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Charity Ratings Kill Innovation

By Phillip Haid

This may be blasphemy but I am going to say it. Charity ratings help to kill innovation.

Now before the charity ratings organizations go crazy and tell me how wrong I am, let me acknowledge a few things.

I am not against charity ratings. They play a valuable role in terms of evaluating efficiency, accountability and transparency. But they seem too focused on expense ratios and not enough on impact. If an organization's program spending relative to their operating spending is 70/30 but has a huge impact on health care or climate change, is that worthy of a lower rating to another organization that has an 85/15 ratio but far less impact?

But let's leave this argument for another time.

My problem with charity ratings is that by focusing on the relative spend between mission (program) and operating, charities are reluctant (some are even scared) to spend money on innovating the way they engage the public.

The vast majority of charities innovate around their program delivery because it's core to mission and it goes to the right side of the expense ledger. But not so when it comes to public engagement and mobilization. It is seen as a pure cost (operating expense) and they are therefore afraid to try new ways to raise money, engage volunteers or advocate, because if the innovation fails (as many do) their positive ratio will be affected, impacting their rating.

The problem with focusing on program to expense ratios is two-fold. One, it separates the raising of money from mission and I strongly believe that for non-profits to scale, money and mission have to be integrated. Second, worrying about ratios kills the desire to be first, and try new things that could engage new audiences in your cause.

Companies are constantly innovating and taking risks. Standing pat is not an option if you want to stay on top. This is obvious when you look at the change in top companies (based on market capitalization) over the past 20 years. But the same cannot be said for the charitable sector. The top charities in the U.S. (based on total assets) over the past 20 years are the same ones that were on top 30 years prior.

What this shows is that there is a lack of innovation in the non-profit sector because it is (a) very easy to enter the sector (no barrier to entry) but very difficult to scale, and (b) no one is willing to take sizeable risks that could significantly accelerate growth because 2 to 5 percent annual growth is safer and preferred.

So what are some possible solutions?

One is to widen the rating system by focusing more on impact and providing a bonus score for organizations that take calculated risks in both their programs and public engagement.

Another possible solution is to start cultivating a culture of risk-taking within the charitable sector by encouraging the boards and senior staff of non-profits and charities to allocate 5 percent (or more) of their budget to innovating the way they raise money and engage volunteers.

The more charitable organizations are willing to try new forms of engagement, test their efficacy, admit failure and learn from mistakes as well as successes, the better off they and the entire sector will be. Because the current model isn't getting us far enough, fast enough.

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