FSG
FOUNDATION STRATEGY GROUP
Perspectives on Corporate Philanthropy
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Corporate Giving and the Corporate Foundation

by Mark Kramer, Marc Pfitzer and Kyle Peterson

How should a corporation coordinate direct charitable contributions with grants from its foundation? If there is no foundation, should the corporation create one? And if so, should it be endowed or funded annually?

These are some of the perplexing questions that our clients often ask. Our answer is always the same: There is no compelling reason why every corporation should have a foundation. And if there is a foundation, there is no universal rule for the optimum division of contributions between it and the company. Companies must focus instead on the best way to achieve social impact and competitive advantage. The company's overall social investment strategy should determine structural and organizational issues, rather than vice versa. And once the strategy is in place, management must clearly delineate areas of responsibility to avoid generating either internal or external confusion.

Giving through a Foundation

There are only a few legal restrictions in the US that limit what foundations can fund, most notably the prohibitions against lobbying and self-dealing. This means that foundation grants cannot be used to influence legislation or in ways that provide a direct economic benefit to the corporation or its officers. For example, giving a grant to a university to conduct research on behalf of the company, to recruit employees, or as a *de facto* discount on its purchases, would not be allowed. But very few corporate contributions raise issues like these. And they may be entirely irrelevant for European foundations, where regulations differ from country to country and some foundations actually own the companies that fund them.

However, the fact that most contributions *could* be made through a foundation doesn't mean that they *should* be. The answer depends on the strategic role that the foundation plays within the larger context of corporate giving and corporate social responsibility. In our experience, that role is not often well-defined. The origins of most corporate foundations may be well-remembered – a legacy from some past acquisition, public relations initiative, or a civic-minded CEO – but their initial purpose and past history does not necessarily define the most valuable role that they can play today.

The "Independence" of Corporate Foundations

Lack of clarity about the relationship between the foundation and the company seems to be the single issue that causes clients the greatest concern. Foundation staff often struggle with the degree to which they are – or should be – independent of the company,

FSG News

Clients

FSG's latest work covers a wide range of issues for community, private and corporate foundation clients around the world:

For a corporate philanthropy client, FSG developed a more sustainable approach to create social and business impact — a Social Investment Fund to support entrepreneurs who are part of the company's supply chain in developing countries. In addition to creating jobs, the initiative will create new services which are currently lacking or unaffordable for the vast majority of the population in Latin America and Africa.

The Social Investment Fund differs from traditional grantmaking in that it features loans and/or equity investments in small and medium-sized business.

For a $400MM foundation on the West Coast engaged in building the field of social entrepreneurship, FSG is working with staff and board to clarify goals and develop a comprehensive evaluation plan.

Congratulations

We are pleased to announce that Mark Kramer has been named a Senior Fellow in the Corporate Social Responsibility Initiative of

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and this can be a major source of internal confusion. Often there is a lingering unspoken sentiment that the foundation *ought* to be independent, causing the company to downplay the relationship and encouraging ambiguity.

In reality, the choice is not between unfettered freedom and absolute obedience. The foundation will need to serve the company's interests on certain issues or in certain locations, but it may have a free hand in other areas. What matters is that the areas of independence and corporate control are clearly and consistently spelled out. Otherwise, the resulting ambiguity will create inefficiency, stress, and lost opportunities internally – and send contradictory signals to stakeholders externally.

The Benefits of Using a Foundation

With all this potential for confusion, what are the off-setting benefits of corporate foundations?

First, they permit the company to time-shift its contributions. This can serve to smooth fluctuations in earnings, capture a windfall, or announce a major contribution before knowing how it can best be spent. One company made immediate headlines by contributing $25 million to its foundation during a time of crisis in its local community. Unfortunately, time shifting can be taken too far: ten years later, most of the money was still sitting in the foundation unspent.

A second advantage is that the foundation's separate governance structure enables outside experts and stakeholders to sit on the board and contribute to its deliberations – without making them employees of the company. In theory, the ability to add independent directors should provide relevant expertise, significant credibility and greater transparency. In practice, however, outside directors of corporate foundations are rarely found.

A third benefit is the somewhat limited degree of independence that foundations may have from their corporate donors. Although many corporate foundations profess independence, very few are endowed, staffed and governed separately from the company. In most cases, the foundation board consists entirely of senior corporate officers and its grant budget is funded currently by the company. Consequently, company officers can hire and fire foundation staff or cut off further contributions, rendering the foundation's "independence" illusory. Therefore, although a corporate foundation may bring a somewhat greater degree of credibility with outside parties, most sophisticated stakeholders recognize that they are merely dealing indirectly with the corporation itself.

Precisely because the foundation's independence is so fragile, it is essential that companies clearly delineate the degrees of freedom accorded foundation staff. The question of whether a grant should come from the foundation or the corporation rides on the clarity and consistency of this delineation. If grants programs are shifted around as departmental budgets change, it will be impossible to administer them effectively or maintain the necessary clarity of roles.

To Endow or Not to Endow?

The fact that a corporate foundation is never truly independent also helps answer whether it should be endowed or funded currently. If the company earns a higher return on its capital than the foundation does on its investments, which is often the case, then it makes more sense to fund the foundation currently and leave most of the capital where it can earn the highest return. In the special case of multi-year commitments to a grantee or major initiative, the company may want to pre-fund the entire amount to avoid imposing a burden on future contribution budgets – but pre-funding a grant commitment falls far short of contributing to create a full endowment like a private foundation.

Of course, a foundation's endowment can also be used to advance social objectives through investments that create social benefit. Some companies have provided loans for economic development or to assist nonprofit agencies. Using the foundation's investment portfolio for social objectives makes sense but, again, it is extremely rarely done. As a result, contributing a substantial endowment to a corporate foundation often fails to buy true independence and merely ties up capital that provides neither an immediate social benefit nor an optimum investment return.

Separating Philanthropy from Corporate Strategy

Apart from the benefits of a corporate foundation, noted above, there is one major drawback: the risk of alienating corporate social investments from the rest of the company. Our experience suggests that companies create the greatest value, both for themselves and for society, when they use philanthropy to strengthen their competitive contexts, leverage their distinctive capabilities beyond monetary contributions, and align their social investment programs with overall corporate strategy.

Putting this approach into practice requires a close relationship between line managers and corporate giving staff. It calls for creativity in discovering company resources that could be tapped for social objectives, and identifying the social issues that affect the company's competitive positioning. It requires flexibility as different business units in various locations may select different social issue to tackle. Above all, it requires a single comprehensive social investment strategy that is meaningfully aligned with the business.

In short, effective corporate philanthropy must be "baked in" to the business, not "layered on" through an unrelated contributions program. Having a corporate foundation does not preclude this close integration of social and economic activities – just as the absence of a foundation doesn't assure it. But a foundation does increase the complexity of coordination and may contribute to a culture that disconnects philanthropy from the business. At the very least, it requires that foundation staff be knowledgeable about the business, and work comfortably with corporate or business unit staff.

When Should a Corporate Foundation be Created?
If there is no corporate foundation, should one be created? The advantages and disadvantages discussed above suggest certain situations where establishing a foundation might be favorable:

- If the company envisions extended partnerships with NGOs and international aid organizations, or if its motives might somehow be suspect to outside stakeholders, then the modest veneer of independence may be helpful.
- If there is a need for outside expertise on the board, then the governance structure may be beneficial.
- If there are likely to be fluctuations in earnings, then the flexibility in timing may be useful.
- If the investment portfolio of the foundation can be used for social purposes.

Conversely, creating a foundation may carry disadvantages in certain circumstances:

- If, in the US, the contributions are likely to create direct economic benefits for the business or influence legislation.
- If the leverage of unique corporate capabilities requires close integration with the business units, or if the social investment strategy is highly decentralized.
- If the corporate brand and communications channels can be leveraged to create social value or to more directly tie the contributions to the company's reputation.

Making It Work
Ultimately, our experience working with major corporations around the world suggests that whether or not a company uses the foundation structure is immaterial to the effectiveness of its social investment program, as long as the overall strategy is sound and the responsibilities are clearly and consistently delineated. Most strategies can be implemented equally well through foundation or non-foundation structures. Once a clear strategy has been developed, existing philanthropic responsibilities can be "migrated" to the most effective positions within the corporation or foundation, and new structures can be developed to complement existing ones.

The key to a successful social investment program is to look beyond structural considerations, historical biases and departmental conflicts, and to focus on the company's overall social investment strategy across all business units and philanthropic structures. Getting clear about philanthropic strategy and then translating that into consistent operational practices can produce tremendous benefits for the company in terms of increased efficiency, more productive staff, more engaged employees, more satisfied stakeholders and, most important of all, substantially greater value for the business and for its communities.

FSG News

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the Center for Business and Government at Harvard University's John F. Kennedy School of Government. During the course of this year, Mark will work with selected global companies to apply scenario planning techniques to identify new opportunities in corporate social responsibility.

Congratulations also to Kyle Peterson on the birth of his son Finn Manning Foday Peterson.

A Growing Team

We are delighted that a new Consultant has joined our team.

Karin Jestin has joined us as a Senior Consultant in our Geneva office. Karin comes to FSG with significant experience both in the corporate and non-profit sectors. Prior to joining FSG, Karin worked for the International Federation of Red Cross and Red Crescent Societies, coordinating the implementation of a worldwide change initiative, and supported community development and disaster preparedness efforts in the Middle-East and North Africa Regions.

Karin began her career as a consultant with McKinsey & Company focusing on strategy, organization and operations for clients in the Paris, Geneva, Milan and London offices.

Karin holds an MA in International Management from HEC, France and has done graduate work at Stern School of Management at New York University and the University Luigi Bocconi, Milano, Italy. Karin is also fluent in three languages.

If we can be of help to your corporation or its foundation in evaluating existing or potential social investment structures and their alignment with strategy, please give us a call.

In the U.S., contact Kyle Peterson at 617-357-4000 x 117
In Europe, contact Marc Pfitzer at 41-22-807-2482

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About FSG

The Foundation Strategy Group was founded with the vision of improving corporate and private philanthropy's potential to impact society. With offices in Boston, San Francisco and Geneva, our international team of consultants is drawn from the world's top strategy firms and dedicated exclusively to developing philanthropic and CSR strategies that achieve measurable results.

Our operational experience enables us to assess the impact of current giving programs or design worldwide management systems that link philanthropy, CSR, and social investment. Our investment in ideas, depth of practical experience, and collaborative approach, keep us at the forefront of the field and help our clients create greater impact.

For more information call us or visit our website.

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