiment of a precious American value -- helping your neighbor when he or she can no longer make it alone.

But the nonprofit sector is in trouble.

The sector has been bludgeoned repeatedly for nearly two decades, and the pressures on nonprofits today are daunting:

- **Continuing cuts in public sector support.** Government spending on social services and the arts is plummeting, at every level -- state and federal funding collapsed by a total of 23 percent during the 1980s -- and we're in the midst of another wave of reductions today.

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- **Fluctuations in individual and corporate giving.** Individual giving sank by nearly 20 percent during the first two years of this decade and has not yet rallied completely. Wealthy Americans are now giving only four percent of their annual income to charity compared to seven percent during the 1980s. Corporate philanthropy has increasingly been replaced by cause-related marketing and has diminished substantially since its high-water mark in the early 1980s.
- **More nonprofits competing for available funds.** At the same time, the number of nonprofits has exploded. For every three that existed just seven years ago, there are four today, and they are all gathering at the same watering hole.
- **Many more people in need.** As recently as 15 years ago, few nonprofits were dealing with such problems as AIDS, homelessness or crack babies. Today, Catholic Charities is serving four times as many people as it did a decade ago, millions of people are losing their welfare benefits, the population of frail elderly people continues to mushroom, funding for the National Endowment for the Arts is constantly in jeopardy, and so on.
- **Pressure from funders and others to merge or downsize.** One Foundation executive told me recently, "there're just too damn many nonprofits out there, and they're tripping over each other," and he's not alone. In addition, there are increasing demands for accountability, marketplace realities such as managed care, and other forms of institutional stress such as rising costs, depleted reserves and staff burnout.

And repeated blows to the reputation of the sector. From the Aramony scandal of 1990 to the New Era ponzi scheme of 1995, nonprofits have suffered by association. Recent Gallup polls reveal that *one in three Americans believe the nonprofit sector should be eliminated* because we are perceived as unethical, inefficient, and ineffective.

This is not the world in which most of us grew up. This is not the nonprofit world of the 1950s or even the 1980s. But it *is* the world in which we are living, and it poses a daunting challenge for nonprofit boards of directors.

THE PIONEERS

The nonprofit sector has been mugged by reality. Volunteers and staff members have taken yeoman strides to meet the challenge, but they're continuing to fall further and further behind. The very survival of many social service, arts and other nonprofit organizations is at stake.

But nonprofits *must* survive and continue to serve, and in recent years organizations across the country have begun responding to the challenge in a new way. What we are beginning to see is a tectonic shift in the culture of the nonprofit sector, in the way it behaves, in the way it thinks about itself, and in the way it is funded. The shift is shattering old definitions, uprooting careers, and changing the very nature of the job.

And the movement is being led by a new type of social servant, a growing body of pioneers who are telling us to shed the old definitions and to take responsibility for our own survival -- to stop depending so heavily on contributions and government support.

These men and women are social entrepreneurs, and they are changing the face of the nonprofit sector.

Simply put, "social entrepreneurs" are nonprofit executives who pay increasing attention to market forces *without* losing sight of their underlying missions, to somehow balance moral imperatives and the profit motives -- and that balancing act is the heart and soul of the movement.

Many are making it work. By adopting entrepreneurial strategies, they've been able

- To sort through everything they do from both mission *and* an earned-income perspective
- To expand their most effective and needed programs and to productively dispose of the others
- To start business ventures rooted in the core competencies of their organizations

- And to become increasingly self-sufficient financially and less dependent on government and charity

For example:

- **John DuRand** began working in the mid-1960s with seven people who were mentally retarded. By the time he retired during the winter of 1997, Minnesota Diversified Industries had become a \$57 million not-for-profit business employing more than 1,000 people.
- **Margaret Cossette** started in the mid-1970s with six part-time employees and a \$16,000 grant. Today, Missouri Home Care is a \$10 million for-profit business providing non-medical care to more than 2,500 elderly people in 39 rural counties.
- **Dr. Mimi Silbert** helped start Delancey Street Foundation with \$1,000 from a loan shark in the early 1970s. Today the Foundation operates nine profitable small businesses, employs only former convicts and drug addicts, and has returned more than 10,000 people to the mainstream.
- **Bill Kling**'s entrepreneurial adventure at Minnesota Public Radio started when Garrison Keillor off-handedly promised to send his listeners a calendar if they responded to an informal survey (at the time, no such calendar existed). Today the station operates a for-profit subsidiary that generates more than \$165 million in annual gross revenue.
- **Rick Surpin** and his colleagues started brainstorming ways to create jobs for African-American and Latino women in 1984. Today Cooperative Home Care Associates is a \$5 million business employing more than 300 women in the South Bronx alone, captured the National Business Enterprise Trust award in 1992, has been the subject of a case study at Harvard, has launched a for-profit subsidiary and has expanded into four other cities.

But it's not necessary to start a business venture in order to be successful as a social entrepreneur. Most entrepreneurial efforts start small -- and they are driven by a double bottom line, a mixture of both "mission" and "money."

THE "MISSION" GOALS

Social entrepreneurs have two "mission" goals: To sharpen their organizational focus and to expand their impact. When Jack Welch took over as CEO at General Electric in 1981, he asked Peter Drucker to tell him the single most important thing he could do to improve the company. The answer was simple: *If you're not the best or the second best supplier of a product or service, you should stop providing it!* In other words, *stop trying to be all things to all people.*

But that advice runs against the grain of the traditional nonprofit mentality. We see people in pain, we start a program. We see somebody else in pain, we start another program. Soon we're overwhelmed, and most nonprofit executives will admit that they're trying to do too many things for too many people. They're searching desperately for a way to focus, to identify their most effective and needed programs -- and to productively dispose of their more peripheral programs, either finding a home for them in other agencies, by allowing them to die a natural death, or by eliminating those that are wreaking financial havoc on the rest of the organization. Drucker calls it "organized abandonment," and it's the first and most important step toward sharpening an organization's focus. For example, Children's Home Society of Minnesota eliminated three of its seven divisions and within a single year had opened four new facilities, acquired part of another agency and raised its operating budget by 17 per cent. More recently, Child Center of Our Lady, a St. Louis nonprofit serving children with behavioral challenges, eliminated seven of its 15 programs and entirely changed its mission.

One important caveat: *Being a social entrepreneur does not mean eliminating a program just because it loses money.* If a nonprofit is the best or the only provider of a program that is critically needed, it has an obligation to continue the program -- and a managerial challenge to find other sources of revenue to cover the cost.

However, it makes no sense for five or six nonprofits in the same geographic area to deliver the same product or service. If one of your programs ranks third or lower, let it go! Hand it over to number one or number two and concentrate on the areas where *you* are the leader.

*Despite having fewer programs, successful social entrepreneurs are still able to **expand** their impact — the second mission goal.* Because they are able to concentrate more of their resources on fewer programs, they have more time to develop positioning strategies and marketing plans that work and are able to selectively add new programs to meet the emerging needs of their communities.

THE “MONEY” GOALS

Despite the importance of mission goals, however, most people who think about entrepreneurship in the nonprofit sector think first about financial returns. This is understandable. According to INDEPENDENT SECTOR, the average nonprofit in 1977 had more than three months of operating capital in reserve at any given time: By 1989 the average reserve had diminished to less than four days. Recent INDEPENDENT SECTOR studies have also revealed that the average nonprofit nationwide still produces less than 15 percent of its revenue from earned income.

Nonprofits can generate earned income either from their current programs or from entirely new activities, some of which would then be structured as programs and others as business ventures. In either case, *the primary goal is to become increasingly self-sufficient financially* and less dependent on government subsidies and charity. But the concept of "earned income" is a confusing one to many people in the nonprofit sector, and it's important to emphasize a few key points before describing the levels of self-sufficiency that might be possible.

Simply put, *earned income implies a quid pro quo arrangement in which there is a direct exchange of service or product for monetary value.* This definition includes such things as fee-for-service payments (either directly from clients or indirectly from a third party such as Medicaid or an insurance program), revenue from product sales, consulting contracts, tuition, rent or lease payments, and may also include traditional forms of revenue-generation from book publishing and conferences.

But the following types of revenue do not qualify as earned income: Undesignated, unrestricted, or general operating grants; contributions from individuals; bequests; sponsorship of special events; most types of cause-related marketing; and so on.

There are three types of increasingly ambitious financial goals that nonprofits can pursue if they adopt entrepreneurial strategies:

INCREMENTAL GAINS

(for individual programs or entire organizations)

This goal can be achieved by any nonprofit, and it can start to happen almost immediately: A reasonable three- to five-year objective would be to increase earned income by an amount equal to 15 percent of the organization's annual operating budget.

For example:

- **The Metropolitan Atlanta Council on Alcohol and Drugs (MACAD)** has gone from \$30,000 to \$300,000 per year in earned income, in part by capitalizing on the Internet. The organization provides information and referral services over the phone for people seeking a substance abuse treatment facility. Initially available only in a binder, the information was later computerized for internal purposes and now is updated every week on the Internet, with MACAD selling access to its database to the courts for \$100,000 per year.
- **The Minnesota Orchestral Association** will soon be covering about ten percent of its annual operating costs from the profits generated by a single new business venture. The Orchestra considered more than 100 potential ideas before settling on one that would help it create a new generation of classical music lovers, an important part of its mission. The new business is based on

the concept of a videotaped "story concert" that combines well-known children's books with animation and original orchestral music. The videos are aimed at eight- to ten-year old children, and the first received the American Library Association's Andrew Carnegie Medal for Excellence in Children's Video, which is given to only one children's video in the country each year.

SELF-SUFFICIENCY

(for specific programs or business ventures and, on rare occasions, for entire organizations)

This goal can be achieved by some nonprofits, but it will usually take a considerable period of time.

For example:

- **The Kansas City chapter of the American Red Cross** discovered during the mid-1980s that fewer and fewer people were coming to its walk-in service centers because they were located in older parts of town (only about 200 people a month were visiting each center). In order to reverse that trend, the chapter decided to reposition itself by opening a retail store that would sell safety equipment in a perimeter shopping mall and to locate a service center immediately next door. The intent was to break even with the store and to generate foot traffic for the center. Within five years the chapter had three successful stores and the average foot traffic at each of the adjoining centers was 2,700 people per month.
- Among many other programs, the **Bidwell Vocational Training School** in Pittsburgh trains welfare recipients, unemployed steelworkers and inner-city teenagers to become chefs. Their reputation grew during the early 1990s when students started providing catering services to individuals and organizations on an informal basis. Eventually, the organization realized it had a business opportunity and started a separate venture that today generates more than \$3 million in annual gross revenue and handles culinary contracts at the airport, the science center and other locations around the city.
- When Charlie Graham arrived at **St. Vincent de Paul Rehabilitation Center** in Portland, Ore., in 1985, it was a \$1 million sheltered workshop that was 80 percent subsidized. When he left in 1995 it was a \$10 million affirmative business that was 90 percent self-sufficient. Graham triggered the transformation by immediately changing the mission of the organization and then doing something nonprofits rarely do: He bought an existing, for-profit company and hired the previous owners to train his employees.

SIGNIFICANT PROFITABILITY AND GROWTH

(for spin-off business ventures or entire organizations)

This goal can be achieved only by a very few nonprofits, and it will usually take them a very long time.

For example:

- **Housing Works** is a New York city nonprofit providing housing, advocacy and supportive services for homeless people living with AIDS and HIV. Seven years ago, as the AIDS industry began to emerge, Housing Works committed itself to providing jobs for its clients. Today the organization operates three upscale thrift shops, a used book café, and a dollar store. Annual revenues are about \$5 million, with a profit margin of 30 percent (the \$1.5 million in profit covers about 12 percent of the parent organization's annual budget).
- When Gary Mulhair became President of **Pioneer Human Services** in 1984, the Seattle nonprofit had a heavily subsidized budget of approximately \$4 million. Today it's a profitable, \$30 million organization providing transitional and long-term housing, job training, and employment for people who have been in prison or in alcohol and drug treatment programs. Most of the 3,000 to 4,500 clients served each year work for one of Pioneer's many businesses, which include a light-metal fabrication facility, a wholesale food business serving nearly 400 food banks in 20 states, a corporate cafeteria for the Starbucks Company, an institutional food business preparing about 1,000 meals a day, a property management company, a hotel in downtown Seattle, and a number of others.

- The mission of New Jersey's largest community development and nonprofit housing corporation is to provide services for Newark residents and to create employment by placing city residents into jobs that deliver those services. **New Community Corporation** has been around for 25 years and today runs a nursing home that employs 240 people, a day care center that employs another 240 and a home health care program that provides jobs for 160. The organization also operates a number of retail stores and has become involved in banking, real estate management, institutional food services, comprehensive job-training, shopping center management, and a fine-dining restaurant. All told, New Community employs about 1,500 people, has its own credit union and business loan fund, and is generating more than \$25 million in revenue each year.
- **Vitas Health Care Corp.** began providing hospice care to a single individual in the basement of a Miami church in the mid-1970s. Today it's a \$150 million a year business that has already served more than 75,000 people in nine states.

POTENTIAL PITFALLS

The nonprofits most prepared for entrepreneurship today are those that have been the most innovative during the past 10 or 15 years. Their challenge is to make the transition from a culture of innovation to a culture of entrepreneurship, however, the journey can be fraught with dangers. In order to make sure the organization's expectations are realistic and their commitment sufficient, nonprofits should spend some time at the beginning of the process attempting to identify some areas that could cause difficulty in making this transition.

Consider the potential pitfalls. Each of these questions, and dozens of others like them, is legitimate and needs to be addressed:

Concerns about the concept of making money

- Does this smell like making money off the backs of the poor?
- What happens to quality when we start emphasizing the bottom line?
- Are we're setting up a two-tiered system that ignores the people who can't afford to pay?

Taxing already scarce resources

- We're already running at more than full speed. How can we possibly find time to do this?
- Do we have the right people?
- Do we have any spare cash?

The "resource" question becomes an insurmountable stumbling block for many nonprofits, yet we have learned that when a nonprofit really wants to do something, it manages to find the people, the time, the money, and the energy it needs

The fear of failure

- How can we avert a financial disaster?
- Will this damage our reputation?
- Can we do this without depleting our energy and resources?

The possibility of failure is very real. Personal careers can crash and burn. There are no guarantees.

What happens if we are successful?

- Will we lose our hearts when we find our wallets? (*all the people who came to do good and stayed to do well!*)
- How can we protect our nonprofit status?
- Can we manage such rapid growth?

And what happens once you succeed? Simple. Somebody raises the bar.

CRITICAL SUCCESS FACTORS

In spite of these valid concerns, more and more nonprofit leaders are becoming social entrepreneurs, either by adopting internal earned income strategies (designed primarily to cover more of an organization's costs, not necessarily to turn a profit) or by creating social purpose business ventures (whose primary purpose is to make a profit).

Here are a number of factors critical to success:

1) Candor

The first raw material for social entrepreneurs is candor, and it's probably the toughest thing for any entrepreneur. Starting a new venture, or even an earned income strategy, is difficult enough therefore you must be honest about your product or service, your market, your competition, your resources, and numerous other factors that help determine success or failure. The mantra here is very simple: "Beware of yourself!"

2) Passion

Please, do not attempt to become a social entrepreneur because you think you "should" do it, or because your funders tell you to do it. Unless you are ignited by the prospect, unless it drives you out of bed in the morning and sends you charging into the day, it's not for your organization. That doesn't mean your organization cannot begin adopting entrepreneurial strategies, but the person charged with carrying out any entrepreneurial activity must be passionate about the proposition.

3) Clarity of purpose

The third raw material is clarity, and it has two components. First, why is your organization heading down this path at all? What are the driving forces behind this shift in direction? It's important that the members of your entrepreneurial team come to a consensus on this issue before they start the planning process because you will be intensely scrutinized once you begin and you will need to have a consistent, compelling answer ready for your critics (and there will be critics!). Here are four good rationales:

- *Mission:* We're doing this because it will enable us to serve more people
- *Survival:* We're doing this because our more traditional sources of funding are drying up
- *Opportunity:* We're doing this because the market is beckoning
— we're already experiencing a demand for our service
- *Freedom:* If we can generate more of our own money,
we won't be so tied to the priorities and restrictions imposed on us by others

Those four words—mission, survival, opportunity and freedom—became the rallying cry for the entire effort and a major reason for the organization's success.

But there's another aspect of clarity that's equally important, even though it forces you onto treacherous soil, and that's the answer to the following question: "What will success look like?" It's important to define some long-term goals before you begin: If you don't, you will never be able to demonstrate your success to anybody (including yourselves) and you will be vulnerable to false prophets along the way.

4) Commitment

The fourth raw material is commitment, because the typical nonprofit is plagued by crises. Unless the board *and* the staff declares that entrepreneurial planning is a priority, it will be swept aside by the flood of day-to-

day demands. Unfortunately, too many boards are reluctant to commit because they are either risk-averse or searching for a quick fix. Both attitudes are understandable, but they conflict with marketplace realities.

The fact is, some earned income strategies will fail. Unless the board is willing to accept that fact and take some chances, it should not proceed at all! And the board must also be willing to take a longer view: Too many board members still think in terms of "cost" rather than "investment," and they're reluctant to proceed unless they can see a rapid return. Entrepreneurship doesn't work that way. It takes time.

5) Courage

Becoming a social entrepreneur takes courage, both personal and institutional. Above all, it takes the courage to change, because every nonprofit has an organizational "culture" that gets in the way. That culture exists whether we are aware of it or not. It's a collection of shared values that tell us who we are, what we stand for, how we should treat our clients, and so on. These values are rarely spoken aloud but are self-evident to new employees who pick them up by osmosis within a few days or weeks.

Culture eats change for breakfast. Perhaps the single greatest obstacle for nonprofits attempting to adopt entrepreneurial strategies is the traditional nonprofit mentality, a mindset that not only says we should be all things to all people but simultaneously insists that "we're not supposed to make money!" This deeply ingrained mentality views philanthropy as the bedrock of the organization, but social entrepreneurs reject that concept out of hand: To them, earned income is the primary financing strategy, not philanthropy.

What's happening here is "paradigm paralysis," a phrase coined by corporate trainer Joel Barker. As Barker points out, paradigms can be useful tools. They give us a way to make sense of the world, to establish a set of rules and regulations, and to organize and interpret incoming data. But they can be a double-edged sword. Blinders are slapped into place and we begin to interpret the new information according to our pre-conceptions. We become frozen. Change becomes our enemy.

Institutional paralysis can be overcome, with a sufficient dose of courage. But occasionally it takes something dramatic. A few years ago, when the board of directors of a nonprofit in Louisville, Ky. offered its leading candidate the job as CEO, he realized the existing make-up of the board worked against entrepreneurship and he agreed to accept the position only if every member of the board resigned. They agreed.

Still another CEO, who ran a sheltered workshop, decided to change the basic values of his organization. He invited his 11 senior managers to a downtown hotel where he wined and dined them, asked them to sit down—and then fired them all. Five minutes later he passed out application forms. "Starting tomorrow," he said, "we are no longer a rehab agency, we're a business. Starting tomorrow, we no longer have clients, we have employees. And starting tomorrow, you are no longer clinicians, you are business managers. If you can get your minds and hearts and souls around that concept, I want you back. If you can't, I'll help you find a job somewhere else."

Nine of the 11 returned to their jobs. Two could not accept the philosophic shift. But, from that day, the culture of the organization changed and the primary goal became the operation of a viable business.

In sum, changing the culture of an organization is no easy task. As board members, you need to ask yourselves: Are you capable of making tough decisions? Are you willing to take some risks? And are you ready to take the heat? If you suspect that either you or the organization will waffle, wait until you are completely ready. Work on the areas of softness before you proceed.

6) Core values

The sixth raw material addresses the key question "Is it possible to balance mission and money?" The answer is to help the organization identify a set of four or five core values that is clearly articulated, institutionalized, and constantly reinforced.

Starting down the path of entrepreneurship means you will be tempted by things you've never been tempted by before, and you'll need an internal sense of balance to help you resist them. Some social entrepreneurs are not able to resist temptation. Just watch "60 Minutes" for a month and you'll see investigative reporters rip into social entrepreneurs with the same zeal they normally reserve for corporate raiders.

Identify your core values before you begin. Make sure they can be quantified. Build them into your strategic plans and your annual operating plans and monitor them religiously. Measure your progress at least once a year, and trumpet them loudly.

7) Customer focus

One of the most difficult shifts in perspective required of any nonprofit adopting entrepreneurial strategies is to understand your audience.

When I worked as an executive for a Fortune 100 company, it took me at least five years to fully internalize the difference between "market push" and "market pull." If you start with your products and services, then go out in search of a buyer, you're trying to *push* your way into the market. But if you start with the people you are serving, find out what they need, then build those products and services, they will be *pulling* you into the market. And here's the good news: As soon as you find yourself trying to convince yourself or anybody else that one of your ideas for earned income or for a business venture is a good idea—it's not. Good ideas pull you *toward* them.

Unfortunately, most nonprofit executives have as tough a time trying to internalize the difference between market push and market pull. No matter how many times nonprofit executives claim to "get it," they are found frequently talking about "*our* programs, *our* plan, *our* staff, *our* needs, *our* board." Too many are guilty of starting with organizational needs rather than the needs of the marketplace.

8) A willingness to plan

John Wooden, who led his UCLA basketball team to ten national championships, once said that "failing to prepare is preparing to fail," thus, the eighth raw material is a willingness to plan. According to the Small Business Administration, 90 percent of business failures are caused by management mistakes, not by competitors, changes in the market or other external factors.

The planning process for an earned income effort is straightforward and based on common sense. Unfortunately, many people in the nonprofit sector are impatient and are tempted to skip steps. Don't. The stakes are too high.

One of the most important aspects of planning, of course, is getting off on the right foot. Here are three suggestions to help you do so:

- *Ask for help*

Be sure your planning team includes some "business mentors," proven entrepreneurs who have successfully built their own small or medium-sized businesses. They'll provide a reality check that's invaluable. Bring in some "wild cards" as well, people who may not know much about your agency or even about business *per se*. Tell them their job is to ask all the "dumb" questions out loud, to probe the areas others might neglect because they're too close to the table. You might be surprised at what you learn.

- *Put somebody in charge*

Your team needs a leader, especially if you're embarking on a comprehensive entrepreneurial planning and marketing process. Don't expect one of your staff members to take on this task in addition to his or her regular job: A team leader for a typical planning process may have to devote as much as half of his or her time for a year or more. Without that type of focus, the process will drift.

- *Create a comfort zone*

Once you've recruited your team, take some time to make sure that everybody involved is comfortable with your strategic framework, and that they know and agree upon the answers to the following five questions:

What is our vision? (*How do we want the world to change?*)

What is our mission? (*What will we do to bring about that change?*)
What are the core values that guide us?
What forces are driving us to take part in this process?
What outcomes do we expect?

Most nonprofits find it worthwhile to spend one or two meetings at the beginning of the planning process clarifying the answers to these questions and are often surprised at what happens. The "mentors" and "wild cards" (and occasionally the insiders) challenge some of your most dearly-held assumptions and the answers begin to change.

9) Think like a business at all times

Over the years, social entrepreneurs have learned some harsh lessons about the market. Here are six that apply regardless of whether you are concentrating on your current programs or starting something new:

Find a niche: The market can be tumultuous and cruel. To succeed, you must have a sound business concept, regardless of whether you're enhancing an internal program or contemplating a spin-off business venture. In other words, you need a market *niche* — a product or service that works, somebody who wants it, and somebody who's willing and able to buy it.

In the nonprofit sector, of course, the last part is frequently the toughest, because the "client" and the "customer" are often two different parties. But, as Paul Hawken says in his book, *Growing a Business*, the goal of any entrepreneurial effort is to reduce your idea to its essence — and then continue reducing it until you find a space that is small enough for you to defend but large enough for you to make a profit.

Be a player or don't play at all: This one takes real courage, and it's best expressed in the advice Peter Drucker gave to Jack Welch. It's very difficult for nonprofits to eliminate programs, but the pain can often be mitigated by finding a home for them in another agency that's better positioned to provide the service. By doing so you will simultaneously be freeing yourself to concentrate on the programs where *you* are better positioned.

Price your products and services aggressively: Putting a price on what we do is another aspect of marketing that is equally difficult for people in the nonprofit sector to accept. Nonprofits have been trained over the years to rejoice if we can cover our costs much less show a modest profit. But neither of these approaches can help us fund the future or even our current overhead.

When setting pricing strategies, nonprofit managers need to think in terms of annual budgets, not just the costs associated with a specific project. For example, successful service companies in this country have a gross profit margin of 40 to 60 percent on everything they sell. They need that *gross* margin in order to finish the year with an over-all *net* margin of three to five percent (the definition of a successful service business). Net margin is the resulting profit of an organization after overhead, payroll, and other internal and external sales costs are deducted. In other words, if it costs one dollar to deliver a service, charge \$1.40 to \$1.60. Nonprofits need to adopt this strategy.

Some people call this approach "value" pricing. Of course, introducing the concept abruptly would come as a shock to most current payers. Nevertheless, any nonprofit hoping to become increasingly self-sufficient financially will have to consider this approach and, at the very least, begin raising its prices incrementally.

Stick to your knitting: During the late 1970s and early 1980s, a number of nonprofits across the country began to pursue unrelated business income in an attempt to offset the escalating cuts in federal and state funding. Most of the efforts failed because the nonprofits not only tried to start a business (which was foreign to most of them), but they were also trying to do it in an arena they knew nothing about.

Most of today's social entrepreneurs have therefore abandoned the unrelated business strategy and are concentrating instead on searching for earned income in their core programs. In other words, there's a direct relationship between mission and money. And there's an additional benefit as well: Many of the nonprofits that started unrelated businesses in the past were required to pay taxes, but the unrelated business income tax (UBIT) does not apply to business ventures tied directly to an organization's mission.

If nonprofits actually reach the stage of starting a social purpose business venture, it often takes one of two forms:

A *direct service business* that provides products or services to the organization's target population (for example, home care for the elderly)

Or an *affirmative business* that is created specifically to provide four things for the organization's target population: real jobs, competitive wages, career tracks, and ownership opportunities

Build the right team: If you do decide to start a spin-off business venture, it's essential that the leader of your team be a genuine entrepreneur. Over the years, however, it's become apparent to us that *there's a great difference between innovators, entrepreneurs, and professional managers*. Each of these is needed in the evolution of a program or an organization, but at different times, and rarely does an individual possess more than one of the three skills. Innovators develop and field-test prototypes. Entrepreneurs turn prototypes into businesses. And professional managers secure the future.

Even if you find the right person to lead your venture, he or she cannot do it alone. Four out of five small businesses in this country fail during the first three to five years. But six out of seven small businesses started by graduates of the Harvard Business School succeed. Why? Not because they're any smarter, but because they *understand* that they don't know anything! The first thing Harvard grads do is surround themselves with people who have expertise in their areas of weakness.

The Massachusetts Institute of Technology (MIT) did a study a few years ago tracking 814,000 small businesses through the first eight years of their existence. They found that the survival rate of companies that had at least four people in the brain trust at the beginning was substantially higher than those that had three or fewer. Of course, one of the four must be a proven entrepreneur, but too many entrepreneurs try to do everything themselves and that rarely works.

Be patient: Business ventures take time to mature, even if they start as internal programs. Here are two more findings from the MIT study:

- Very little growth occurs during the first six years
- The product or service provided by the business changes completely at least once during the first eight years

10) The separation strategy

Entrepreneurial business ventures have to move quickly, and they cannot do so if they're encumbered by bureaucracy. For that reason, any business started by a nonprofit should be kept as separate as possible from the parent organization. In Paul Firstenberg's book *Managing for Profit in the Nonprofit World*, he writes:

"The basic point . . . is that the creation of a successful profit-making component within a not-for-profit environment—the building of a culture-within-a-culture, so to speak—is a difficult business . . . The chances of successfully doing so will be enhanced if the (profit-making) component is, from the outset, clearly labeled as such, and its different objectives and need for a different operating style are recognized from the start . . . The greater the separation in terms of form, staffing, oversight, and location, the greater are the chances that the profit-making component will be able to function with the necessary clarity of purpose and operating style appropriate to its objectives."

Part of a workable separation strategy, of course, is a willingness to create an independent board of directors. The board should have no more than six or seven members, and most of them should be outsiders:

- Three or four should be proven entrepreneurs
- One should be a person who is in the business of starting businesses (*a seed capitalist or an attorney specializing in startups*)
- One should be the senior executive of your parent nonprofit (*to serve as the conscience of the new company, but not to become involved in operations*)

- One should be a champion from the parent board who is specifically charged with protecting the new venture from interference by either the parent board or staff

11) Do something

You will *never* have all the resources you need. It takes a genuine entrepreneur to get things set in forward motion. Timid entrepreneurs will wait until they have the "perfect" plan. But a "pretty good" plan executed with passion today will always defeat a "perfect" plan tomorrow (primarily because there's no such thing as a "perfect" plan!). Don't be afraid to make some mistakes. They help to work out the bugs.

12) Be flexible

The last raw material is the ability to improvise. There is no right way to proceed, and the laurels will go to the individuals and the organizations that learn how to adapt, quickly.

A FINAL WORD

Woody Allen penned something a few years ago that sometimes seems to mirror the Hobson's Choice confronting people in the nonprofit sector: "More than any other time in history," he wrote, "human beings face a crossroads. One path leads to despair and utter hopelessness . . . the other, to total extinction. Let us pray we have the wisdom to choose correctly."

This monograph has been an attempt to brighten the horizon, to encourage all of us to stop thinking small, to stop underestimating our staff members, our clients, and ourselves, and to stop dreaming limited dreams.

But it's important to close with one final warning: Don't start an entrepreneurial venture unless you are ready. Many nonprofits are ill-prepared to begin adopting entrepreneurial strategies. Their board members and senior executives are increasingly aware that something has to change, but many of them lack the courage, the savvy and the staying power required to do so. Before you begin, therefore, it's important to ask yourselves these questions:

- Is this something we *really* want to do?
- Do we understand the risks and are we willing to take them?
- Are we being realistic about possible results?
- Is the timing right?
- Do we have the right people and are we willing to give them the freedom, responsibility, and authority necessary for entrepreneurial success?
- Do we have enough staying power (*dollars, time, psychic energy*)?
- Are we willing to make mistakes?
- Are we willing to actually eliminate programs?

Positive answers to these questions will not guarantee success, but they may give you the confidence to proceed. And if you awaken in the dead of night six months later aghast at what you've started, remember the three-word mantra pioneers such as John DuRand use to encourage newcomers to the field. It's a phrase that captures the underlying philosophy of social entrepreneurs, and you may want to try it yourself: "Profit . . . is . . . good!"