McKinsey on **Nonprofits**

An in-depth look at the problems facing senior managers | Published by *The McKinsey Quarterly* | September 2006

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A **nonprofit** goes for broke

When the Atlantic Philanthropies decided to spend its entire endowment by 2020, it faced huge challenges—which it has so far managed successfully, providing an example for institutions contemplating transformative change.

Article at a glance

Growth is the byword for success at many organizations, but not for the Atlantic Philanthropies, a $3.8 billion foundation that has decided to give away its endowment and shutter its operations by 2020.

By spending down the endowment quickly instead of using it as a war chest to finance perpetual philanthropy, Atlantic expects to achieve superior social returns.

The organizational challenges stemming from the decision proved daunting and ultimately affected everything from Atlantic's choice of grantees to the kinds of people it employs.

Atlantic's story offers strategic, operational, and organizational lessons for any foundation or comparable institution that is considering transformative change.

A **nonprofit** goes for broke

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Staying in business is a preoccupation for most organizations, but not for the Atlantic Philanthropies, a large private foundation dedicated to improving the lives of the disadvantaged and other vulnerable people. In 2002 Atlantic decided to spend its entire endowment—nearly $4 billion—before 2020. Its move reflects a belief in "giving while living" and the conviction that when it comes to social impact, money spent today is worth more than money saved for tomorrow. Although such ideas aren't new to philanthropy, the decision to take them to their logical conclusion and shutter a foundation is rare. After all, perpetual foundations can refine where and how they invest in order to ensure that they meet changing social needs for generations—and make huge financial and social contributions as a result. Moreover, the challenges associated with such a radical exercise in change management are daunting.

Atlantic found that its decision ultimately affected its choice of grantees, approach to grant making, and organizational structure.[1] To be sure, the decision to spend down wasn't made in isolation; it was influenced by two other noteworthy events: the formal abandonment of the foundation's practice of anonymous giving and an emerging effort to refocus the grants.[2] These moves, by themselves, would have been significant, but the spend-down decision made the resulting changes more urgent and far-reaching by acting as a catalyst to prompt the board, management, and staff of Atlantic to focus even more tightly on its legacy and goals.

The changes are ongoing. Atlantic is still refining the detailed objectives of its grant-making programs, dealing with the impact that spending down has on its work processes and human resources, and testing its new approach to evaluating projects and programs. Although the full social impact on the grantees will become clear only over time, the foundation has already shown how a major philanthropy can change direction. Atlantic offers not only encouragement for foundations considering a limited-life approach but also strategic, operational, and organizational lessons for similar institutions contemplating other significant changes.

Giving while living

Atlantic's new approach to giving is the product of two powerful ideas. The first was articulated most clearly by Andrew Carnegie, the US industrialist and philanthropist, who suggested in 1889 that "the man who dies . . . rich dies disgraced."[3] Carnegie argued that the wealthy should treat their fortunes as a public trust while alive, rather than waiting until death to give wealth back to society. For many philanthropists, this notion of giving while living manifests itself in the creation and management of perpetual foundations that use large endowments to produce an annual income for disbursement—in the United States, a little above the 5 percent of assets mandated by law.[4] Carnegie himself endowed 11 trusts that still exist today.

Carnegie's philosophy gains force when linked to the time value of money, a standard financial concept that, when applied to philanthropy, shows that using an endowment to finance attractive social investments sooner rather than later offers superior social returns.[5] How so? A foundation with a fixed life span or a high payout rate can quickly pit its resources against today's most urgent problems.

[1] In late 2005, McKinsey worked with Atlantic to review the lessons of the process that had transformed it from 1999 to 2005. During that period, McKinsey hadn't worked with the foundation.
[2] From Atlantic's creation, in 1982, until July 2001, all grants were anonymous, and the foundation itself had little or no public profile.
[3] Andrew Carnegie, "Wealth," *North American Review*, 1889, Volume 148, Number 391, pp. 653–4.
[4] The Foundation Center estimates that US foundations independent of communities and companies disbursed 5.7 percent of their total assets in 2005.
[5] Paul J. Jansen and David M. Katz, "For nonprofits, time is money," *The McKinsey Quarterly*, 2002 Number 1, pp. 124–33.

Exhibit 1

Atlantic's programs

	Countries	Program objectives
Aging	Bermuda, Northern Ireland, Republic of Ireland, United States	• Encourage society to treat older adults with respect • Improve access to health and support systems • Build strong cadre of older adult leaders • Support older adults' contributions of expertise to society
Disadvantaged children and youth	Bermuda, Northern Ireland, Republic of Ireland, United States	• Support educational programs to prepare children for adulthood • Support comprehensive, preventive health care • Support mentoring programs, family counseling
Population health	Australia, South Africa, Vietnam	• Build capacity of health institutions • Support alignment of national policies with local interventions • Increase promotion of national health initiatives • Increase number of population health professionals • Improve health-system information systems • Address neglected health conditions
Reconciliation and human rights	Northern Ireland, Republic of Ireland, South Africa, United States	• Support reconciliation, peace building • Improve access to justice, public services for vulnerable groups

Source: The Atlantic Philanthropies

Although giving while living and maximizing social returns have recently enjoyed a higher profile thanks to Warren Buffett's decision to channel more than $30 billion of his fortune through the Bill & Melinda Gates Foundation, only a few philanthropies have ever spent their entire endowment. Examples of those that have include the Aaron Diamond Foundation, which made $220 million in grants from 1987 to 1996, and the John M. Olin Foundation, which closed in 2005 after distributing $370 million.

Atlantic's example will be on a different order of magnitude. Created in 1982 by Charles F. Feeney, a cofounder of Duty Free Shoppers, Bermuda-based Atlantic is one of the world's larger foundations. If Atlantic was based in the United States, its June 2006 endowment of $3.8 billion would place it among the top 15 US foundations.

Giving while living and maximizing social returns are two ideas that have long appealed to Feeney, who considered limiting the life span of Atlantic very early in its operations. In his words, "If I have $10 in my pocket and I do something with it today, it's already producing $10 worth of good."[6] This philosophy was formalized in 2002, when Atlantic's board agreed to spend the entire endowment before 2020. Doing so will require annual grants of $300 million to $350 million for the next decade—equivalent to an initial payout rate of nearly 10 percent. In 2005 Atlantic made almost $300 million in grants in Australia, Bermuda, Northern Ireland, the Republic of Ireland, South Africa, the United States, and Vietnam. This money was distributed to nonprofits working in four program areas: aging, disadvantaged children and youth, population health, and reconciliation and human rights (Exhibit 1).

Spending down

Although Atlantic's leadership had a clear sense of the goals and guiding principles behind its decision to spend down, what came next was often complicated and difficult: a "messy" process, in the words of one Atlantic executive. This messiness was largely inevitable, given the scope and timing of the changes taking place, as well as the number of parties affected. A

[6] Charles F. Feeney, interviewed by Conor O'Clery, "One life to give," *Irish America*, December/January 2004.

foundation doesn't need to limit its life span to change its strategy, operations, or organization. But as Atlantic's example shows, a focus on a finite period of time can prompt—and facilitate—changes in anything from where and how a foundation gives its money to the way it manages and motivates its people (Exhibit 2).

A hanging in the morning

The decision to spend down can have profound effects on a foundation's strategy. Fortunately, a fixed end date also serves as a powerful catalyst. As one Atlantic board member wryly put it, "Nothing focuses the mind like a hanging in the morning." Indeed, the decision creates an institution-wide focus on a foundation's legacy and impact, and this can make change much easier to achieve.

Questions of impact are important to all foundations, of course, but they are unusually salient when time is running out: a limited-life organization has only one chance to realize its vision. Although Atlantic was already considering realigning its grants and programs as a way to raise its impact, the spend-down decision strongly influenced its new areas of concentration: for instance, its management and board decided that grants would now focus on problems allowing it to make considerable progress within the spend-down period. What's more, Atlantic now had to find enough grantees capable of absorbing investments exceeding, in some cases, $5 million—big money in a sector accustomed to much smaller payouts.[7]

The consequences of the new reasoning became apparent in late 2002, when Atlantic's board eliminated three potential program areas from consideration—population dynamics, communicable diseases, and the decriminalization of drugs—as too complex to address in the spend-down time frame. Likewise, considerations of impact contributed strongly to elements of Atlantic's new programs on aging, disadvantaged children, population health, and human rights:

[7] The Foundation Center's 2006 survey of nearly 1,200 large US foundations found that of 125,000 grants made in 2004, only 240 exceeded $5 million.

Exhibit 2

Before . . . and after

	2001 (before changes)	2005 (after changes)
Spending	• Increasing rate of spending; no formal policy	• Explicitly spend down endowment over 12 to 15 years
Programs	• Higher education • Nonprofit sector • Precollegiate education, youth development	• Aging • Disadvantaged children and youth • Population health • Reconciliation and human rights
Grant making	• Opportunism, flexibility • High degree of local autonomy • Less structured approach to evaluation	• Focused programs • High engagement with grantees; focused bets on fewer grantees • Rigorous evaluation, measurement
Organization	• Loose federation of country offices • Operations secondary to program staff • 82 employees	• Global matrix by program, geography • Operations integrated with program staff • 100 employees • Investments in HR, communications, evaluation
Culture	• Anonymous • Programs, locations separated	• Increasingly open internally and externally • Globally collaborative

Source: The Atlantic Philanthropies

for example, the human-rights program dropped a broad proposal aimed at improving the “rights cultures” of particular countries in favor of a more focused and shorter-term initiative to build stable, professional networks of human-rights organizations within them.

Meanwhile, as Atlantic explored the new goals and priorities, it was also negotiating painful exits from its long-standing programs. In 2001 80 percent of its grants ($269 million) were concentrated in education (including primary, secondary, and higher education) and in organizational and leadership-building programs for the nonprofit sector; within two years, it awarded no money in these areas. Atlantic’s approach to the exits was to move quickly to minimize uncertainty while remaining sensitive to the needs of grantees by honoring existing grant proposals and awarding almost $180 million in exit grants in 2003.

The time pressure created by the spend-down decision helped complicate the process. Some early decisions had to be revised at a cost in time and effort: task forces were created to develop detailed grant strategies within the new focus areas, for example, but an initial lack of managerial involvement in the effort led to confused expectations and, ultimately, extensive rework after the board saw the results. That experience dampened morale among staff members who were otherwise energized by the changes. Another unintended consequence of the time pressure was that staff members charged with designing new programs also had to manage the exit from current ones. This burden placed an unexpected strain on Atlantic’s personnel and grantees, some of whom later complained of inadequate communication.

Despite the problems, the pressure of a deadline did have benefits: it helped focus Atlantic’s leadership and staff and spurred them to not only raise—and address—difficult questions about the foundation’s mission but also make tough strategic choices about how to allocate resources most effectively.

New roads need new vehicles

In some ways, the operational challenge of spending down is clear: for example, a foundation must increase the liquidity of its investment portfolio while decreasing the volatility of its returns as its spending commitments rise and the end of operations approaches. However, the impact of these changes on Atlantic’s operations was much more far-reaching, as Atlantic faced the hard task of establishing the mechanisms that would make the most of its spending. In the end, it found itself reexamining most of its grant-making principles and processes.

Before 2001 Atlantic’s grant making was characterized by opportunism and flexibility. Individual judgment was the principal quality control. These characteristics worked well for a secretive organization whose country offices and grant-making programs operated independently. Yet the Atlantic staffers and managers we interviewed in 2005 suggested that although the original approach produced some important successes, it also created a relatively high degree of variability in outcomes. With no more than 15 years of existence left, Atlantic needed a more consistent grant-making approach that could produce big results faster. This consideration reinforced an existing desire among Atlantic’s board and management team to establish a more focused and measurable system.

Atlantic’s response was to adopt a new set of three grant-making principles to complement the foundation’s new strategic goals. These principles were inspired in part by earlier successes with big-budget, focused programs—such as Atlantic’s work on higher education in Ireland—that had already begun operation before the spend-down decision was finalized. The first principle is a willingness to place fewer but more transformative bets on grantees, so that an impact becomes apparent within three to five years. The second is a desire to establish and maintain a greater degree of engagement with grantees to help them improve their strategic planning and effectiveness.

(Similarly, Atlantic has placed more emphasis on measuring the impact of its own work and on sharing the lessons inside and outside the organization.) Finally, Atlantic now aspires to make grants to nonprofits that can use the money as leverage to obtain support from other funding sources, thereby maximizing the effect of every dollar spent.

Atlantic is starting to weave these principles into the day-to-day workings of its operations. It has formalized its due-diligence process, for example, and now has grant proposals reviewed by a new program-investment committee, which applies common standards to all grant-making programs and identifies areas of potential collaboration among them. Atlantic's efforts to measure its impact on grantees are now supported by a small team responsible for assessing the way grants are used and programs are implemented. Last, Atlantic has created a team of senior managers to monitor and address the effects of spending down on the foundation's core work processes, program strategy, organizational culture, and human-resource requirements.

The foundation's staff and management report that these efforts have already helped focus the grant-making process because it is now easier to choose among opportunities. In the words of one staffer, Atlantic can now say, "This is what we are about, and this is what we are not about." There is a general and growing optimism that the improved consistency seen thus far will ultimately translate into more effective grant making.

Permanent revolution

The organizational implications of Atlantic's new direction were profound, affecting everything from the foundation's size and structure to the skills required of its people. Atlantic's experience reinforces the notion that the uncertainty accompanying sweeping change can create anxiety among employees—even those inspired by the changes. Moreover, the uncertainty must be managed carefully, lest it bring instability or even distract people from an organization's mission. This uncertainty is exacerbated in a spend-down environment where, after all, every employee's tenure has a visible end date. As one staffer noted, the organization is in "permanent revolution."

Consider Atlantic's organizational structure, which has changed markedly since 2001. The adoption of the new program strategies and grant-making approach encouraged the foundation to replace its loose federation of country offices with a more integrated, global structure arranged around specific programs and geographies. Further, the desire to increase the level of engagement with grantees forced Atlantic to support its program staff with an expanded team of "functional" colleagues working in areas ranging from evaluating the impact of grants to communications and human resources.

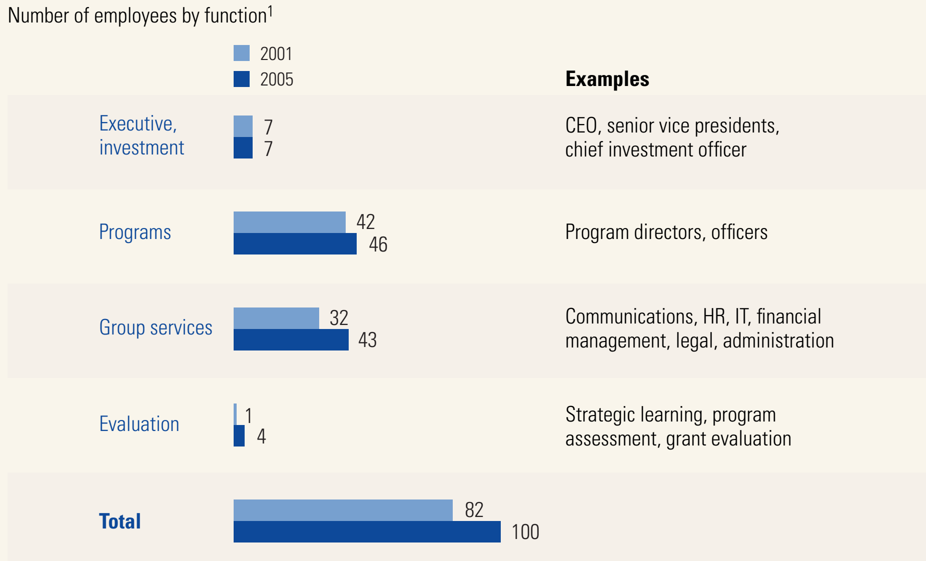
Another difference is integration. Before 2001 Atlantic's program staff tended to be autonomous, requiring mostly administrative support. Since then, the operations staff has made efforts to integrate its functions more closely with the work of the grant programs. Today program officers often seek the expertise of the operations staff when they face complex financial, legal, or organizational issues among potential grantees.

The need for operational support and personnel to evaluate the effectiveness of grants contributed to a 22 percent increase in staff levels from 2001 to 2005. (Three-quarters of the new positions were in support roles.) This is a huge change for a small organization such as Atlantic, which even today has a staff of only 100 people (Exhibit 3). Further, the overall increase in the number of employees during this period significantly understates the magnitude of the shift, as it includes some 75 people who left Atlantic from 2001 to 2005—a major development for an organization where turnover had been minimal.

Clearly, such a degree of upheaval would be stressful for the employees of any organization. For many Atlantic staffers there was particular frustration that the length of the process produced

Exhibit 3

Staff changes at Atlantic



[1] Numbers reflect 75 people who left Atlantic from 2001 to 2005.

Source: The Atlantic Philanthropies

a debilitating sense of "change fatigue." Atlantic's response—an attempt to maintain momentum while providing enough stability to take advantage of the changes already made—suggests three lessons for institutions confronting similar situations. Moreover, Atlantic's example highlights the way strong leadership and an active board can help carry an organization through difficult times.

First, it is important to understand that staffers may find uncertainty about change as difficult to cope with as change itself. Atlantic made the decision to spend down, refocus programs, and rethink its grant-making approach in early 2002, but the implications for the staff weren't clear until the program strategies and organizational structure were finalized, in mid-2003. This delay may have been unavoidable for Atlantic's management, but it came at a cost to morale: for example, the length of time it took to evaluate the changed organization's personnel needs, combined with various departures during this period, added up to what one interviewee called "death by a thousand paper cuts." Moreover, the excess time needed to make program decisions extended unproductive debates over program strategies and made it difficult for people to commit themselves to new approaches.

Second, Atlantic's response shows that by involving people in important decisions, a foundation can create a reservoir of excitement that makes change easier. Atlantic's management took particular care to invite the participation of the staff at several key junctures and in most cases incorporated its input. According to one staffer, an invitation to participate in the program strategy task forces "won hearts and minds" for the new vision, as did inviting managers to participate in the restatement of the foundation's mission. However, Atlantic's initial failure—corrected later—to provide clear criteria to the staffers charged with exploring new program areas created unnecessary frustration.

Third, it's necessary to communicate, communicate, communicate. After the launch of the strategy task forces, in early 2002, for example, Atlantic's senior managers were understandably reluctant to open a discussion on the future roles of the organization's staff until their nature became clear. Some staffers saw this reticence as a lack of transparency, and the seeming "business as usual" attitude—when change clearly was imminent—was stressful for them. Morale improved after management responded with new initiatives, in mid-2003: for example, a new global human-resources group was created to review skills and opportunities more comprehensively and establish training and development programs to help those moving to new roles within the foundation. Atlantic's senior management also appointed key employees to a team created to identify—and tackle—pressing issues among staffers, thus providing them with another channel of communication. More recently, celebrating milestones, such as the start of mainstream grant making in the new program areas, has helped Atlantic to chart its progress in achieving its goals and had a positive effect on the staff. Regularly identifying and communicating accomplishments can help inoculate organizations against the effects of change fatigue.

During troublesome periods of uncertainty, Atlantic benefited from the commitment of its management and its board. Many staff members reported that the decision to abandon anonymity and to spend down made them feel "incredibly privileged." Moreover, Atlantic's senior-management team reinforced this energy by, for example, consistently articulating a passion for the new focus on disadvantaged populations and a commitment to develop the programs and systems to support it. The senior-management team was also able to learn on the fly and to correct its course quickly when necessary. Surveys of the staff in 2003 and 2004, for instance, helped managers to assess progress, identify problems, and prioritize responses—efforts that boosted morale.

The spend-down decision also motivated Atlantic's board. Any foundation with a living founder must balance the board's strategic leadership with respect for the founder's wishes, which may well evolve over time. For Atlantic the adoption of a limited life span demanded unprecedented involvement from the board in strategic decisions. Board members report that these demands "concentrated minds wonderfully" and underlined the important role that the board will continue to have in expressing the vision of Atlantic's founder effectively and successfully.

Atlantic has taken the bold step of tying its legacy to the impact it can achieve in the next 10 to 15 years. Although the effects of this decision have proved challenging and have had big organizational costs, there is widespread agreement within Atlantic that the changes have increased its ability to improve the lives of disadvantaged and vulnerable people. The fact that the foundation has been able to make difficult trade-offs, adapt to changing circumstances, and keep its momentum as the process unfolds offers encouragement to any institution contemplating transformative change. Q

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