Venture Philanthropy – Possibilities for Swiss foundations to release more seed capital

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Due to the economic crisis, less seed capital is released in Switzerland as well as in other countries. The third sector and the civil society are challenged to fill in this gap. This commitment allows them not to limit their work to largely charitable work and service delivery, but rather to take care of duties and responsibilities which previously were assumed by entrepreneurs.

This study analyzes the possibilities for the Swiss foundation sector as part of the third sector to increase the release of seed capital. The aim of this study is to demonstrate that venture philanthropy may help foundations in this context. It highlights the chances and risks of such behavior of foundations. The results of this research may be taken as a starting point for similar developments in other countries.

The study is based on theoretical considerations from literature reviews and the analysis of Swiss law. It is an interdisciplinary paper where legal and economical aspects are taken into account. Foreign approaches and solutions will be considered. The study is completed with interviews of foundations.

The article of Letts et. al. “Virtuous Capital: What Foundations Can Learn From Venture Capitalists”\(^1\) is taken as basis of this study. Letts et. al. compared the differences in how venture capitalists interact with their start-ups and how foundations work with their NPO. These differences can be taken as the starting point for a process of reflection and change in the foundation sector. The analysis is based on these differences (risk management, performance measure, closeness of relationship, amount of funding, length of relationship and exit). Subsequently it is presented if and how foundations can implement these demands under Swiss law.

Risk management

Foundations are requested to change their risk management. Therefore foundations should act more like entrepreneurs, i.e. more efficiently, effectively and professionally. The revision of the Swiss foundation law (in force since 1 January 2006) implemented some entrepreneurial elements. On one hand, a founder may request for modification of purpose according to 86a Swiss Civil Code. On the other hand, new regulations regarding the audit (art 83b et seq. Swiss Civil Code) came into effect. As for all legal forms the same audit rules apply, the gap between foundations and businesses diminished. Private codes like the Swiss Foundation Code\(^2\) recommend to foundations to realize their mission in a more effective and entrepreneurial way. There exist foundations which impose on themselves in the statutes those recommendations.

Performance measure

Foundations should not only support programs, but also the organization of the NPO they support. The qualification of those costs as project costs or administrative costs depends on


\(^2\) The Swiss Foundation Code was edited by SwissFoundations, the association for grant-making foundations in Switzerland (for information see http://www.swissfoundations.ch/en/portrait/swiss-foundation-code.html).
the applicable rules. Hence the ratio between program costs and administrative cost may vary.

Closeness of relationship

Foundations are invited to offer a range of noncash, value-added assistance (e.g. take one or more seats on the company’s board to help shape strategy, extensive coaching and mentoring of the start-up’s senior manager, involvement in critical hiring decisions). Thereby it should be observed that the foundation does not gain too much influence on the management of the supported NPO. If a foundation influences the shaping of the strategy too much, the foundation may become liable as factual organ of the supported NPO.

Amount of funding

As foundations have only a limited amount of money to support NPO, they should concentrate on a smaller number of NPO. In doing so, the question arises if only the best NPO should be supported. Such a behavior may come in conflict with the common opinion in the NPO-world that not only the fittest should survive.

Length of relationship

Foundations should expand their grant-making time horizon to five to seven years. As in Swiss foundation law, the maintenance of assets has to be observed, a foundation may not fulfill its perennial obligation if no revenues are generated. Therefore the contract with the NPO should contain a condition that grants are only paid out if revenues are generated. Otherwise the founder has the possibility to determine in the foundation statutes that the foundation assets may be spent down.

Exit

Foundations should give grants with the understanding that the grants run out one day and the NPO should become self-sustainable. Some authors have the opinion that there exists no exit in the NPO-world as there are no investments. In this context it is discussed if mission-related investments of foundations are possible under Swiss law.

Conclusion: Foundations under Swiss law may meet some of the demands of Letts et. al. and therefore act as venture philanthropists. Thereby more seed capital can be released which is extremely important in time of economic crisis where entrepreneurs are less investing. In acting so, foundations should be aware that they are facing some risks (e.g. to become liable if they become too involved with the NPO). Provisions must be in the foundation statutes to implement certain venture philanthropy principles (e.g. the possibility to spend the foundation assets down). In applying venture philanthropy principles, Swiss foundations have not only the chance to overcome the economical crisis but also to realize its mission in a more effective way. The results of this study may make a contribution to the discussion of similar developments in other countries.

E.g. the rules of the foundation ZEWO to calculate the administrative costs: Methodik zur Berechnung des administrativen Aufwands, Die Einnahmen- und Kostenstruktur gemeinnütziger Organisationen, 2008 (http://www.zewo.ch/pdf/methodik_d.pdf).