



## **Reset, Ready, Start**

**Lessons from ZeroDivide's Inaugural Year**

**August 2009**

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## **Background context**

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The following paper offers an up-close look at what it really takes to change how you do business. ZeroDivide, founded as the Community Technology Foundation of California, has evolved through several stages in its short life span. Funded as the result of a utility merger settlement, the Foundation exists to support access and use of new technologies by low-income and other underserved communities. In its first few years, the organization operated much like other grantmaking foundations, and expected to spend itself out of business within ten years of its founding.

However, the leadership and staff soon learned that even their best efforts in this structure could only scrape the surface of what communities wanted and were capable of developing. The opportunities of digital media, the application of new skills and tools to economic and community development efforts, and the potential that was being sparked by the Foundation's grants were too great to be catalyzed and then abandoned.

From this recognition, as well as a review of the changing context of philanthropy, the Foundation made several noteworthy decisions. It chose to pursue additional funds to maintain its work. It chose to alter its focus to building sustainable enterprises with its nonprofit partners. It chose to restructure its grant making processes and timelines, to retrain its staff to do this, and to bring in new kinds of expertise when needed for its community partners and its staff.

It is too soon in ZeroDivide's work to know how successful these decisions will prove to be. This paper is not intended to document success or failure, but to highlight the types of changes the Foundation has made and the reasons for them. It is also intended to illustrate some of the larger trends currently shaping philanthropy. These trends include efforts to build sustainable enterprises, the push for greater accountability, the development of quantifiable measures of social impact, calls for increased transparency, and a move toward closer working relationships between donors and nonprofits.

## **The community benefit roots of ZeroDivide**

ZeroDivide represents a relatively new, and increasingly common, type of grantmaking organization. Created as a result of community advocacy during the merger of two telecommunications companies, the foundation's very existence exemplifies the community benefit beginnings of many similar funding organizations. Health conversion foundations make up the majority of these types of funders. The privatization of student loan companies, legal settlements associated with tobacco and settlements levied against from public utility companies.<sup>1</sup> Why is this important? While these funders are structured to look much like private foundations, they also are born with and usually retain important community connections. These connections may be built into board leadership roles, mandated through certain geographic or issue-specific restrictions, or chartered into the organization's operating structure in terms of public meeting requirements, the use of community advisors, or other requirements. These requirements are intended to maintain a public voice and decision-making role over the foundation over time.

The benefits of these public connections are many, including representative voices, close connections to public leadership, and expertise from public agencies that can facilitate important partnerships. There are also downsides to these ties, especially if a foundation chooses to seek additional funds and finds it has little or no development expertise on its board. It has frequently been the case that the boards of these kinds of foundations will decide to extend the organization's work, only to realize that they are no longer the right board to carry that work forward.

## **More than any one organization**

While ZeroDivide's own organizational structure plays an important part in the following story, it really is only a supporting part. Many of the changes discussed are as much a part of the broader story of philanthropy in the early 21<sup>st</sup> Century as they are part of ZeroDivide's story.

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<sup>1</sup> There are more than 150 health conversion foundations in the United States. A major legal settlement against the tobacco industry led to the creation of The American Legacy Foundation, and the Stewardship Council resulted from a PUC settlement against Pacific Gas & Electric.

Specifically, the last ten years have seen a remarkable growth in interest in sustainable social change organizations. In some cases, this is synonymous with real social enterprise, scalable business models built and deployed to produce financial returns and significant social impact. In other cases, most of those in which ZeroDivide is engaged, for example, the moment is more transitional – nonprofit organizations that have relied on grants and individual donations actively building revenue streams. These efforts take significant work – they require subtle cultural shifts, wrenching operational changes, and a leadership ability to wring alignment from potentially divergent demands. The ZeroDivide story shows how these changes work for the funder – requiring new skill sets, new allocations of expertise, and new grant making procedures, guidelines and timelines. For ZeroDivide’s partners new financial skills and systems had to be put in place, sometimes quickly and sometimes over time, to track data that investors want, to calculate financial and social returns, and to maintain bottom line costs against top line revenue and social value.

These accounting changes are part and parcel of two other contextual forces. Greater accountability – for dollars, impact, activities, and even strategic direction – has been something of a rhetorical reality for years. In the past five years, however, actual practice has begun to catch up with wishful thinking. Some of this is itself part of expanded societal expectations about information – as we get used to being able to search for anything online at any time, we also expect to be able to find any information we want, when and how we want it. Data sources on nonprofit spending and on social investing are improving. Helping organizations collect and provide the data they need in order to meet the demands of these expectations and tools is one part of ZeroDivide’s work with its partners. ZeroDivide also needs to meet these new standards, and has experimented with new tools for information sharing, made changes in its governance practices, and is developing new measurement practices so that it fill its role in the chain of accountability from action to investor and back again.

The same drivers for accountability are also increasing demands for transparency. Here too the following look at ZeroDivide’s partners and its own ways of working offers useful insights. Greater sharing of information, more quickly, and in more readily accessible forms are only the

tips of the iceberg where greater transparency is concerned. For ZeroDivide, internal efforts at sharing knowledge more readily and rapidly resulted in the use of staff and consultant blogs, 360 review meetings, staff reflection and learning sessions, and increased communication between board and staff.

The demands of new measurement systems and calls for greater transparency will only succeed if there are useful, respectful working relationships between funders and community organizations. These cannot simply be willed into being. They do not emerge easily, instantly, or on demand. When ZeroDivide considered the new skills it would need in-house in order to redirect its work it chose to keep existing staff and train them in social enterprise, rather than bring on experts in social enterprise and help them build community relationships. This, more than anything else, demonstrates the recognition by ZeroDivide's leadership of the critical value that working relationships play between funder and organizations. This decision practically shouts out a core value, "everything else can be learned; but respect and commitment can only be earned."

### **The meaning of this moment**

Some are looking at this moment in philanthropy as a time of great tension – between rigor and humanity, head and heart, systems and soul. So many of our institutions – public and private – are in transition due to new financial pressures, global competition, and new government priorities that it would be shortsighted to expect philanthropy to be somehow exempt from major changes. During moments such as these it is tempting to either declare "all is new" or "nothing will change." The truth lies somewhere in the middle and will likely not be fully evident until several years in the future. In the meantime, while ZeroDivide, its partners, and other philanthropic organizations are undergoing these shifts, we hope their story, their challenges, successes and failures to date will be useful for others.

## **Introduction to ZeroDivide**

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In its work, ZeroDivide has been a leader of innovation on many fronts. Founded as the result of community advocacy work during the merger of Pacific Bell and SBC Communications, ZeroDivide was created as a community funding source to transform individuals and

communities through the power of information and communications technology. Known originally as the Community Technology Foundation of California, ZeroDivide has been one of a few foundations exclusively funding technology-related projects in communities to narrow the digital divide and ameliorate social inequities. The Foundation has spent almost \$50 million addressing these issues to-date.

In 2006, after eight years of operation and the looming spend-down of its corpus, ZeroDivide reflected on what it had learned from its grantmaking, took stock of social and economic trends, and reaffirmed its commitment that funding for the intersection of technology and social change remained an important gap to be filled. Nonetheless, the Foundation was no longer committed to the grantmaking strategies it had been using and felt that meeting its mission required a fresh approach. The foundation seized the opportunity to restructure its role within the larger philanthropic landscape to consider the potential of sustaining its own work and the work of its partners.

ZeroDivide moved forward on its belief that social enterprise represents a significant new opportunity to have an impact and asked Blueprint Research & Design to document the process thus far in its philanthropic restructuring. Over the past year and a half, Blueprint conducted interviews with grantees, ZeroDivide staff, board members, consultants and mentors and held internal “reflections sessions” with the foundation staff. This paper does not attempt to answer some of the more complex questions facing the sector. However, it does provide a window into one foundation’s experience of leveraging social enterprise tools for its grantees, enabling others who may be similarly restructuring to learn from ZeroDivide’s experience.

## **The Community Enterprise Concept**

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As a foundation charged with serving the public good, ZeroDivide could have taken various routes to meeting its mission. The menu of choices facing a funder interested in building a community’s access to capital include grantmaking , program-related investments (PRIs), mission-related investments (MRIs), funding social businesses or providing other forms of capital such as loans, secured debt, or guarantees. ZeroDivide intentionally chose to fund

nonprofits and their pursuit of social enterprise because they believed in building the capacity of the nonprofits whose missions leads them to serve their communities.

At the heart of ZeroDivide's shift toward community enterprise is the underlying belief that underserved communities can generate their own capital—new or enhanced businesses, jobs and enterprises—to improve social and economic conditions. By developing their own businesses and sources of capital, the hope is that communities can better sustain their local economies, withstand global market fluctuations, and be less dependent on the foundations that typically support them. Furthermore, by empowering communities, underserved populations can fulfill their desire to *create, produce* and *distribute* their own content and not just act as passive consumers of it. Also as a result of funding and nurturing community enterprises, ZeroDivide theorizes that policy and industry/market change would occur as community organizing and engagement with industry increase as a result of these enterprises.

ZeroDivide realized it could leverage its position as a foundation and its expertise in technology to supply “patient” capital for nonprofits. Providing wrap-around technical assistance and the opportunity to incubate enterprises that might have potential for scaling up and replicating for broader effect, the foundation decided to focus on community enterprises—enterprises that begin, germinate and then scale-up in communities. While there have been numerous discussions of *social enterprises*—nonprofit organizations that mix social responsibility with business ventures—the concept of *community enterprise* redefines who can be an entrepreneur and focuses on enhancing or mobilizing *community-based assets* for social change.

The times leading up to ZeroDivide's strategic shift were characterized by a general “can do” attitude about markets, innovation and capitalism, particularly in the Bay Area's welcoming environment to social enterprise and philanthropy. This optimism helped fuel the enthusiasm, and beginning in January 2007, ZeroDivide began the process of implementing these ideas.

## **Ramping Up**

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As a traditional grantmaking institution, ZeroDivide lacked the initial capacity and expertise to fund and manage community enterprises. In order to develop the necessary skill sets, the foundation decided to reconfigure its board, help train its staff, and integrate different departments into the new process.

The decision to invite new board members was fairly straightforward; to help guide the implementation of this new model, the foundation needed to recruit board members with direct social enterprise experience. Now venture capitalists, social entrepreneurs, corporate marketing executives and social enterprise CEOs sat together with the community activists that had historically comprised the board.

However, the decision to align its staff to be able to support social enterprise was more complicated. Essentially, ZeroDivide's managers had two choices: train existing staff or replace them. Going against what some might have recommended ZeroDivide did not replace its staff with "experts" in social enterprise. Instead, the foundation decided to prioritize keeping and retraining current staff members, who had strong connections with grantee communities and held deep knowledge about technology's power to transform underserved populations. The Foundation chose to "learn and do" simultaneously: training staff on how to be a community enterprise funder while simultaneously creating a new grant program and implementing a new program model. The Foundation hired a consultant with business start-up experience to work closely with grantees and staff and a former venture capitalist consultant to provide training to the staff.

## The Model

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### Making Grants

ZeroDivide's plan to support community enterprises was at its core an extension of its traditional grantmaking. Depending where the grantee fell on the spectrum of developing and implementing community enterprise, ZeroDivide offered funding within two major streams:

- **Big Bets.** Four large, multi-year grants ranging from \$450,000-\$1 million for a total foundation investment of \$2.6 million over two years. To ZeroDivide, the high risk/reward ventures of the Big Bets represented its best chance to demonstrate the community enterprise model. Selected from a pool of previously successful grantees, the Big Bets submitted proposals with clear social impact goals and models for financial sustainability.
- **Pipelines.** Thirteen smaller grants designed to seed and test ideas that might receive Big Bet funding in the future. These \$75,000 grants, selected through an open letter of inquiry, lasted over a 6-18 month timeframe and represented every stage of an enterprise lifecycle: from the idea phase to R&D to planning to implementation.

### 360° Ecosystem Support

ZeroDivide also provided wraparound technical assistance—known as 360° Ecosystem Support—as an important complement to its Big Bets and Pipeline grant programs. While the foundation offered 360° support to both Pipelines and Big Bets, the intensive one-on-one advanced support was primarily for the Big Bet enterprises. The plan of support featured:

- **Workshops and Conferences.** Shortly after making its first grants, ZeroDivide hosted an all-grantee, day-long workshop including topics on marketing, market research, legal issues, business planning, and sales. Throughout the grant period, the foundation also referred grantees to, and paid for their attendance at, other relevant workshops or conferences.
- **Mentoring.** A mentoring period for Big Bets followed, where ZeroDivide matched volunteer mentors with expertise in venture capital, marketing, executive recruiting, product development, finance, communications, and technology development with Big

Bets according to their 360° support plan. ZeroDivide introduced the match and then stepped back for the relationship to form. Based on a Pipeline needs assessment survey, Pipelines also received a mentoring period with a local technology consulting nonprofit. ZeroDivide brokered the mentoring arrangement and left it up to Pipelines to follow through on developing the relationship.

- **Business Planning.** As part of their grant agreement, each Big Bet needed to deliver a business plan outlining their business model, market analysis, competitive advantages, operations, social impacts, goals and benchmarks, and financials within six months. Big Bets, ZeroDivide staff, and consultants went back and forth through multiple iterations of their plans to reach agreement on a sustainable plan.
- **Pitching Training.** The 360° support year for the Big Bets culminated in sales pitches made at the first Social Capital Markets conference (SoCap 2008). ZeroDivide staff and consultants worked closely with each of the Big Bets to create and hone their four-minute pitches. The Big Bets presented their pitches to a diverse audience of venture capitalists, philanthropists, and others from the social enterprises community and a panel of venture capitalists provided feedback (the pitches are available as a podcast on <http://zerodivide.org/podcast>).

## e-Democracy Evolution

In developing the new grantmaking model, ZeroDivide created two program streams: Community Assets and e-Democracy. The Community Assets program design worked toward underserved communities having established enterprises that employ mobile, wireless and social media technology to promote the ideas, voices, and experiences of the underserved. The e-Democracy program goal is to increase the voices of underserved communities to achieve more engagement and influence in the public arena, via technology tools.

ZeroDivide's expectations for the e-Democracy enterprises were different from the start—they would be on a different timeline, they would not be selling a product or a service, and they would be analyzing different metrics of their success.

The challenge was that ZeroDivide didn't know what metrics were realistic or how an enterprise geared at building civic engagement might earn income. What makes it an enterprise as opposed to an e-Democracy project? ZeroDivide received very few e-Democracy proposals and ended up funding only 3 Pipeline grantees.

Today, ZeroDivide does not have an earned income requirement for e-Democracy grantees, but they are looking for organizations to create sustainability through diversification or new sources of funding. They will provide TA to their grantees to gain some kind of income along the way, either through increased visibility resulting in more members, more donations, or higher levels of donations. The enterprise in and of itself will most likely not be an income generating proposition.

One e-democracy grantee, **HOPE (Hispanas Organized for Political Equality)** developed web-based advocacy tools to increase the number of informed Latina voters, motivate them to become politically active and advocate, and increase the number of Latinas directly communicating with policymakers to impact state policy. Important metrics for them might include: whether they have much more active individual campaign; whether they've moved to a membership model; understanding where members subscribe; and gaining new source of revenue—donations, corporate sponsorships, pro bono opportunities.

To date, HOPE has found it challenging to diversify their income due to corporate and small business cutbacks. They have, however, seen a 6% increase in Latina voters increasing their participation, potentially leading to policy changes down the road, and at the very least setting up the infrastructure so that policy changes can be more immediately realized.

## Fast Forward: What Success Did the Big Bets See?

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The key successes ZeroDivide and its Big Bets realized after an initial round of enterprise funding are captured in the stories of two Big Bets below. For more details about each enterprise, please visit ZeroDivide’s website ([www.zerodivide.org](http://www.zerodivide.org)) to link to each organization’s website in its community investment portfolio.

### ***A Story of Ripple Effects and Positive Youth Outcomes: Youth Outlook***

Youth Outlook (YO!) is an umbrella youth media organization that houses YO!TV, YO!Radio, and four affiliated youth media projects (Debuge, The Beat Within, The Know, and Roaddawgz). YO! also podcasts and streams youth content directly from its website, [www.youthoutlook.org](http://www.youthoutlook.org). YO! trains and employs youth ages 14-25 in all aspects of its programs. YO!’s enterprise provides bundled advertising access on all its platforms to “old and new” media and advertising companies. They create and distribute youth generated content that influences opinions and moves policies.

#### **Youth Outlook: Annual Summary of Metrics**

- Gross revenue of almost \$150,000, which was 150% above projections
- Cost of goods/services plus other expenses exceeded projections by 200%
- The operating profit/loss was \$32,750
- The actual number of clients YO! trained and hired exceeded projections by over 100%.
- YO!’s new customer base exceeded projections by 60%.
- Trained 45 new youth

Unlike many foundations, ZeroDivide’s terms allowed YO! to use its Big Bet funds to purchase technology equipment. Their acquisition propelled them into the same class as all professional online content producers since now they had professional-grade equipment. And now they could pursue international stories because they had the right recording equipment. The investment funds also went to shoring up YO!’s marketing and sales department by hiring two

professionals, one of which was their first staff member solely dedicated to business management. Now the organization had someone who could broker YO!’s work with business opportunities for content providers, which gave the journalists, artists and creators more opportunities for growth and supplied YO! with more income.

For YO! the finely-tuned approach to its enterprise made it a more attractive funding opportunity for other private foundations and local government. The organization has been able to approach other funders with the same concept to ZeroDivide and secure additional funding for their enterprise. YO! was also awarded unexpected grant money from the San Francisco District Attorney's Office Back on Track Program to provide media skills to previously incarcerated youth.

YO! also reached a new cohort of youth through their new media platforms, from which they recruited young people to write and produce content. Young people write news stories for YO!'s website or print magazine on world affairs and politics, neighborhoods, lifestyle or school. Recent topics included "Will it Get Better? Young People Discuss America's Economic Woes," "Deportation Rips Family Apart—Moves Students to Organize," and "Incarcerated Youth Share Feelings on Slaying of Oakland Cops."

***A Story of Increased Confidence and Rapid Youth Impact: Change Agent***

Change Agent Productions (CAP), a program of the YMCA of Greater Long Beach, trains low-income, inner-city high school and college-age youth on digital and social media technology to promote positive youth development, enhanced academic success, and career readiness. Its enterprise offers video productions, graphic design, and digital media training at competitive

**Change Agent Productions:  
Annual Summary of Metrics**

- Earned \$110,000, over 250% increase over projections.
- Exceeded revenue in the first 6 months of operations.
- Cost of goods/services and other expenses exceeded projections by over \$90,000.
- The operating profit was \$17,500.
- Doubled their new customer projections
- Recruited over 100 minority youth artists and trained over 100 clients, also exceeding its projections.

prices to its target market of nonprofits, school districts, government entities, corporations, small businesses and foundations.

CAP had already been implementing aspects of its enterprise before the ZeroDivide grant. But CAP reports that the large levels of funding, the intensive 360° technical assistance, and the faith that ZeroDivide had in its enterprise to succeed gave the organization confidence to move forward with a renewed energy. This, combined with the

largely unrestricted funds removed the “crisis mode” mentality CAP, as a nonprofit, was accustomed to having and helped the organization really dig deep into their enterprise strategies. It also gave CAP confidence to move in new circles and pitch their enterprises to new audiences, with a sharper vision and a new level of confidence that CAP could actually compete as a business.

Meanwhile production and contracts were underway, making CAP busier than expected. More and more high school sites are adding training labs and asking CAP to set those up and train staff to use them. Referrals added up through their joint offering of AV services and conference brochure design. CAP had to add a new staff position to meet these demands.

All of this work is done by high school kids who, with intense energy, are getting paid for their talent and work, learning corporate-grade technology skills and workforce development skills such as taking their work seriously, presenting to an adult audience, getting to work on time, and coming across professionally. CAP’s independent evaluation has shown that its youth have higher GPAs, fewer absences, and higher leadership, technological and educational attitudes after their participation. Eighty percent (80%) of its youth who graduated high school attended college.

Within six months, CAP met its gross revenue projections for the year and by year end, CAP had earned an actual total of \$111,000 through 19 paid client projects.

**Summary: Key Successes**

- *Substantial increase in the organization’s confidence.* The Big Bets could carry out their enterprises with sharper vision because lots of staff, consultants and mentors were behind them.
- *The 360° support had the ripple effects of building the rest of the organization’s capacity.* The support and funding ended up building capacity throughout the entire organization, beyond the enterprise.

- *Leveraging additional capital and the potential for private individual capital.* The intense work that ZeroDivide did with the grantees left them in a stronger position for approaching other funders.
- *More youth involved in wider aspects of the organization.* The enterprises were able to serve more youth and serve them more intensively.
- *Three Big Bets made more money than they expected.* Most Big Bets exceeded their revenue projections, but did not make a profit.

## What Did it Take?

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ZeroDivide needed to work very differently—internally and with its grantees—than it had in the past. What did working differently feel like for ZeroDivide and its grantees, all of which had previous funding relationships with ZeroDivide? This section features stories that highlight the due diligence process, the culture change necessary for enterprise success, and the trade-offs that came with decision-making with a newly-trained staff.

### ***A Story of Due Diligence: ZeroDivide***

ZeroDivide had to overhaul its existing grantmaking processes to deploy this new model of community enterprise funding—the Foundation was determined to make its first new investments in the summer, only six months after adopting its new strategy. Like most traditional philanthropic funders, ZeroDivide had usually posted an announcement about its funding opportunities, applicants responded, and the staff sifted through proposals, using the typical criteria related to soundness of proposed idea, level of potential community impact, and organizational capacity to implement the proposal.

## **Building the Team**

Many analysts may have advised ZeroDivide to replace its staff with “experts” in social enterprise. ZeroDivide remains committed to its decision to train its current staff about social enterprise rather than bringing in such experts. At the same time, this decision did not come without its costs. Keeping existing staff allowed ZeroDivide to:

- Retain a culturally and ethnically diverse staff, which is rare in the field of social enterprise
- Keep a commitment to professionally develop its staff
- Build on the existing processes and internal dynamics of grantmaking
- Retain and strengthen the relationships it had with its grantees and communities which allowed for more honest business planning and problem solving

The challenges and costs associated with this decision included:

- A difficult first year, as staff simultaneously built their social enterprise skills and implemented its new grantmaking model
- Unevenness in the staff's understanding of social enterprise – the lexicon, the analytical tools available and how to use them
- Putting grantees in the middle as it had to broker technical assistance (TA) relationships for them
- Opportunity costs associated with staff participating in their own learning plans

## **Staffing a foundation for social enterprise**

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Now it was a different story. ZeroDivide needed to quickly develop more capacity in financial, technological, and marketing analysis. Staff scanned the field to find existing tools, checklists, or frameworks to help them figure out exactly how to assess proposals and help applicants create their community enterprises. Staff members admit in the beginning they were almost hesitant to share the Foundation's strategy with others in the field, since they knew so little about how to go about their work.

No other funder was working in ZeroDivide's niche of social enterprise, technology and underserved communities, so not finding any satisfactory tools during the scan, the Foundation created its own tools. The Foundation relied on internal resources and included its finance, communications and technology staff alongside its community investment officers to assess proposals, pose questions, and meet with organizations. They also learned from and

customized all that the field had to offer, including work from such ground breaking funders and REDF, Acumen Fund, and the Draper Richards Foundation. The staff was not used to pushing business and financial outcomes or market research as part of its work. Now it had to translate what had just been learned about social enterprise into digestible language for the organizations, which in many cases did not follow the jargon.

The “learning by doing” became taxing for staff, who all were trying out new roles and responsibilities in new job functions. Technology, finance and communications staff were not used to direct interactions with organizations, and no one knew whether all of the intensive one-on-one support would even lead to funding for the organizations they saw pouring significant time into applications. The high stakes—up to \$1 million for each Big Bet—added to the pressure.

The process was also demanding, intense, and periodically confusing for applicants. At the same time, grantees recognize that the process helped them refine their enterprises and build a trusting relationship with the Foundation, which in at least one case, proved to be critical later on.

For both the Foundation and applicants, the traditional power dynamics in grantmaking were somewhat inverted. Historically, the funders have the capital that grantees need to do their work. The funder is often seen as the expert, the one with the field-level view that can help grantees do better work. In ZeroDivide’s case, the new model put a different spin on this power dynamic. Though the Foundation still had the capital that the grantees needed, it was also learning alongside grantees how to do the work—the funder and the grantee were both undergoing a cultural shift simultaneously. ZeroDivide understood from its own experience what it was asking of its grantees.

The organizational culture shift necessary to become a successful enterprise might have been underestimated by both ZeroDivide and the grantees.

## **DUE DILIGENCE CHECKLIST**

When ZeroDivide conducted its due diligence, it did not have a standard set of criteria that Big Bet or Pipeline applicants had to meet to receive funding. The foundation believed it made overall good investment decisions, yet at the same time, this first year the staff already had relationships and some trust with the organizations, and in a handful of cases, this made it easier to use previous successes and relationships as criteria for funding.

Now, first and foremost, staff agree, are the readiness and willingness among potential grantees for culture change, clear social impact goals, and strong financial management systems. Here are the other categories of analysis that staff currently use during its due diligence process.

### **Planning and Development Activities**

- Parent organization embraces a culture of social enterprise and sees venture as core component of agency strategy/mission
- Has developed a clear and focused business model for the venture
- Has completed thorough market research regarding the proposed product or service
- Has identified and contacted additional investors for venture
- Has completed a social venture business plan, including a marketing plan and 3 year budget/revenue projection

### **Operational Activities**

- Has fully developed and tested its product or service among target audience
- Operational infrastructure (financial & accounting, business contracts, etc.) in place
- Has identified appropriate staffing team to run the business (not just re-purposed staff)

### ***A Story of Culture Change: Youth Radio***

Youth Radio trains underserved youth in multimedia production, helping them develop technical and professional skills and bringing awareness of youth issues to a general audience. It provides intensive, free, after school media training and broadcast journalism education to over 400 low-income and youth of color annually. To date, Youth Radio has distributed content to major national media outlets such as National Public Radio and CNN.com. Youth Radio plans to expand its operation from a high-end youth development and media production company to a national aggregator and curator of youth-created content. Youth Radio's enterprise, Youth Media International, distributes youth-created content that generates advertising and sponsorship revenue.

Like all of the Big Bets, Youth Radio had to maintain its mission focus while developing crystal clear revenue generation strategies. It quickly was immersed in the new culture of business models and social enterprise—even before it had received any grant funds from ZeroDivide. At this stage Youth Radio had to narrow focus from five potential revenue streams to just two,

which was a difficult decision when all five had potential, and some had sustained the organization to date. Youth Radio had never used the terms “break-even point” or “strategic investor” before, and it took a while until staff felt comfortable throwing around these terms in their conversations.

The organization also spent significant time developing market research for its business plan. While Youth Radio was used to describing the “problem” that existed for the youth they served and how they would “solve” it, now the organization had to articulate the *market* problem. They had to answer questions such as, “How are people consuming youth generated content today? What platforms do they use to access it? When will they and won’t they pay for it? What areas are showing growth? Contracting? How is the economy affecting media consumption, and how do we position ourselves to take advantage where there’s opportunity? What are the risks and how do we outsmart them?” In addition they had to conduct a hard competitive analysis. Youth Radio could no longer simply list the other youth media organizations and how they were different, but now had to add another layer of analysis: “Why is a young person going to come to our content as opposed to YouTube or MTV or CurrentTV or BET?” Struggling through and answering all of these questions would help Youth Radio make the case that organizations would become partner/sponsors and help them generate revenue.

**Youth Radio: Annual Summary of Metrics**

- Gross Revenue over target
- Cost of Goods/Services Sold slightly lower than projected
- Operating margin better than projected
- Four new contracts, growth in broadcast, print and online audiences
- Over 12,000 hours of youth producer-editors creating digital media
- 100% of graduating seniors enrolled with Youth Radio accepted to college

Youth Radio also was challenged in switching from nonprofit accounting to business accounting. Before, all of its incoming flows were “grants.” Now depending on the purpose and source, incoming flows have the potential to be labeled “income,” “earned revenue,” “capital infusion,” or a “grant.” Youth Radio has had to learn how to negotiate all of these terms with its contractors as well as sift back through contracts to pull out what was monetized for content. They have also had to learn how to calculate the cost of goods sold, the true costs of production. As a nonprofit receiving foundation dollars, this goes against the traditional culture of showing a balanced bottom line and naming the success factors pertaining to the venture, all within the terms of the grant, usually one year.

Youth Radio also was in the position of reframing its relationships as fellow “journalists” became “clients.” This took significant cultivation as long-term relationships, contractual terms and costs needed to be renegotiated—and the organization was also not used to negotiating with corporate entities. Youth Radio was now sitting at the table with NPR (and other clients) and presenting opportunities in true partnership form to major sponsors. After its first year, Youth Radio surpassed its goal and earned over \$80,000.

***A Story of Trust: BAVC***

Bay Area Video Coalition (BAVC) is a media arts center that engages independent media makers, underrepresented groups, and nonprofit organizations in media creation and innovation. Its enterprise is utilizing a high-speed fiber network to transform its in-person technology training programs into an online format. The goal is to expand the market base for these state-of-the art training services and build a profitable online enterprise.

During the application process, BAVC appreciated the candid questions from all of the different ZeroDivide staff departments and found the process critical to refining its enterprise. At the same time, the organization sensed that the process did not reflect the “real world” business investment, mainly due to the collegial relationship the organizations retained from the past and the sense that the decision making was based more on subjective than objective criteria. For its part, ZeroDivide now recognizes that it did not know enough at the time to ask all of the right questions or to be able to foresee how some of BAVC’s operating systems would eventually hinder its enterprise implementation.

For the last couple of years, BAVC has seen its net revenue from training classes steadily decline as technology and other expenses have become more expensive. As a cutting edge media arts center, it’s critical that BAVC has the most up to date, state of the art technology. In addition, a significant portion of BAVC’s revenue income comes from state contracts, which are paid on a reimbursement basis, which forces BAVC to absorb training costs until they are reimbursed. To fill the gaps until it is reimbursed, BAVC focused on increasing training revenue and then struggled with narrowing and focusing on only one revenue stream, and thus

completing its business plan. To help BAVC finish its plan, ZeroDivide provided a grant for a business consultant who helped BAVC make the strategic decision to go deep with the one business line.

Meanwhile, the organization continued to struggle financially in part due to the shifts in the economy, including the tightening of loans and credit that were previously available to BAVC. The problems exacerbated until BAVC was forced to approach its most trusted funders. ZeroDivide (along with two other key funders) decided to help the organization weather this storm, and just over a third of its grant funds were diverted from the enterprise to the organization's general operations. For ZeroDivide, this meant that BAVC suspended its enterprise development to address the immediate operational life of its organization. But BAVC's work during this time has served to position the organization for growth. In a striking parallel to the current banking crisis, BAVC held on to its highest performing assets and had to divest from those that were underperforming.

BAVC and ZeroDivide agree that their strong historical relationship, (continued because ZeroDivide kept its existing staff) was the primary reason BAVC could approach the Foundation with an honest assessment of its situation. While the story is not yet over, BAVC's enterprise is aligned with its strongest asset and ZeroDivide continues to help the organization assess financial and organizational performance measures to monitor progress in an ongoing way.

BAVC's work with an outside business planner, funded by ZeroDivide, was deeply important to the continued planning of the initially funded project. Since developing that initial plan, BAVC went on to receive a grant from the Taproot Foundation that provides for deeper and broader planning in support of online class offerings. BAVC has now developed two prototype classes based on an assessment of the field and the initial business plan, and is sharing these prototypes with potential partner and funders. The organization plans to complete at least three online classes by the close of 2009. ZeroDivide's funding remains the critical support that allowed BAVC to reach this stage in online course development.

### **What did it Take? Key Lessons**

- *Keeping and training existing staff can pay off, but has trade-offs.* This work can be done without social enterprise “experts,” but it will likely not be smooth in the beginning.
- *Required culture shift comes with unanticipated intensity.* And the culture shift comes for both the grantee and funder.
- *Start the 360° TA support before the grant is made.* A high level of technical assistance is required for the grantees to develop their enterprise proposals, to prepare them for the work ahead. Thus there is an intensive due diligence process for both funder and grantee.
- *Develop clear criteria for decision-making.* Especially where historical relationships exist, it is easy to fall back on trust and subjective knowledge in the absence of clearer decision-making criteria.

### **Beyond the Grant: 360° Technical Assistance Support**

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Particularly for the Big Bets, ZeroDivide’s new grantmaking model needed lots of support and work after the grant check was distributed. With its intensive high-stakes, high-touch funding model, ZeroDivide arguably had a greater interest than usual in seeing its grantees’ enterprises succeed. Beyond the grant, ZeroDivide offered 360° technical assistance support that would ultimately get the grantees ready for the next level of funding. The stories below feature ZeroDivide’s experience and a composite profile of the Big Bets’ reactions to the support.

#### **ZeroDivide’s Experience**

No one at ZeroDivide sat back to wait for progress reports to come in. The 360° team had assessed the risks and rewards associated with each grantee, identified the additional needs the enterprises would require for success, and together with the grantees developed a customized 360° plan of support to be implemented during the Big Bet grant period. Once the grant was awarded the TA support commitment amplified and needed to draw in outside expertise.

While the support plans were customized, much of the formal assistance offered was standardized training, and grantees took from it what they most needed. ZeroDivide also offered high quality consultant presentations at workshops and conferences and trained everyone to deliver a pitch to venture capitalists and philanthropists at a Social Capital Markets conference.

One exception to the standard support was the mentoring period, which matched the Big Bets with a mentor who had necessary expertise to meet their TA requirements. Here ZeroDivide envisioned a consulting relationship that would allow the enterprises access to experts who had first-hand experience in getting enterprises off the ground, provide a forum to react to ideas, and leave the Big Bets poised for the next level of implementation.

For some Big Bets, the mentoring provided the high level of support needed, and everyone involved agreed that ZeroDivide lined up high-caliber mentors. The problem was that the unanticipated business planning process left each Big Bet at different developmental stages in their enterprise pursuits. Not everyone was ready for the mentor for the prescribed period of time the mentors were available.

ZeroDivide now realizes that an unanticipated potential benefit of the mentoring relationship would be in helping the enterprises think about their next level of funding. The mentoring may have been one more avenue to help get the grantees in the door to have those conversations, as grantees would be introduced to venture capitalists or others with wider connections than ZeroDivide.

Upon embarking on its new model, ZeroDivide did not create an “exit strategy” to implement with the Big Bets. It did begin its work envisioning that the grantees should leverage the next level of funding on their own, as in a traditional venture capital/venture relationship. Big Bets developed business plans that projected three years out. For grantees to meet their long-term goals, they require the same committed level of funding in the future that ZeroDivide provided

during the launch stage. However, ZeroDivide's self-identified role is that of a venture/launch funder, and not a sustaining funder.

ZeroDivide realized that it needed to more intentionally prepare Big Bets for the next level of funding after having demonstrated that their business models work. While the Big Bet itself will ultimately be responsible for the leveraging, ZeroDivide's charge is to look at the organization as a whole, help it figure out the appropriate proportions of financial and social impact, help them pitch on their own, and plan an exit strategy that will include matching and introducing Big Bets to a broader array of philanthropic and donor networks.

### ***The Big Bets' Perspective***

Among the Big Bets, many felt they simply weren't ready to access the mentors. Mostly the timing wasn't right in their business plan cycle, because they were busy doing things such as hiring and training new staff for their enterprises. For some, there was not a clear understanding of how exactly mentors could be used to their greatest advantage. Since there was a time limit, the opportunity passed by them without their benefitting to the fullest extent from the available expertise.

At the same time, of all the 360° support ZeroDivide offered, the Big Bets found third-party support aimed at a general audience such as workshops and conferences least helpful—at least in this phase of their enterprise development.

What was most highly valued by the Big Bets (and the Pipelines) was ZeroDivide's customized, hands-on training and direct, one-on-one advising from staff, consultants, and mentors. These also were the most time and resource intensive for ZeroDivide. The every-day interaction, support and work from the foundation and its consultants and mentors allowed the enterprises their biggest successes. As one Big Bet reported, their enterprise didn't know what they didn't know. The greatest value was to have outsiders ask questions the organization wouldn't think to ask itself and to reinforce the language of business development and not nonprofit development.

At this point the Big Bets need and want ZeroDivide's help introducing them to other social enterprise funders. As long as they remain nonprofits, they will not attract venture capitalist funding, but the enterprises are attractive to other foundations or individual philanthropists interested in helping nonprofits develop their double or triple bottom line. Some of the enterprises also are debating whether or not to spin-off as for-profit enterprises and could use some assistance in evaluating the trade-offs, advantages and disadvantages to this option.

### ***Beyond the Grant: Key Lessons***

- *Implement More Customized 360° Support.* The TA support provided to the grantees must be highly targeted, continue throughout the grant and begin even before the grant is made.
- *The Foundation has a Role to Prepare Grantees for the Next Level of Funding.* The foundation cannot step back after its investment even though that's how venture capitalists operate. These are unique investments and the foundation must further the success of its investments by making connections between funders and enterprises—whether the enterprise remains a nonprofit or not.

### **Timelines and Expectations**

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ZeroDivide expected that after a year, it would be able to prove its new program model—that nonprofit social enterprises benefiting their communities would be able to partially sustain themselves by earning income on their products and services. At the outset of their grants, the Big Bets would complete their business plan and begin implementation, while the Pipelines would refine their ideas, research and development and become primed for Big Bet eligibility.

The following stories feature some of the results of the Big Bet business planning process and their path toward earning revenue as well as ZeroDivide's refined timeline and expectations.

***A Story of Business Planning and Building Sustainability: Change Agent***

As part of a very large nonprofit with a goal-oriented culture, Change Agent Productions (CAP) believed it was already used to thinking in enterprise terms. At the same time, it found completing the business plan challenging and time consuming. Through the process CAP learned that it needed to improve its management of the business aspects of its enterprise and really sharpen its financial management skills, including clarifying and accounting for different lines of business, separating business revenue from grant revenue and understanding its true costs per job. This was tricky, as CAP is part of a larger organization that provides administrative infrastructure. CAP had also not thought about the creative-content legal aspects of its work before, and this introduced an entirely new learning stream for the production house. For example, who gets the creative license when CAP is working with third-party clients? How can CAP use the product it created for a client to market itself? CAP also had to become well-versed in creating its contracts and learning the new legal terminology that this required.

All of these challenges held back formation of CAP's business plan by three months, longer than both CAP and ZeroDivide had anticipated. CAP was ready to move forward with implementation and found the constant back and forth with ZeroDivide on finalizing the business plan frustrating—that at a point the details of the plan were getting in the way of getting the work done. At the same time CAP knew the process was giving them a language to work with and asking questions that helped CAP create a better business.

Eventually CAP did get both the business plan and its enterprise-related work done. In its first year of enterprise implementation, CAP exceeded its revenue projections by over 300%, meeting its revenue goals in its first six months of operation. CAP seems to be in a good position to attract greater resources based on the success of its business model – the organization has been able to demonstrate that it has a viable product that is attractive to a niche market at a competitive (below market) price. Transitioning from a complete subsidy model to a flow of income, CAP has already been able to demonstrate that a percentage of income will allow it to be more self-sustainable into the future (economic conditions notwithstanding).

**Big Bet Metrics Dashboard**

Each Big Bet creates their own “dashboard” of metrics it will follow through its enterprise. While the specific business and social metrics may vary from grantee to grantee (examples below), they all track similar financial metrics.

Standard Financial Metrics – Big Bets

Gross Revenue  
-Cost of Goods/Services Sold  
-Other Expenses  
=Operating Profit or (Loss)  
Operating Margin  
New Grants for Business

Sample Business Metrics- Big Bets

New customers  
Number of repeat customers  
Size of new contracts  
Number of hits/page views on website  
Number of podcast downloads  
Number of community comments generated  
Number of youth participating in election coverage

Sample Social Metrics – Big Bets

Number of clients trained/hired  
Number of youth receiving individual college/career counseling  
Number of youth attending college  
Number of youth trained in digital media and technology skills

And CAP will be satisfied that its model continues to require subsidies. CAP strongly believes that there’s a unique niche for nonprofit social enterprises that will use its earned income streams to leverage foundation funding to benefit underserved youth. CAP does not see that happening with a pure for-profit model.

***A Story of Business Planning and Revenue Generation: Youth Outlook Profile***

Youth Outlook (YO!) is the umbrella organization that houses YOUTHOUTLOOK.org, YO!TV, YO!Radio, and four AFFILIATED YOUTH MEDIA PROJECTS (Debug, The Beat Within, THE KNOW and ROADDAWGZ) with a national distribution of 20,000

Youth Outlook (YO!)’s business planning was also delayed until well into the grant period. Similar to CAP, YO! is a subsidiary of a larger nonprofit media parent company. This made calculating its true costs challenging and time consuming as YO! had to separate out all of its costs from the parent organization. In addition, planning and the 360° assessment from ZeroDivide revealed a need for hiring a permanent marketing team, which took longer to fill than anticipated.

Support from YO!'s parent company was necessary to bring its enterprise to life, and because of the changing culture at YO!, after a while this became a challenge. YO!'s parent company provides overhead and back office support, and its methods of financial accounting no longer aligned with YO!'s needs. In addition, the parent company and YO! shared staff, and generating the enterprise turned out to take much more staff time than anyone had anticipated, creating tensions about management and responsibilities. YO! and its parent company had to spend some dedicated time hammering out the tensions and coming to mutual understandings about working together so that each entity's goals could be met.

**Assessing Social Enterprise Readiness**

ZeroDivide now assesses its Pipeline grantees along these benchmarks.

Business Benchmarks--Pipelines

- Product or service fully developed
- Business model developed
- Product or service tested in marketplace
- Marketing plan developed
- Identified appropriate staffing for enterprise
- Organizational culture supports enterprise
- Financial and other management systems/processes support enterprise
- New funds leveraged
- New partnerships

Social Benchmarks—Pipelines

- Social metrics identified
- Met intended social outcomes

Technology Benchmarks—Pipelines

- Successful technology implementation

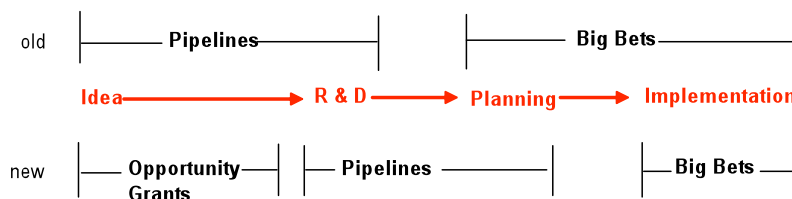
YO!, like all of the Big Bets, came to realize that the business plan is a living document and will continually be updated as unknowns and projections become hard numbers and reality. YO! found that its original projections were unrealistic and that it had to pay much more for market research metrics than it had anticipated. YO! was also awarded unexpected grant money from the SAN FRANCISCO DISTRICT ATTORNEY'S OFFICE BACK ON TRACK PROGRAM to provide media skills to previously incarcerated youth.

These unexpected costs notwithstanding, YO! earned more revenue than anticipated, mostly from contracts and partnerships, rather than selling ads and sponsorships for its distribution platforms, although it did not turn a profit this first year. YO!'s income generating plan moving forward includes increased earned income from its ads, newly-structured sponsorship levels, contracts and partnerships, and also includes additional foundation support.

### **A Funder’s Expectations—ZeroDivide**

For ZeroDivide, The Big Bets’ successes give hints that their program model has the right assumptions—that community enterprises can at least partially financially sustain themselves by earning income from technology-based products and services and at the same time have an impact in communities. The financial sustainability aspect of ZeroDivide’s program model has been the one most widely questioned—ZeroDivide staff, supporters and skeptics have all posed the question of whether these enterprises can or should be fully financially self-sustaining. ZeroDivide did not begin this work assuming that the enterprises would become 100% financially sustainable; the foundation expected some level of subsidy for the enterprises, although exactly what level was not clear and not commonly agreed upon among staff. The inaugural year of grantmaking has told ZeroDivide that it can indeed work with enterprises to prove their market and their product and get them to a place to attract greater resources.

In the first round of funding, ZeroDivide also expected to include an initial few months of business planning for the Big Bets, after which they could launch their enterprises. And they had anticipated that after an initial round of funding the Pipelines would be in a position to launch as Big Bets. After a year, neither the Pipelines nor the Big Bets were as far along in their social enterprise implementation as ZeroDivide (and the grantees) thought they might be. Business planning ended up taking a significant part of the year and took everyone longer than originally anticipated. No one had fully anticipated the time that the market research and analysis would take, or the time it would take getting all the organizations up to speed on the financial concepts necessary to write the plan.



In future efforts, ZeroDivide will move the business planning process and researching and testing the market phases to Pipeline grants; the business plan will be a deliverable for eligibility

for Big Bet funding. What had been Pipeline grantees will now be funded through an Opportunity Fund.

***Timelines and Expectations: Key Lessons***

- *One Year is Too Soon to Prove the Program Model, but There Are Hints of Success.* A social enterprise funder should have realistic expectations about when to see strong evidence of enterprise financial sustainability, changes in the market place or changes in community indicators.
- *It's Not Realistic to Expect 100% Financial Sustainability.* Full sustainability absent any subsidy should not be the goal of social enterprise funding. Rather, the more important questions are to what extent, and how quickly a community enterprise can move from a 100% subsidy model to at least partial sustainability? What share of revenue can be expected to be earned income?
- *Business Planning Should be a Longer-Term Focus.* Too many elements along the learning curve for nonprofits warrant extended time and focus on market research and creating business plans.

**Conclusion**

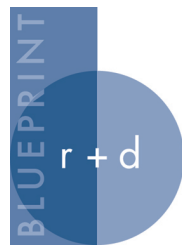
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ZeroDivide's strategic shift was game-changing: everything about the way the Foundation operated changed. After its inaugural year, however, ZeroDivide has established a solid platform upon which to build and will continue to fund nonprofit social enterprises. Unlike many in the field who are agnostic about where the enterprise resides, ZeroDivide posits that nonprofit community enterprises contribute unique value. They are assets in communities that are often overlooked and not adequately capitalized in ways that will develop, highlight and strengthen community assets.

Many questions of the social enterprise movement remain unanswered since its emergence. How, specifically, are social enterprises distinct from and more advantageous than traditional nonprofits and for-profits? As a grantmaker and as an entrepreneur, when would you select a

social enterprise in lieu of a nonprofit or for-profit? What are the right metrics for measuring social enterprise performance? Currently, adding to this list of questions is a tempered optimism for the idea that markets and capitalism hold the ability to transform communities. How will our current economic times impact philanthropists' ability and enthusiasm to fund social enterprise?

Finally, whether the larger field will take advantage of the opportunity to restructure itself is a timely and important question. As many have noted, social enterprises often face significant barriers in funding despite their successes in the community, and the growth in the practice of and knowledge surrounding the field of social enterprise seems to be too significant to be simply ignored.



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