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Rethinking Ways to Give Wisely

Special Report by Amy Feldman
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Individuals in the U.S. give away more than \$200 billion a year, yet the vast majority of those decisions are made ad hoc. Few donors have any idea whether they are giving to the best organization in the area they want to improve, or even whether their giving is doing what they want it to do. A slew of nascent efforts to rate and grade charities, as well as the pending overhaul of the big kahuna of nonprofit ratings groups, may change all that.

That's especially true in the current economic downturn. Donors have less money to give, while charities need more cash to provide services to more people in need. The result is more donors who want to know that the money they do give makes a difference, and not-for-profits taking more steps to show their results. But the longer-term trend predates the recession. Baby boomers have become used to getting advice on their finances, yet there are few places to turn for philanthropic advice for those giving less than \$1 million. While increasing numbers of people have set up donor-advised funds, which can be a smart financial-planning move, these vehicles don't answer the question of where to give the money for greatest effect.

"There is a lot of energy around this right now," says Laura Callanan, a philanthropy expert at McKinsey & Co. "Social impact assessment is the holy grail for people doing philanthropy and nonprofit work. How do you know what works and why? And how do you know that money is making a difference in people's lives?"

After all, a homeless shelter, international relief organization, or other philanthropy is not a business; its social impact needs to be evaluated on different criteria than profit and loss and the true impact of its programs may not be clear for years to come. Plus, doing an in-depth analysis may be too expensive for many small not-for-profits that are already stretched for funds.

"We as Americans like to do things immediately," says GuideStar President Bob Ottenhoff. "But a lot of the problems in Haiti, they have been experiencing for years or for decades. We learned this from Hurricane Katrina—the initial surge of support isn't sufficient."

For donors, then, the best approach is to think about your philanthropic giving more along the lines of how you view your investment portfolio. That means thinking through the big questions first (what matters to you?), and then drilling down to those groups that are doing the best work. The new rating efforts take different approaches to answering the second part of that.

GiveWell, launched in 2007, offers rigorous Wall Street-like research on nearly 400 charities, in which it tries to determine how effective they are. Few charities have enough data or analysis to provide such proof, and GiveWell only recommends those that can. "The charity needs to do a lot of analysis on its own," says GiveWell co-founder Holden Karnofsky. "It sounds like common sense, but it is also the most difficult question to answer."

Root Cause has begun doing similar research reports, though geared toward financial advisers. Its first batch of research covers educational groups in Mas-

sachusetts. GreatNonprofits, also started in 2007, allows donors, volunteers, and social-service recipients to write reviews ala TripAdvisor or Yelp; it currently has reviews of some 3,000 not-for-profits.

PORTFOLIOS OF NOT-FOR-PROFITS

Philanthropedia, which recently launched, garners the opinions of experts in different sectors and creates what it calls "expert mutual funds," portfolios of not-for-profits in areas such as climate change or microfinance with a dozen or so holdings in each. Partners for Change is also working up a mutual-fund-like approach, though its concept will mimic the portfolios of successful foundations in certain areas. Executive Director Jim Litwin says that he expects to launch in the summer, so that advisers will be prepared to roll out the offerings to clients in the fall giving season. Litwin hopes that by targeting advisers, rather than individuals directly, he will be able to reach donors with \$10,000 or more to give, rather than the smaller amounts that many give online. As Litwin says: "These foundations have already done all the work on what the most effective organizations are, so why can't you leverage that knowledge of where to give?"

Consider how Charity Navigator is rethinking its star rating system under the direction of Ken Berger, its executive director since June 2008. With star ratings on 5,500 charities and some 4 million hits to the site each year, Charity Navigator is the biggest of the online philanthropy rating agencies, and sets the tone for how individuals think about their giving. From its 2001 founding until recently, however, it had rated charities largely on financial benchmarks—and given them high marks for low overhead, a metric that academic research now shows is not that helpful in evaluating a nonprofit's work.

The bigger question—and ultimately the bigger opportunity—is how these new efforts to rate charities and to influence donors' decisions will impact the way that philanthropies themselves operate. The hope among those who are launching these efforts is that if not-for-profits knew that their programs weren't working that well, they would revamp them based on that information. Also, if more of that \$200 billion ends up going to the most effective charities, it could push the least effective ones to rethink what they're doing. "We're starting to see a shakeout now," says Nancy Kelly, an accountant at the Metis Group, who has focused on not-for-profits for 25 years. "You're seeing more competition for dollars and more merger activity than in the past 15 years. It is forcing nonprofits to look at their operations like a business."