

CONNECT THE DOTS

A series of topical papers presented by the Omaha Community Foundation to begin a conversation on subjects that matter to our community

WHAT IS CAPACITY BUILDING?

Imagine you own a competitive business. For six years, you don't buy new computers or software. Your only salesperson leaves, and you decide not to hire another. You are the founder and CEO of the company and set up the board of directors with a group of friends and family who handed you the reins. But the market for your products and services is changing. The downturn in the economy has meant that many of your customers can't buy from you anymore. You are just barely making payroll each month. What can you do?

Now imagine you run a nonprofit organization. Same scenario. Both types of organizations are being buffeted by the same negative forces, so what can you do? The answers, of course, depend on the unique circumstances of your organization and the market it serves. On the simpler end of the spectrum, it may be that you'll need to invest in software to better track donors, or you might have to charge fees for services you once offered for free. At the more complicated end, it may mean negotiating a merger so that your organization's clients can be served by a larger, more unified nonprofit.

Making tough, strategic decisions about how to adapt to the internal and external changes affecting your organization is one of the keys to "capacity," defined as the infrastructure that your organization relies on to fulfill its mission. This infrastructure encompasses a wide range of capabilities, knowledge and resources — such as technology, board development, financial management and fundraising — all the things that strengthen your nonprofit's ability to have greater impact.

The cold reality is that in all nonprofits, capacity is either being continuously built or is remaining stagnant. The former is the model for continued success. The latter is the slow and painful death of a nonprofit, or what the Stanford Social Innovation Review calls "the nonprofit starvation cycle," wherein an organization barely hangs on for an extended period, then discovers it's too late to adjust.

In 2010, the Omaha Community Foundation (OCF) launched a "Nonprofit Capacity Building Initiative" to address the all-too-common problem of the death spiral. As part of that, OCF has re-pointed its Fund for Omaha program toward "Greatest Need Grants," which allow applications for operational and capacity building applications as well as the traditionally funded project-oriented grants. Through these efforts, OCF leadership hopes that funders focus more on the critical elements — such as capacity building — that lead to organizational success.

The Omaha Community Foundation's Connect the Dots series serves to raise significant issues for our community and provoke discussion. This fourth report in the series is intended to educate donors and others about the importance of investing in nonprofit capacity building. We hope that funders will keep this infrastructure question in mind as they make contribution decisions concerning the nonprofits they support, just as they would invest in their own businesses.



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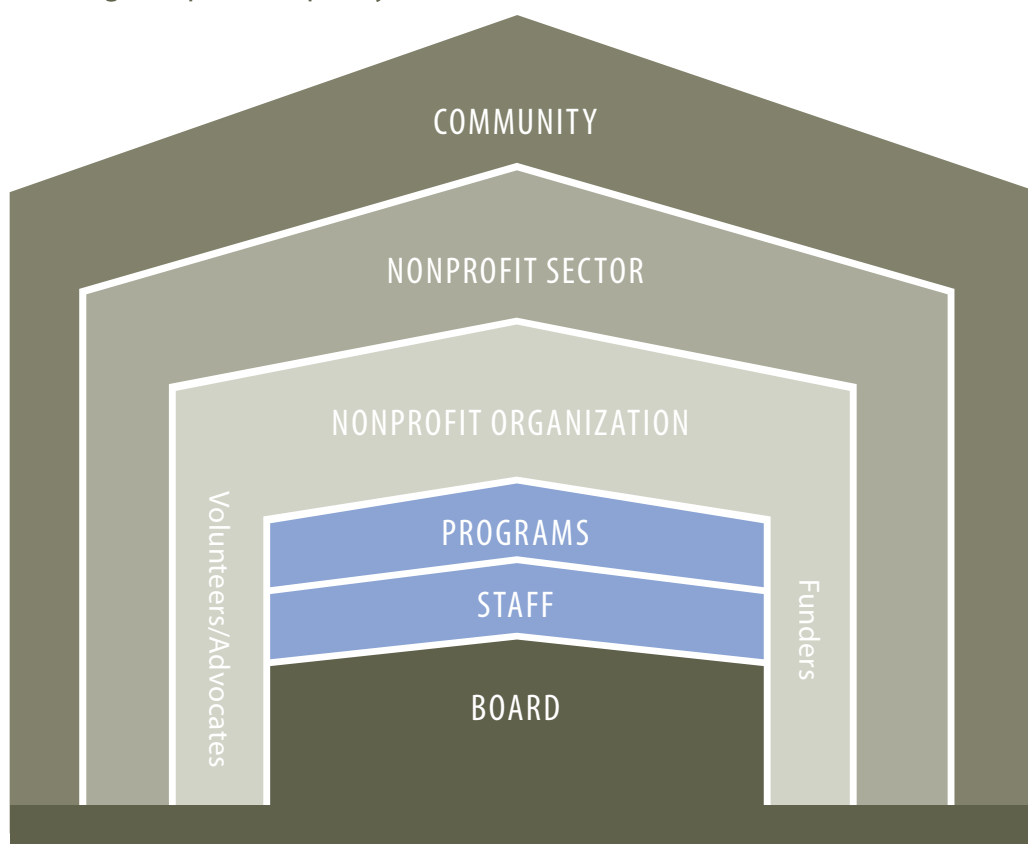
Let good grow.

WHY CAPACITY BUILDING?

Strengthening nonprofits ultimately strengthens the whole community. Simply put, a good nonprofit organization has a strong board that hires capable staff that runs quality programs. The board and staff ensure that capacity is constantly being built and is

never stagnant. This solid and growing organization is supported by donors and volunteers. A community will be more prosperous and peaceful when its nonprofit sector is made up mostly of these kinds of mature groups.

Model for Strong Nonprofit Capacity



In breaking down capacity building, four basic types of capacities are discussed in a recent James Irvine Foundation report. While the four overlap, they can be distinguished in the following way to better understand what determines the effectiveness of a nonprofit organization.

- **Leadership Capacity**—the ability of an organization’s leaders to inspire, innovate and decide direction to best achieve its mission. This includes creating a vision, prioritizing the work flow and making correct decisions.
- **Adaptive Capacity**—the ability to assess and respond to changes both external and internal to the organization. This includes evaluation, planning and collaborating.

- **Management Capacity**—the ability to effectively and efficiently use organizational resources to carry out the functions of a nonprofit. This includes hiring, firing, policy setting and budgeting.
- **Technical Capacity**—the ability to deliver programs, products and services. This includes program oversight, technology, fundraising, facilities maintenance and legal compliance.

Each of the four is important, and all must be in place for an organization to achieve its mission. When donors decide where to give, they should have in mind which capacity area they are investing in. Philanthropy, at its best, involves informed donors making sound strategic choices about where to invest their charitable dollars.

WHAT IS THE DEMAND AND SUPPLY FOR CAPACITY BUILDING?

The demand for capacity building is the need that nonprofits identify for strengthening their infrastructure to better achieve their mission. This demand comes to OCF from a variety of sources. Nonprofits often tell OCF they need capacity building, but more often they tell us, "We need more money." But in probing deeper, we ask, "How will more money help you better achieve your mission?"

Through the Capacity Building Initiative, OCF is discovering, and beginning to meet, the demand. Its goal is to create a comprehensive and coordinated system for building capacity that strengthens the region's entire nonprofit sector. The initiative has three phases:

Phase 1

Ten nonprofits in the Omaha-Council Bluffs region were selected, and each received a grant of \$5,000 to work on capacity. Their activities include:

- **Self-assessment and Consulting.** Their boards and staff have identified and then prioritized their capacity needs. Consultants helped nonprofits meet those needs.
- **Peer Learning.** Executive Directors of the 10 participating organizations meet monthly to share with colleagues the challenges they face and how to address them.
- **Executive Coaching.** Each Executive Director had access to personal coaching on leadership skills.



Each group starts with a survey that the board of directors and management staff fill out. This is followed by a facilitated discussion among board and staff to determine where they agree and disagree on the strengths and weaknesses of the organization. They then come to consensus on the top priority needs. In this group of 10, OCF has seen the following themes emerge as top demands for capacity: (1) Fundraising; (2) Human Resources; (3) Board Development; and, to a lesser extent, (4) Technology and (5) Facilities.

Phase 2

OCF will create ongoing opportunities for groups of 10 to continue learning and select a new group annually.

Phase 3

OCF will implement a coordinated and integrated system for capacity building. This may include forming an advisory group, performing a community inventory in which we map the field of capacity building providers in the region and convene those providers in order to design a more integrated system, with special attention to filling the gaps between supply and demand.



WHAT IS THE DEMAND AND SUPPLY FOR CAPACITY BUILDING? CONT.

To determine the demands for capacity in a larger sample than our group of 10, we commissioned a survey by the University of Nebraska at Omaha’s Center for Organizational Research and Evaluation (CORE). The survey was sent to 454 nonprofit Executive Directors in the region, and 47 completed them, a 10.4 percent response rate. The top responses to the questions about which areas of capacity were most important and posed the greatest challenge to mission fulfillment were: (1) Fundraising and Resources; (2) Marketing and Outreach; (3) Board Governance and Internal Operations; (4) Information and Communication Technology; (5) Collaboration, Networking and Advocacy; (6) Human Resources; and (7) Planning and Programming.

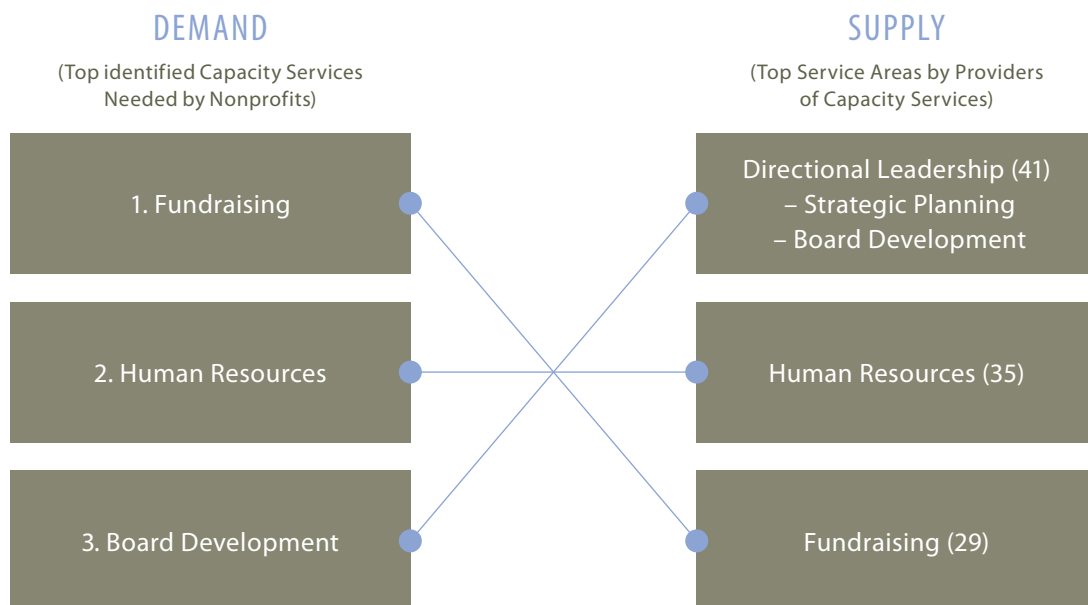
The CORE study also asked for estimates of the “cost to remove major organizational capacity barriers.” The 47 responders put numbers to their greatest needs. Taking the top three demands identified by the OCF’s Initiative 10 nonprofits, which also fell among the top demands identified by the CORE study, we can make some educated estimates of what it might cost per nonprofit to meet the demands:

1. Fundraising = \$20,050 per nonprofit.
2. Human Resources = \$28,300 per nonprofit.
3. Board Development = \$9,600 per nonprofit.

TOTAL = \$57,950 per nonprofit to address the top three needs identified in the Nonprofit Capacity Building Initiative.

The supply side of the capacity building equation is what consultants, firms, volunteers, academic institutions or others provide to nonprofits to meet their demands. To get a better handle on what the supply of “capacity builders” in our region offers, OCF commissioned a study to map the field of capacity builders. We found that of the 135 capacity building providers in the region that were included, the largest number (41) were categorized as helping with directional leadership (strategic planning, board development, leadership training). The second largest category of providers (35) was human resources. And the third largest (29) was fundraising. In this initial research, the supply side seems to align quite well with the demand side. Ideally, all this capacity building will lead to greater effectiveness and efficiency.

The Demand and Supply of Nonprofit Capacity Building



In the group of 10 nonprofits, the above themes emerged as their top demands for capacity.

OCF commissioned a survey to study to map the field of capacity building services offered in our region. The above services had the most service providers.

HOW IS A NONPROFIT'S EFFECTIVENESS AND EFFICIENCY DETERMINED?

Assessment of a nonprofit's effectiveness is difficult. It's easy to count the number of people who walk through the door or the number of meals served, but it is difficult to determine how effectively the underlying social problems are being solved. While some foundations apply basic formulas — the United Way will not fund an organization that spends more than 25 percent of its total budget on administration and fundraising — there is a wide variation in what nonprofits spend on programs and overhead. The Nonprofit Overhead Cost Study by the Center on Philanthropy at Indiana University and the Urban Institute found that overhead costs (payroll, rent, utilities, mailings, websites, etc.) typically account for 10 to 35 percent of a nonprofit's spending. Quantitative analyses are only as solid as the available data, and inaccurate reporting — unintentional or deliberate — can obscure an organization's financial picture. Sometimes, nonprofits "hide" some overhead costs so that funders don't view them negatively, especially donors who look at costs strictly.

Counter to widely held assumptions, case studies show that nonprofits that spend too little on capacity needs, such as fundraising, marketing and infrastructure, are less effective than those that spend more in accordance with their varying needs throughout their life cycles. For example, newer nonprofits may have greater expenses for startup operations and awareness-raising campaigns. For more established agencies, rolling out a capital campaign is more expensive than applying for a single grant, but promises security for the future. Given that nonprofits change over time, donors should not depend too heavily on the snapshot of any single year.

Other factors that contribute to a nonprofit's financial picture include location (rural areas may offer fewer amenities than urban areas); mission (organizations supporting unpopular causes may need to spend more to raise the same amount of money as those promoting more popular human needs); and industry (an all-volunteer telephone hotline has predictable expenses, while nonprofits that provide disaster relief can only estimate their yearly operating costs).



Developing a set of qualitative measures to complement quantitative formulas provides a more robust picture of nonprofit efficiency. There are no commonly accepted checklists, but considerations could include:

- Does this nonprofit have a good sense of its mission?
- Do all of its services, programs and products serve to fulfill that mission?
- Does this nonprofit address an unmet need in the community?
- Does this nonprofit duplicate services offered by others in the community?
- Does this nonprofit build local partnerships and networks to maximize resources?
- Does this nonprofit attract supportive board leadership?
- Does this nonprofit practice sound fiscal management?
- Does this nonprofit work to change systems to solve underlying problems or provide services for short-term relief from the symptoms?

While "efficiency" can be defined many ways depending on the type, age and industry of nonprofits, it is difficult to compare agencies. And yet, more donors are looking for the greatest impact for their dollars, taking a return-on-investment (ROI) approach to their philanthropic contributions. And the high ROI offered for capacity building may be the wisest investment a donor can make.

NEXT STEPS FOR DONORS

The first lesson from this exploration of capacity building is that donors who want to make the most impact from their giving should simply ask nonprofit leaders to honestly tell them their organizational needs. An unrestricted donation is always an extraordinarily appreciated gift. Rather than funding what you think a nonprofit needs, ask them, “What is your greatest need right now?” You may be surprised at what you hear.

Donors should also ask about efficiencies, but be open to unanticipated responses. While there is no one-size-fits-all answer to ensuring the efficiency of nonprofits, there are legitimate questions to ask, such as, “Are there other nonprofits with which you can collaborate

on back office or marketing or other operations in order to save on overhead?” and “Have you assembled a board of directors that can provide counsel in the key areas of your nonprofit, such as program development, fundraising, strategy and legal advice?”

A final lesson is that nonprofits need wise and generous donors, but they also need to find diversified revenue streams. Different nonprofits are going to have very different strategies for diversifying funding, but that is the point. Donors need to be aware of and engaged with the nonprofits they support in order to challenge them to best achieve their mission. That is, after all, what good investors do.



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