Deciding to Fund Nonprofits: Key Questions

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Everyone wants guidance when making tough funding decisions, especially when they involve often controversial, time-consuming, or passionate appeals from community-based nonprofit organizations. What community services do government officials want to support by funding nonprofits? How can government officials decide which nonprofits to fund? How can they determine the appropriate level of funding?

Unfortunately there is no one right answer or practice. The practice or the philosophy that works well in one jurisdiction may be ill suited to another. This article does not suggest a single solution, a one-size-fits-all for nonprofit funding. Instead, it describes six questions that local officials should consider in designing a funding process for nonprofits:

1. Why do we want to fund nonprofits?

2. Why do we want to have a formal process for making funding decisions?

3. How will we identify community needs that we want to help nonprofits address?

4. How will we obtain nonprofits' proposals for meeting community needs?

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In hard financial times, dividing up the funding pie wisely to meet community goals is all the more important.

MANAGING THE POLITICS OF FUNDING NONPROFITS

The county manager lives next door to the chair of the board of a local non-profit. The chair uses every casual interaction as an opportunity to advocate for first-time funding of the nonprofit. The manager feels pressured.

Elected officials vote against funding a particular nonprofit because it has not shown how or whether it achieved the expected outcomes. Its supporters have been expressing their dissatisfaction through telephone calls to staff and elected officials and letters to the editor of the local newspaper, insinuating that the nonprofit is being singled out for scrutiny because its service population is not a popular one. The media start getting interested.

As planned, government staff make recommendations for nonprofit funding on the basis of objective criteria. The manager agrees with every recommendation except one, related to a request from an agency with strong political support in the community. He instructs staff to allocate more money. Staff are frustrated by his instructions.

Will these kinds of scenarios continue to surface if a local government designs a funding process by answering the six questions proposed in this article? Probably. Nonprofit advocates still will request funding. A few nonprofits still might resist fulfilling expectations of accountability. Government officials still might want to alter the defined process in order to satisfy community leaders.

What *will* change, though, are the philosophies and the tools on which the staff and elected officials can rely in responding to the challenges presented in the scenarios.

In the first scenario, the manager can give his neighbor a document that explains the process for funding applications and the service goals that the county has defined. He then can invite the neighbor to submit an application on behalf of her nonprofit at the appropriate time.

In the second scenario, staff and elected officials can refer to documentation of the purchase-of-service agreement and explain how those expectations were jointly developed at the beginning of the funding relationship.

The third scenario might be the most challenging from the perspective of support staff. It points to the importance of obtaining commitment from stakeholders to uphold the process once designed. It also suggests that building in oversight by stakeholders can reinforce the integrity of decision making.

Individual internal or external stakeholders still might expect special treatment, even in a well-defined process, and there might be unusual situations in which making exceptions to the rules is in the best interests of the community. However, governments act as stewards of public funds most effectively when they have defined goals, processes, and oversight. Both the community and the nonprofits benefit when such safeguards are in place.

5. How will we review proposals?
6. How will we make funding decisions?

The first two questions encourage local governments to clarify their reasons for setting up a funding process. The next four questions provide a way to assess alternative decision-making processes.

Ideally, if a local government has the opportunity to design or redesign its funding process, it will consider these six questions sequentially. Avoiding or skipping a particular question may introduce confusion when the government tries to implement the process.

Two Preliminary Considerations

When people make plans, they sometimes overlook the following simple truth: they must know what they want to achieve in order to determine whether they have achieved it. The two questions that follow provide a framework for assessing whether local governments' funding decisions are achieving the desired results.

1. Why do we want to fund nonprofits?
North Carolina law provides that public funds be spent only for public purposes.[1] What public purposes do local officials want to serve through nonprofit organizations?

One possible reason for funding nonprofits is to provide general support for the work that nonprofits do to better the community. For example, a city may want to support assistance to homeless people by helping fund a homeless shelter or a community kitchen operated by a nonprofit. A county may want to encourage new employment opportunities by helping fund an economic development corporation or a Chamber of Commerce.

Rather than funding a broad range of valuable community services, elected officials may decide to tie their expenditures to programs that directly support a specific goal of their jurisdiction's strategic plan. For example, if economic development is a county's primary goal, its funding for nonprofits might focus on economic development, literacy, and subsidized child care to enhance the employability of area residents. If the county's priority is youth development, it might support nonprofits that provide after-school programs, tutoring, or recreation opportunities.

A second reason that local governments might fund nonprofits is to have them provide specific programs or services. Instead of building and staffing a swimming pool, a town might decide to partner with a nonprofit organization and help fund its capital or operating expenditures for the pool. Instead of operating an animal shelter, a town might contract with a nonprofit to operate the shelter.

Nonprofits may be better service providers than governments when they can

- supplement public funds with contributions of time, expertise, and money from volunteers and other donors.
- move more flexibly or quickly than government to address a pressing need.
- build a sense of community or encourage civic participation by involving volunteers, neighbors, or others who are known and trusted by a particular community.
- bring specialized expertise on community issues or on a specific

population because of their mission and experience.

- augment, complement, or fill in gaps in government services.

Governments can tie funding of nonprofits to general or specific public goals, but doing so requires that elected officials and government staff clarify their reasons for funding nonprofits. With such clarification, discussions about allocations can focus on larger community goals rather than on the circumstances of individual nonprofits or specific people (for illustrations of

politics that might intrude on the funding process, see the sidebar opposite). Explicit consideration of why local officials want to fund nonprofits can help them determine whether their reasons are sufficient for continuing that support.

Clarifying their reasons for funding nonprofits also changes how governments view nonprofits. They tend to stop viewing nonprofit funding as "charity" or "gifts" and start viewing it as a purchase of valuable community services and a partnership with other organizations serving citizens. Indepen-

dent of the decision-making process, a philosophical shift benefits the public by causing governments to develop purposeful alliances with nonprofits rather than maintaining a relationship of benevolence. (For a description of such an evolution in philosophy in Wake County, see the sidebar on this page.)

There are several reasons that a local government might not want to fund nonprofits.[2] Government officials might

- decide that the government can provide the same services better or at a lower cost than nonprofits.

- prefer to put resources into government departments, even if services are not as effective or efficient.

- not want to devote staff time and attention to oversight of partnerships with nonprofits.

- fear making nonprofits dependent on government funding.

- want to cut spending instead of providing the service.

Officials should examine each reason to determine if the assumptions on which it is based are correct. For example, officials might assume that funding a community service through government departments is more efficient than funding nonprofits to produce the service. However, a nonprofit might deliver the same services for less than government by using volunteers and supplemental grant money from outside sources.

In addition, avoiding the funding of community services through nonprofits simply because it "never has been done that way" ignores a growing national trend that encourages community problem-solving and broad collaboration among governments, nonprofits, the faith community, and the private sector. Most North Carolina local governments do, in fact, fund nonprofits to some degree. A 1999 survey by the Institute of Government found local governments to be working with nonprofits in various ways: planning with them, coordinating services, developing policy options with them, and providing them with in-kind support.[3] The most common mode, however, was provision of financial support to nonprofits,

which was reported by 79 percent of the municipalities and 95 percent of the counties surveyed.[4] The 217 North Carolina local governments responding to the survey reported budgeting a total of nearly $75 million for nonprofits in 1997–98. This represented an average allocation of 0.9 percent of municipal budgets and 1.5 percent of county budgets.

Obviously, funding nonprofits is common among North Carolina counties and municipalities. Understanding the purposes behind that funding will help public officials (and citizens) decide how to make better funding decisions.

2. Why do we want to have a formal process for making funding decisions? Recent interviews with local government staff show a wide variation in philosophies, practices, and concerns relating to how local governments decide to fund nonprofits:[5]

> *"We look to the department heads to assess whether the nonprofit service is needed."*

> *"New requests should come to the manager first."*

> *"Our county only funded one nonprofit, and that was because one commissioner has a personal interest and knowledge about the operations of this nonprofit."*

> *"We don't have a process for receiving nonprofit applications because we don't have additional money to fund new nonprofits."*

> *"There are no guidelines. Established nonprofits get the funding; they have the political support."*

> *"We only fund the nonprofits we have a history of supporting."*

> *"Since nonprofit funding is a relatively small part of the total county budget, it does not get a lot of attention from county staff."*

The credibility of the final choices depends in part on the manner in which the government makes the decision: who decides, what information the decision makers receive, what opportunities exist for community input, and how all of that is perceived by the public. A decision-making process can serve a variety of purposes. It can

- demonstrate fairness.
- encourage citizen input.
- maximize accountability.
- minimize negative consequences or public criticism.
- streamline decision making.
- coordinate decision making with other local funders.
- determine whether the nonprofit can achieve the government's goals.

Some of these intentions may be in conflict. To design a process that will

Among the community services that nonprofits may provide are swimming pools and animal shelters.

work well for their community, officials need to identify, clarify, and address their purposes for setting up a process. Then they need to select procedures and practices that will help them realize those purposes.

Four Key Questions in Designing the Funding Process

1. How will we identify community needs that we want to help nonprofits address?

If a government does not gather information about specific community needs, then meeting those needs is likely to be accidental rather than deliberate. A government can learn about public issues that people want it to address in several ways.

Officials might compile information that staff and elected officials have accumulated in the course of their contacts with citizens. For example, departments can be asked to list priorities for services in their areas of responsibility. Some local governments do this as part of their annual budget-preparation process. Elected officials sometimes use work sessions or retreats to develop lists of priorities for government action. Both government staff and elected officials can gain insight into the needs of the community simply by doing their normal work. If, however, their perspectives do not encompass the diversity within a community or if they do not seek to become connected with and informed about local groups that are not represented, then they may be missing relevant information or new trends.

Another way to learn about community needs is to seek input from nonprofits or the broader community. Asking nonprofits to present evidence of community needs places the burden of determining and describing needs on the nonprofit and therefore lowers information-gathering costs for the local government.

However, this alternative is subject to bias. It tends to favor politically savvy nonprofits and might exclude legitimate community needs of invisible, disenfranchised, or unsophisticated populations. Public hearings, community forums, and other opportunities for citizens to express their views can help provide a broader assessment of community needs.

If one of the reasons for developing a formal funding process is to encourage citizen input, more open, inclusive methods of gathering information may be preferable. If streamlining decision making is a goal, relying on nonprofits to identify and document needs might be more appropriate.

An informal process of exchanging information may be all that is necessary to gather comprehensive data on needs if a community is relatively small and

provides regular opportunities for conversation among diverse stakeholders. This approach may not work as well in larger or more urban areas.

More formal methods of needs assessment include focus groups or surveys of carefully selected samples of the population.[6] Although this approach is more costly, the expense might be shared among local funders, like the United Way, community foundations, and other governments. A joint needs assessment might be particularly useful if one of the purposes for developing a formal process is to coordinate funding with other local funders.

2. How will we obtain nonprofits' proposals for meeting community needs?

Just as advertising may increase attendance at a special public event, the manner in which governments invite funding proposals may determine what they receive. Again, community characteristics, such as the size of the local population or diversity in political philosophies, might drive how a government decides to conduct this process. In a small community, government staff can simply call or send letters to the nonprofits telling them that it is time to submit a proposal. In more populous areas, it might be necessary to use a variety of media for the notification—for example, letters, public notices, newspaper advertisements, Web site announcements, or "listservs" (a computer application that collects multiple e-mail addresses under a single e-mail address, allowing subscribers to send a message to everyone on a list using the one address).

If the government's purposes for funding nonprofits are broad, the government may want to offer all local nonprofits the opportunity to submit proposals. If, however, the purposes are relatively narrow, then contacting the nonprofits that are relevant to the identified goals may be sufficient.

A government can ask nonprofits to apply for funding in either of two ways. By issuing a r*equest for applications* (RFA), the local government informs nonprofits about the opportunity and the process to apply for funding and invites community agencies to design programs and outcomes to meet a problem identified by the agencies themselves. In

a *request for proposals* (RFP), the government specifically defines the target of service (certain populations or certain desired outcomes, for example) in addition to sharing information about the funding process.

3. How will we review proposals?

Government staff, community volunteers, or elected officials might review proposals. Deciding who should do so will reflect the governing board's concern about such issues as timing; efficiency; program goals; previous experience with and level of trust in potential reviewers; delegation of various aspects of program design and execution; and balance between program goals and resource allocation goals.

By having *staff* manage the review, the government might ensure that the work of nonprofits will assist it in achieving specific community objectives. This alternative also may offer the quickest, most easily controlled, and most consistent evaluation. However, it also might perpetuate previously established and familiar funding practices or preclude the infusion of new perspectives or ideas by someone outside the funding organization.

A *volunteer board* could screen applications for the council or the commissioners and might be able to alleviate political pressure on staff and elected officials. To use a volunteer board effectively, a government should allocate funds for staff support and guidance, be willing to share authority with the volunteers, and allow adequate time for the volunteers to make their recommendations.

Having *elected officials* review and rate the applications increases community influence in the process and saves some direct staff costs. On the other hand, elected officials might be swayed by the interpersonal dy-

namics of their board or by the interests of a few vocal or well-connected constituents.

By using some combination of these structures, a community might agree on the relative priority of certain goals and deal realistically with the limits of its own resources. For example, a board that values developing a broad perspective on any important issue might ask both department heads and a volunteer advisory board to review applications and make suggestions for funding to the manager. The manager might then make a final balanced recommendation to the elected board.

4. How will we make funding decisions?

The elected governing board holds the ultimate responsibility for making funding decisions, which it carries out through adoption of a budget ordinance. But it may set up procedures for subordinate groups to allocate the funds it authorizes. For example, some governing boards authorize a certain amount of funding for nonprofits and ask a citizen advisory committee or a staff task force to recommend how to allocate those funds.

Having public criteria and procedures for deciding which nonprofits to fund, and at what level, can help relieve boards of some of the political pressure that they may feel in making those decisions.

Clarity about who will decide and on what basis is important to good relationships both inside and outside government. Changing procedures in the middle of budget review can produce mistrust and resentment. If the board wants to retain full flexibility to decide on nonprofit funding, it should clearly state so at the beginning.

Hard Work but Worth It

Elected officials and staff may be inclined to ask, "Isn't there an

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easier way to do this?" Answering all the questions posed in this article may take a lot of meetings and discussions and may generate disagreements along the way to a single, useful product. However, if key stakeholders, especially elected officials, do not participate in the design of the process, it always will be subject to challenge, circumvention, or negative reaction.

Comparing the relative merits of nonprofits' applications for funds is challenging. Decision makers face hard choices among people in need (such as youth, the working poor, and senior citizens) and competing political interests (for example, the arts, economic development, and human services). They must evaluate the organizational capacity of individual nonprofits to achieve the government's goals.

Having to allocate limited resources among many worthy efforts is understandably frustrating. Decision makers may be tempted to take out their frustration on nonprofits by not engaging in a fully impartial or deliberate evaluation process. That would be inappropriate. The cause of the frustration is not nonprofits but the pressure to make hard choices. Nonprofits articulate existing community needs and bring forth innovative opportunities for addressing those needs.

Recommendations for All Funding Processes

In *The Poisonwood Bible*, Barbara Kingsolver writes, "Everything you're sure is right can be wrong in another place." That observation applies to many governmental practices and is certainly relevant in considering all the possible forms of nonprofit funding processes. The research of the Project to Strengthen Government-Nonprofit Relationships, and the discussions that project personnel have had with practitioners, clearly suggest that no single process can ensure fair, effective, efficient choices about nonprofit funding in every jurisdiction, or even in many jurisdictions.

The project's research and discussions do indicate that, no matter what process a government chooses, it is more likely to be effective overall if

- the government clearly defines at the outset how it will make its funding decisions.
- the government assigns staff to manage the logistics of the funding process.
- the government has a broad-based, flexible strategic plan including goals that nonprofits are expected to achieve.
- the decision makers (elected, professional, or volunteer) avoid personal or professional biases.

Also, mutual trust and accountability among government, nonprofits, and the community they both serve may be enhanced if

- local governments share information as early as possible with all nonprofits and the public regarding the total funding available and the process for application.
- all nonprofits seeking funding use the same application process.
- local governments provide opportunities for input from citizens who are representative of the community.

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- all local governments, foundations, and other community funders use the same application form and, if possible, hold consolidated hearings to receive funding requests.[7]
- after the decisions are made, local governments share information publicly about the amounts that nonprofits sought and received.

Finally, and perhaps most important, local governments should share information about the decision-making process equally and openly within the community. This is the basic platform from which a well-designed process is successfully launched.

Notes

1. The relevant North Carolina General Statutes are Section 153A-449 for cities, 160A-20 for counties.

2. Participants in the Navigating Nonprofit Relationships training offered by the Institute of Government generated this list.

3. Gordon P. Whitaker & Rosalind Day, *How Local Governments Work with Nonprofit Organizations in North Carolina*, POPULAR GOVERNMENT, Winter 2001, at 25, available at www.nonprofit-gov.unc.edu.

4. Total funding for nonprofit organizations is likely to be considerably higher than reported in the survey. Most respondents reported only funds earmarked for nonprofits in their government's annual budget. The totals did not include funding that comes through contracts within the operating budgets of government departments.

5. Lydian Altman-Sauer, Margaret Henderson, & Gordon P. Whitaker, *Strengthening Relationships between Local Governments and Nonprofits*, POPULAR GOVERNMENT, Winter 2001, at 33, available at www.nonprofit-gov.unc.edu.

6. For a discussion of survey procedures, see the article on page 23.

7. Such coordination makes an immediate positive difference for the nonprofits. For example, nonprofits that provide services in Orange County and were requesting financial support from assorted funders in that jurisdiction used to fill out four different application forms, due on different dates, requiring different kinds of information. Agreement to use one consolidated application format saved the nonprofits time and effort. Such coordination benefits the funders because they all have the same information at the same time, instead of each one getting slightly different versions.