

# Using DISCRETION

**What exactly are trustee discretionary grants?**

**BY LEE DRAPER**

**Who gives them? How are they used? What are the advantages and disadvantages of allocating these types of grants?**

**Here are some answers.**

**A**ccording to the Council on Foundations, approximately 26 percent of grantmakers permit board members to allocate discretionary grants (Foundation Management Series, *Governing Boards*, Vol. II, 10th Edition, 2002). Family foundations are more likely than other types of grantmakers to allow such allocations (48 percent). And the practice appears to be on the rise: The 2001 rate is a 5 percentage point increase from the 1999 survey (Foundation Management Series, *Governing Boards*, Vol. II, 9th Edition, 2002) and a 9 percentage point increase from the 1997 survey (8th Edition), when only 38 percent of family foundations provided discretionary grants to their trustees. (Please see the sidebars, pages 40 and 43, for a definition of discretionary grants and more statistical information.)

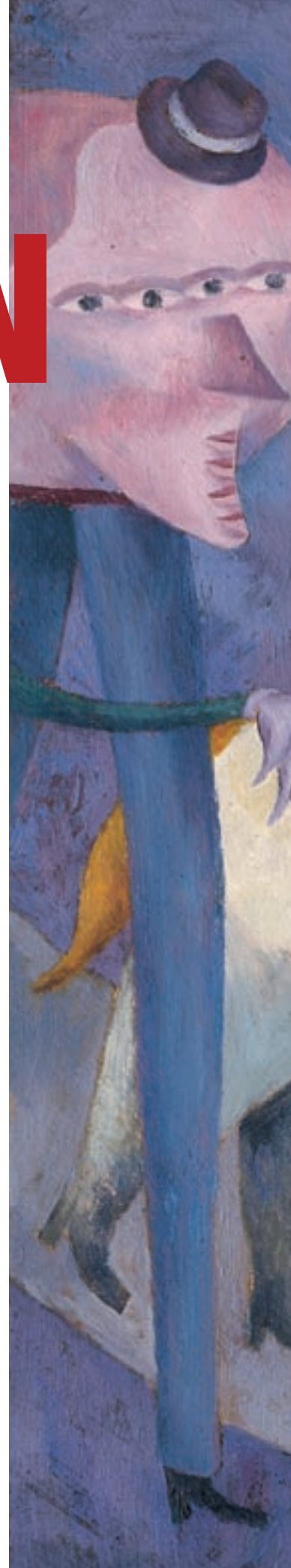
Like most grantmaking strategies, discretionary grants can have both advantages and disadvantages. Let's examine the benefits of using discretionary grants and also identify where they can dilute or even thwart philanthropic impact. How well do they work in bringing different or geographically dispersed family members together? Do they really stimulate long-term interest in philanthropy? Do they ease conflicts or can they create new ones within a family foundation? And what best practices for developing a discretionary grants program should a foundation consider?

## **The Brighter Side**

**Engaging new members.** Discretionary grants are often cited as a training tool for new board members. Serving on a foundation board can be overwhelming at first for many, whether they are family members or are appointed to a private or corporate foundation. Being able to make grants early in their board tenure is intended to provide board members with practical experience, as well as a taste of the meaning of grantmaking.

A recent article in the *Chronicle of Philanthropy*, "Nurturing the Next Generation" (August 7, 2003), recounts how The Nord Family Foundation in Amherst, Ohio, started a discretionary grants program six years ago to develop the grantmaking interests of heirs ([www.nordff.org](http://www.nordff.org)). Although the individual board members choose the organizations to which they would like to award grants from their discretionary accounts, they must take a number of steps in order to complete the process. Thus, each of those new grantmakers gains first-hand experience in conducting site visits, attending board meetings and determining the merits and appropriate amounts of grants.

ILLUSTRATION BY FERRUCCIO SARDELLA



# Defining Discretionary Grants

## Council on Foundations:

Grant funds distributed at the discretion of one or more board members, which usually do not require prior approval by the full board of directors. The governing board can delegate discretionary authority to staff—for example, to respond to emergencies that arise in the community that cannot wait for the next board meeting.

## National Center for Family Philanthropy:

Grants made at the discretion of individual trustees or other authorized individuals, without the standard approval process and/or review by the full board. (“Discretionary Grants: Encouraging Participation...or Dividing Families?” *Passages*, V3.2, [www.ncfg.org/publications-passages.html](http://www.ncfg.org/publications-passages.html).)



The Lumpkin Family Foundation in Mattoon, Illinois, has a similar program—the Sixth Generation Program—designed to introduce young family members to the work of the foundation ([www.lumpkinfoundation.org](http://www.lumpkinfoundation.org)). It encourages members of the upcoming generation who are at least ten years old to recommend two or three nonprofit organizations in their home community for grants. The family member has to research the organizations, complete an application and make a presentation to other family members. Executive Director Bruce Karmazin describes the program as an excellent method not only for teaching the next generation about philanthropy and becoming involved in their communities, but also for bringing the entire family together. Parents, children, cousins and other relatives have developed deeper connections with each other through exploring their personal interests in their communities.

**Connecting geographically dispersed trustees.** As families become larger and members move beyond a family foundation’s original hometown or region, connecting family trustees to the needs of a community where they might never have lived becomes increasingly difficult. Allowing geographically dispersed trustees to allocate discretionary grants where they now reside lets them apply the foundation’s mission, purpose and goals to their own communities and see at close range the impact of foundation grants. They can draw parallels and sustain their commitment to the foundation’s core work.

The Lumpkin Family Foundation found that its discretionary grants program was successful in just this way. Many fifth and sixth generation members—none of whom live in rural east central Illinois where the foundation directs the majority of its grantmaking—are very engaged in the foundation’s work, partly because they can direct grants to their local regions.

**Leveling the playing field.** As generations extend beyond the original donors, family branches can have very different levels of personal wealth. When one side of the family has a strong asset base while another branch does not, tensions may arise. This disparity is exacerbated when the community associates the family name with active involvement in philanthropic giving and expects all family members to be equally

generous. The challenges of varying financial situations can hinder the philanthropic process. Some family foundations have found that a discretionary grants program can help less well-off family members feel like they have an equal voice at the table. Discretionary grantmaking can defuse competition and enable extended families to engage in personal philanthropy at a level they might not have explored on their own.

**Recognizing volunteer service to the foundation.** Some foundations use discretionary grantmaking funds as compensation in lieu of direct financial payment for serving on a foundation board. For example, a founding donor may want to acknowledge the involvement of nonfamily trustees by giving them the ability to award grants on their own.

At the John Gogian Family Foundation, the founder will provide a discretionary grant fund in 2004 as a way to transition the trustees away from direct compensation (however, both direct compensation and discretionary grants will be phased out within two years). Discretionary grants have been used to recognize the personal sacrifices that family members might make to stay actively involved in the foundation, such as traveling long distances to attend the board meetings.

**Exploring new ideas.** The Nathan Cummings Foundation in New York uses discretionary grants not only to bring the family together in service to the community, but also as a method to test new interest areas and opportunities. Having more eyes and ears in the field can enable the foundation to become more responsive to the diverse needs and innovative approaches in trustees’ communities and can sometimes lead to unexpected partnerships between trustees and program staff. A less centralized foundation is able to examine and promote local approaches, fund community-based organizations and understand regional differences regarding an issue that might not be familiar to staff based at headquarters. Such exploration can add new dimensions and insight that a foundation with a small staff (or no staff) would not have the opportunity to develop.

**Leveraging local involvement and complementary approaches.** For many large national foundations, discretionary grants enable trustees across the country to invest in local strategies in the foundation’s name. Lance Lindblom, presi-

dent of The Nathan Cummings Foundation, says that the trustees' discretionary grants leverage the foundation's name and visibility in many regions ([www.nathancummings.org](http://www.nathancummings.org)). Some foundations that are oriented to policy and research see discretionary grants as a complement to their work, because trustees tend to use their funds to support direct service in the community. Others, like the Gerald Oppenheimer Family Foundation, use discretionary grants to engage younger generations in the community. Tracey Boldemann-Tatkin, director of the foundation, explains that young family members can volunteer in the community to earn the privilege of making discretionary grants.

**Responding to urgent circumstances.** Many foundations establish discretionary grant programs for their CEOs, enabling them to respond quickly to emergencies, natural disasters or unanticipated opportunities. Because discretionary grants require the approval of only one person, they do not have to wait for a board meeting to be greenlighted.

**Providing a "release valve."** Most families have pressure points that can lead to conflict or more deeply entrenched dysfunction. Unlike other types of foundations, where trustees are generally recruited because of common commitments and values, a family foundation's trustees may not always share ideological or political beliefs. They may have very different behavioral or communication styles, opinions and interests. Discretionary grant funds can ease potential conflicts by enabling individual board members to fund dramatically different organizations or approaches, without having to convince fellow board members of their merits or relationship to the foundation's mission. This can avoid considerable internal strife.

Having access to discretionary grants that fund projects of personal interest can also reduce the potential for family member trustees struggling with each other to change the foundation's mission to accommodate those interests.

### **The Darker Side**

While discretionary grants can be useful for foundations, they can also be counterproductive, confuse the public and keep foundations from reaching their fullest promise. Discretionary grants can

be used as an excuse for the board not working together. They can drain significant resources from a foundation's central purposes and retard the growth of individual commitment to giving to the community. Let's investigate the downsides to awarding discretionary grants.

**Avoids joint decisionmaking.** When grant-making decisions do not require the approval of the full board, families rarely come together to find common ground and make joint decisions on funding allocations. Especially in situations where family members simply do not know each other well, discretionary grants can take away opportunities to learn about each other and build working relationships.

Family members can become disengaged from the grantmaking process when they are able to allocate funds without additional obligations and with little or no discussion. The greatest satisfactions in family philanthropy can be defining shared values, forging grantmaking programs based in common interests, celebrating accomplishments made together and passing on a unified vision to the next generations. Discretionary grants can fragment this enterprise.

The Lumpkin Family Foundation recently kicked off its regional grants program, which maintains commitments to causes dear to individual members, but requires that each grant align with the mission and goals of the foundation and pass through a review process. In the long run, the foundation expects the program will encourage family involvement and accentuate the family's joint decisionmaking skills.

**Dilutes the foundation's mission, donor intent and overall impact.** Most foundations place few parameters on the discretionary grant process. Funds may be used for any purpose, even if they fall outside the foundation's stated mission, programmatic priorities or geographic scope. For example, a foundation might be devoted to helping youth at risk, assisting the disabled and reducing homelessness in the community in which the foundation is based. How do a trustee's discretionary grants to medical research and her alma mater in another state further the foundation's goals?

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and guidelines. Some family foundations have seen their general funds decrease when trustee discretionary grant pools grow as family generations and branches increase, bringing more family members onto the board. Especially when so many foundations have experienced a decline in assets, discretionary grantmaking may divert vital funding that would otherwise go to foundations' core programs.

When The Nathan Cummings Foundation experienced a decrease in its overall grantmaking budget, holding the discretionary grant total allocation steady decreased the amount available for the foundation's primary grants programs. As a result, in 2002 the board decided to cap discretionary grants at eight percent of the total grant budget to maintain proportionality and maximize the overall impact in its priority program areas.

***Decreases accountability and impact.***

Accountability is important, since discretionary grants do not go through a standard proposal review process. Generally, a single trustee recommends the grant and no other staff or board member reviews it. The foundation board ratifies the grant as a mere formality. Nonprofits that receive discretionary grants do not have to state objectives, describe their efforts or provide details about how the money will be used. They may not even sign a grant contract or submit interim or final reports. As a result, foundations have no way to monitor progress or assess performance. There is no mechanism to evaluate the impact of discretionary grants.

***Confuses nonprofits and the public.*** Foundations encourage nonprofit organizations to do their research before submitting proposals. They ask nonprofits to read the foundation guidelines and ensure a good fit between the nonprofit's objectives and the foundation's mission, program areas and current interests. However, this research can become confusing when the foundation's guidelines say one thing but its grant disbursement list tells a different story. Nonprofits have no way to differentiate discretionary grants and when they see a variety of grants that appear to be exceptions to the rule, they are confused. So, even if a nonprofit's work is outside the stated foundation interests, its staff understandably might feel it could have a chance of receiving a grant. In submitting proposals, they waste valu-

able time and will receive an inevitable decline. If the nonprofit's work is well aligned with the foundation's stated objectives, its staff might worry that a hidden agenda is at work at the foundation, undermining trust.

In addition, sometimes multiple grants can be awarded from the foundation's general grantmaking program and from a trustee's discretionary fund. This is particularly confusing to the public. For example, a foundation program officer has completed the review of a proposal from an organization requesting \$25,000 for program expansion. The program officer has reservations about the organization's solvency and professionalism and has communicated those serious concerns to the prospective grantee. The program officer recommends that the foundation decline the request at its next scheduled board meeting.

Meanwhile, unaware of what is transpiring, a trustee sends a \$25,000 discretionary grant to the organization with a glowing note. The nonprofit thinks that the foundation has awarded the grant and calls the program officer in delight. How does the program officer respond? What does this communicate to the nonprofit community?

***Blurs legal and ethical lines.*** Discretionary grants can often camouflage self-dealing. Board members sometimes allocate discretionary grants to organizations that offer them personal benefits: fulfilling a giving requirement to serve on a prestigious board; receiving tangible benefits, such as free tickets or exclusive memberships; or being personally recognized in public for having made a major benefactor's contribution.

In one unfortunate instance, a small family foundation board member funneled his discretionary grants to a university where his son was being considered for admission. The university was well aware of the gift and assumed that the foundation supported this pressure. This type of abuse not only conflicts with the missions and purposes of individual foundations, but also with ethical and legal board member conduct.

The risks of misusing discretionary grants are revealed in a recent example involving public disclosure and scandal. On September 19, 2003, the *Washington Post* reported that the New York Stock Exchange Foundation "contributed more than \$1.3 million—about 18% of total giving—to groups affiliated with members of the board's

compensation committee.” The article questions whether or not Richard Grasso, former head of both the NYSE and its foundation, used foundation contributions to encourage compensation committee members to reward him with a \$140 million pay package. Sarah Teslik, executive director of the Council of Institutional Investors, is quoted, stating that “such contributions can help co-opt board members and make them less likely to challenge a chief executive they are overseeing.”

**Deters personal giving.** Rather than increasing philanthropy, discretionary grants can actually decrease total philanthropic dollars contributed to the community. Board members have a tendency to replace the funding they were giving personally with the foundation funds they receive through discretionary grants. Over time, they can view their discretionary grants (and their foundation service overall) as their philanthropic investment, rather than a complement to their personal commitments.

For board members who are inexperienced with personal giving, this has detrimental consequences. As most donors can attest, the personal aspect of giving leads to a deep sense of reward and meaning. Board members who have replaced individual philanthropy with discretionary grants lose this intimate connection and personal satisfaction. When board service ends, the trustee has not necessarily developed or sustained a philanthropic habit. Those trustees might falsely consider philanthropy the domain of foundations and wealthy founding donors and might not continue making contributions at a comparable level, or any level, regardless of their personal capacity for giving.

At their worst, discretionary grants can distort the principle that foundations are devoted to public benefit and that the assets are the foundation’s and no longer the family’s. Discretionary grants can encourage heirs to think of the funding as an entitlement of family membership and believe they have a personal right to control foundation fund allocation.

### Best of the Best Practices

First, the vast majority of foundations (74 percent) do not provide discretionary grants. More than 90 percent of community foundations do not

support this type of grantmaking and almost 50 percent of those that do limit discretionary grants to their board chairs. About 75 percent of independent foundations do not provide discretionary grant funds to their trustees and of those that do, one-fourth limit it to the board chair. If your foundation doesn’t provide discretionary grants, it’s probably a best practice to keep it that way.

If your foundation already supports discretionary grants, there are ways to keep them away from the dark side and on the path toward productive grantmaking. Here are the best of the best practices:

**Maintain consistency with mission, values and goals.** Karen Green, managing director for Family Foundation Services at the Council on Foundations, finds that family foundations rarely have a policy requiring discretionary grants to conform to the foundation’s mission. Yet this is key to having a successful program and achieving real impact. “Keep it mission related. Even if the family is geographically dispersed, have a policy connecting discretionary grants to the mission,” says Green. Family members will feel like they are involved in a common enterprise and more readily discover and share each other’s interests.

**Have guidelines.** The examples of the Nord, Lumpkin and Nathan Cummings foundations, where discretionary grants must go through an approval process to receive final authorization, are not the norm. Often, trustees simply fill out a request form and, if the organizations meet basic criteria (e.g., having 501(c)3 status), discretionary grants are automatically allocated. Foundations that develop guidelines requiring trustees to obtain certain basic information, make a site visit and fill out an application that identifies their reasons for wanting to award the grant find that their discretionary grants yield maximum rewards for the foundation and for the individual trustees. The grants become a vehicle for deepening understanding about grantmaking and helping other trustees learn about each other’s interests in respectful and gratifying ways.

Guidelines can also assist in the board education process and can bridge board-staff relationships. Tracey Boldemann-Tatkin suggests that established guidelines can go a long way in helping board members become personally engaged. Through hands-on experience supporting

## Statistics

### BOARD DISCRETIONARY GRANTMAKING

Grantmaker Type	Percent Permitting Discretionary Grants
Community	8.7
Family	47.5
Independent	25.4
Public	12.3
All	26.1

The median maximum amount is \$10,000, with a range of \$500 to \$400,000. (*Grantmaking*, Vol. II, 10th Edition. Council on Foundations, [www.cof.org/publications](http://www.cof.org/publications).)

### CEO DISCRETIONARY GRANTMAKING

Grantmaker Type	Percent Permitting Discretionary Grants
Community	44.7
Family	41.8
Independent	47.4
Public	50.7
All	45.5

(*2002 Grantmakers Salary and Benefits Report*, Council on Foundations, [www.cof.org/publications](http://www.cof.org/publications).)



The effectiveness of discretionary grants depends on how well the foundation has thought through the practice and established clear guidelines for their use.

organizations they personally care about, board members can become increasingly sophisticated about what nonprofits do, how they work and the formal procedures through which foundation staff ensure the quality and accountability of nonprofit grantees.

The Nathan Cummings Foundation has a number of written guidelines to avoid negative aspects of discretionary grants. For example, the foundation has an established conflict-of-interest policy that, among other provisions, states that a foundation grant cannot lead to personal recognition for the trustee. If a nonprofit recipient wants to present an award, it has “to be given to the foundation, unless the trustee has given an equal contribution personally,” according to Lance Lindblom.

**Set a time limit on their use.** One method of preventing discretionary grants from replacing personal giving is to decrease discretionary accounts over time and cap the time period during which a board member can allocate discretionary grants. For example, new board members can be given a small discretionary grant pool of \$10,000 per year for a period of three years to learn about grantmaking and develop relevant skills without becoming dependent on an outside source of funding for their community contributions.

**Using discretionary funds as matching grants.** Some foundations have developed specific strategies to ensure that discretionary grants will enhance rather than replace personal philanthropy. By matching trustee contributions 1:1 or even 2:1, foundations can leverage individual giving and stimulate trustees to give larger gifts to maximize matching funds for the organizations with which they have become involved.

The Jacobs Family Foundation implemented a matching discretionary grants program with the explicit goal of stimulating individual trustees’ personal giving ([www.jacobsfamilyfoundation.org](http://www.jacobsfamilyfoundation.org)). So the public does not confuse discretionary grants with the foundation’s regular grantmaking, the foundation requires that nonprofits acknowledge the trustee donor rather than the foundation. In this way, the discretionary grants mimic an employee-matching program.

**Communicate difference to the public.** Lindblom states that The Nathan Cummings

Foundation constantly works toward eliminating public confusion about discretionary grants. Discretionary grants are called community grants to differentiate them clearly from the foundation’s core grants. The foundation stipulates that a proposal for a regular foundation grant cannot be considered from an organization that has received a community grant within 12 months. Therefore, the nonprofit does not confuse how to effectively communicate with the foundation and who is ultimately responsible for grantmaking. The foundation sends letters explaining the difference to its grantees; it also defines the two types of grants and describes their distinct policies and procedures in all publications and on its website ([www.nathancummings.org](http://www.nathancummings.org)).

The Emily Hall Tremaine Foundation explains in its biennial report: “Besides the grants made by the Emily Hall Tremaine Foundation as a whole, each board member has the privilege of making discretionary grants every year from limited funds reserved for that purpose. These grants constitute a small proportion of the total. The Foundation does not receive applications for discretionary grants. This list of selected discretionary grants reflects the diversity of the board’s personal and philanthropic interests.” Thereafter, it lists each board member, the name of the organizations he or she chose to support and the amount and purpose of each discretionary grant ([www.tremainefoundation.org/report/discretionary-grants.asp](http://www.tremainefoundation.org/report/discretionary-grants.asp)).

Discretionary grants are a legal form of grantmaking, but their effectiveness depends on how well the foundation has thought through the practice and established clear guidelines for their use. In the past, the topic of discretionary grants often was a guarded secret. Karen Green notes that discussion of the issue is increasingly common. With so many foundations created over the last 20 years, more and more boards will explore the possibilities of discretionary grants. **F&C**

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## Time for a Discretionary Grants Change?

Here's how to redefine, limit or even sunset discretionary grants.

Your foundation has provided discretionary grants to board members for years. However, now those grants consume a sizable amount of the annual grants budget and they don't seem to be actively furthering the foundation's philanthropic mission and priorities. What do you do? How can you wean board members off discretionary grant funds or transform them into more effective vehicles?

Here are some ideas:

- Require that the purpose of all discretionary grants be consistent with the foundation's mission, program areas and stated priorities.

- Define in writing the purpose of the discretionary grants program. For example, state that the grants are intended to support the local communities of geographically dispersed board members, or to introduce new board members to the direct experience of charitable decisionmaking. This helps board members see the relationship of the funds to philanthropic use, not regard them as a perk of board membership.

- Rather than providing each board member with a set dollar amount for discretionary grants each year, establish the total discretionary fund as a set percentage of foundation grantmaking and divide the resulting amount by the number of board members. This strategy is especially useful when boards are expanding or incorporating another generation of family members, since it keeps the discretionary grants pool from growing too large.

- When other forms of financial compensation are provided, ask board members which benefits they prefer to receive.

- Where discretionary grants enable national foundations to provide board members with funds to direct to local communities, create a regional grants committee that oversees discretionary allocations. This committee reviews recommendations brought forward by individual board members, asks questions and stimulates reflection. Foundations using this method have discovered that when previously isolated board members learn about each other's communities, they share resources and sometimes even decide to pool their funds for a year to have a greater impact in one board member's local community.

- Require that board members bring their proposed contributions to the foundation grants committee and provide a profile of the organization and the reasons for making the grant. Approval may be automatic, but the exercise stimulates

board members to be more thoughtful in making their awards. Their colleagues on the board often ask good questions that deepen understanding of the grantee organization's work and operations. This also enables board members to learn more about each other's individual interests.

### Ask for a Commitment

- Add a matching requirement. In the future, have discretionary grants match a board member's contribution dollar for dollar or even 2:1 or more, which stimulates board members to make personal gifts in their communities. Matching gifts

double the foundation's dollars, rather than simply replacing contributions that board members might have made on their own with the foundation's money.

- Award discretionary grants where board members show a significant level of volunteer service in the community (for example, serving on a nonprofit board, chairing a committee or leading a team of volunteers). This stimulates

community involvement and is particularly helpful when board members may not have significant financial resources.

- Use discretionary grants as rewards for extra service to the foundation board by giving a discretionary grant fund for a small amount—such as \$2,500—to board officers and committee chairs.

### Ready to Sunset?

- Relate the elimination of discretionary grants to the poor performance of the foundation's assets and the goal of maximizing resources available for the foundation's core grantmaking programs.

- Implement a discretionary grants sunset strategy over a finite period (for example, three years) to allow board members to adjust to policy changes.

- Make discretionary grant funds available for a limited time—such as during the first three years that a new director serves on the board—or to a limited group—such as an associate board of next generation family members. Couple discretionary funds with other resources (e.g., publications on how to make grants, information on best practices in grantmaking, ability to attend grantmaker seminars, etc.). Require newcomers to make presentations about those resources to the full board or a special committee to magnify their learning about effective grantmaking.

—L.D.