



## **FUND DISTRIBUTION COMMITTEE REPORT # 1: REVIEW OF FUND DISTRIBUTION PRINCIPLES MAY 10, 2005**

The Fund Distribution Committee (“FDC”) appointed the Fund Distribution Review Working Group (“FDRWG”) to review the fund distribution principles, criteria and process of United Way of York Region (“UWYR”).

The first interim report focuses on the review of fund distribution principles, and covers the following topics:

1. Review of the existing funding distribution principle of UWYR
2. Discussion of three alternative fund distribution principles, namely:
  - Option 1: Agency Core Funding
  - Option 2: Zero-Based Allocation
  - Option 3: Allocation by Funding Priority – the recommended principle
3. FDC’s Recommendations

The Board of Directors is requested to consider and approve the FDC’s recommendations of adopting “**Allocation by Funding Priority**” as the new **fund distribution principle for UWYR**.

With the Board’s approval of a new fund distribution principle, the FDC and the FDRWG will proceed to develop new fund distribution criteria and process for approval of the Board in due course.

## Existing Fund Distribution Principle

### 1. Existing Practices and Patterns of Allocation

Currently, UWYR funding is allocated to support the following 3 major activities: Core Program, New and Expansionary (including new members) and Project (including IMPACT, Community Initiatives). Using 2004/05 allocation as an illustration, the actual amounts and proportions of allocations to the 3 activities are:

| Funded Activity    | 2004/05 Allocation Amount | 2004/05 Allocation Percentage |
|--------------------|---------------------------|-------------------------------|
| Core Program       | \$3,670,000               | 94%                           |
| New & Expansionary | \$152,000                 | 3.9%                          |
| Project            | \$80,000                  | 2.1%                          |
| Total              | \$3,900,000               | 100%                          |

### 2. Strengths and Weaknesses of Status Quo

The existing practices have been modified and evolved based upon feedback from member agencies and citizen review panels and volunteers. Member agencies commend UWYR for providing relatively stable funding which is critical to maintain their infrastructure. Many technical and procedural improvements have been incorporated. The existing process is regarded as participative, interactive, fair and transparent. Quality of funded programs is assured. However, there are also numerous shortcomings and limitations of the existing practices that require changes.

#### Core Program Funding

Under the existing fund distribution principles, member agencies' applications of core programs are assessed according to the following 3 criteria:

- Accomplishment of the proposed program plan for the previous year;
- Demonstration of service needs and effectiveness of the proposed program plan to address the needs in the coming year;
- Core competency of the agency.

The relevancy of the proposed programs and UWYR's funding priorities is not examined in the review process.

Only applications for New and Expansionary Program Funding for member agencies and Membership of non-members are reviewed according to UWYR's current funding priorities. Using the 2004/05 allocation as an example, only 3.9% of allocated funds were related to identified funding priorities. In ensuing years, these new programs will become Core Programs, and their relevancy to funding priorities will not be reviewed. In other words, 94% of UWYR's funded programs in 2004/05 were relevant to funding priorities in the past but not necessarily relevant to the current priorities. The status quo does not help profile UWYR as a funder addressing current community needs.

## New and Expansionary Funding

There is a lack of well-defined process and procedures to determine if sufficient funds are available to support new and expansionary programs for member agencies and new members. In 2004/05, the total amount of funding applications received for extra funding in November 2004 was over \$2 million. In March 2004 when UWYR's 2004/05 budget was adopted, there was only \$152,000 available for extra funding. Eventually, only two expanded programs for member agencies and two applications for new members were approved. Obviously, the final decisions caused huge disappointment and frustration to agencies. Nevertheless, FDC members, citizen review volunteers and staff were equally disappointed and frustrated.

It is important to note that member agencies are also concerned that there is no clear policy on priority of funding between new and expansionary programs for member agencies and membership of non-members. Currently, UWYR Board makes the final decision based upon FDC's recommendations.

## Project Funding

Project funding is time limited, and will not be rolled into Core Program Funding.

IMPACT is allocated to support improvement of infrastructure of member agencies.

Community Initiatives Funding support programs which address emerging community needs to member and non-member agencies.

However, relevancy of the funded programs to current UWYR funding priorities is not one of the funding criteria.

### **3. Conclusion**

The existing allocation practices accomplish:

- Providing relatively stable funding to member agencies;
- Assuring quality of funded programs;
- Assuring funded programs meet certain community needs.

However, the existing allocation practices **do not**:

- **Allocate funds according to current funding priorities;**
- **Encourage member agencies to change their UWYR funded programs to meet changing community needs.**

In the opinion of the FDC, the status quo is not desirable and has to be improved. This report will discuss three alternative fund distribution principles for consideration by the Board of Directors.

## **Option 1: Agency Core Funding**

### **1. Common Features**

Some funders believe that funded agencies have the best knowledge of the communities and their clientele in determining the use of their financial resources. Agencies should exercise their discretion to spend funding so that they can be highly responsive to the changing needs of the community. These funders also recognize agencies' needs to maintain and nourish their infrastructure in order to deliver quality services. Funding should be available to support core administration of agencies at their discretion.

The following are some common features of agency core funding:

- Funded agencies are allowed to use core funding at their discretion on services and core administration. Funding is not allocated to support specific programs or services;
- Allocations are determined by the overall core competency and service delivery performances of funded agencies;
- Allocations are not determined according to funding priorities of funders;
- Funding is usually stable as long as agencies meet allocation standards of funders.

### **2. Implementation**

However, there are very few funders that provide core funding. United Way of Greater Toronto ("UWGT") is a rare funder of this category.

In 2004, UWGT allocated \$44.5 million of core funding to 147 member agencies representing 86% of its total annual allocation. In the review of member agencies' funding applications, the following are examined:

- Profiles and needs of the target communities;
- Organizational information, e.g. governance, planning, evaluation, financial management, human resources, marketing;
- Services reports and plans

UWGT's funding priorities are considered when reviewing agencies' applications for new and expansionary funding. In 2004, \$1.36 million was allocated for this category, representing 3.8% of the total annual allocations. The additional funding will become core funding in future.

UWGT also provides numerous short term project funding to both members and non-members. All project funding is related to its current funding priorities. The total allocation in 2003 (information for 2004 was not available when this report was prepared) was \$6.1 million, or 13% of the annual allocation.

### **3. Advantages and Disadvantages**

Agency core funding contributes to the financial stability and infrastructure maintenance of funded agencies. Agencies also enjoy the flexibility to re-allocate resources to provide services responding to emerging community needs. Agencies are critically reviewed in meeting funders' allocation standards. Since core funding supports a variety of services, funded

agencies can still provide numerous interesting anecdotes of services relating to funders' funding priorities.

However, it is extremely difficult for funders to explain to their donors how their donations are allocated according to identified priority community needs. Although over 80% of UWGT's funding allocation in 2004 was not related to its priorities, UWGT was still able to allocate over \$6 million a year in project funding which are related to priorities. Resourceful funder like UWGT has the capacity to meet funders' expectations by allocating significant amount of funding to support services related to priorities, and at the same time, support agencies to maintain and develop their infrastructure through allocation of core funding. UWYR lacks this capacity.

#### **4. Conclusion**

The principle does not provide an effective mechanism to ensure funding is spent on addressing priority needs of the community. It does not contribute to ensuring the accountability to donors, which is a core value of UWYR.

## **Option 2: Zero-Based Allocation**

### **1. Common Features**

Zero-based funding allocation has been widely adopted by government funders and some charitable foundations since the 1990s in social, health, cultural, recreational, and environmental sectors in Canada. However, it is still uncommon to Canadian United Ways as community-based funders. Here are some common features of zero-based funding:

- Meeting the interest or expectations of the source of funding, e.g. governments or donors, is the primary interest;
- Funding is targeted to specific priority areas which meet funders' corporate objectives for name recognition and community profile;
- Competition of applying agencies for limited funds according to funding criteria, rating system and total funds available;
- There is a marked shift of decreasing support of core administrative costs of funded agencies;
- Funding is provided for a specific, usually shorter, period of time with no commitment of renewed funding.

### **2. Implementation**

The following are illustrations of implementing zero-based allocation by UWYR.

UWYR adopts and announces funding priority areas.

Agencies are invited to apply for funding to deliver services that will create impact on funding priority areas. It is questionable if the traditional membership system is applicable in this model. Membership system implies a stable relationship between UWYR and its members. Since the new model intentionally dispels the existence of "secured and long-term" funding for agencies, such a relationship will no longer exist.

It is unnecessary to differentiate "core program" with "new and expansionary program" funding streams. All programs, despite their funding history, will be assessed according to the current funding criteria and rating system.

All applications will be reviewed according to the pre-determined criteria and rating system. Applications that are rated with the highest scores will be awarded funding to deliver the services within the agreed upon timeframe.

### **3. Advantages**

UWYR supports services that bring the highest impact to the communities according to the funding criteria.

The system allows more flexibility to allocate funding when there is shortage of funds. UWYR has no commitment to renew funding to agencies after the expiry of the current funding contracts. Even in years when the results of the fundraising campaigns are less successful than the previous year, UWYR can still choose to fund services that perform the best within the limit of funds available.

It is appealing to some donors that their donations are distributed through a highly competitive process.

#### **4. Disadvantages**

This system does not recognize funded or member agencies as one of the primary stakeholders. However, in the survey of UWYR's selected internal constituents and member agencies preceding the UWYR's Board Retreat in January 2005, "Donors" and "Agencies and their Employees" are the top two stakeholder groups identified. Therefore, any allocation principle, e.g. zero-based allocation, which does not balance the interest of donors and agencies is inconsistent with the strategic values of UWYR.

Zero-based allocation harms agencies in many ways which have been extensively researched and documented. Common damage includes:

- Agencies can't plan ahead, and tend to focus on services that are likely to produce "quick wins" as opposed to programs that may produce results in the longer term;
- Agencies suffer volatility of revenues causing institutional instability. Experienced staff are let go causing waste of human resources. Successful programs are discontinued;
- Rarely is there a perfect match between funder priorities and an agency's mission or goal. Agencies often have to modify their mission and programming strategies to fit funder priorities. These survival behaviours undermine agencies' ability to respond to community needs. Agencies' autonomy is also eroded because their services are driven by funder priorities;
- Agencies' needs to maintain healthy infrastructure are not usually recognized and supported by funders. Most funders are not willing to contribute to agencies' core administrative costs.

Zero-based funding will also erode UWYR's relationship with its member agencies. Membership system has no meaningful position in this system as discussed earlier. Member agencies' support to and participation in UWYR's fundraising campaign activities will unlikely be available. These changes will drastically compromise UWYR's brand as a community-based charity.

The administration of zero-based funding is costly. All applying agencies have to be reviewed at the same time for competition of funding. It will increase the amount of UWYR's staff and volunteer resources to review all agencies every year, since UWYR currently reviews only half of its member agencies every year.

Finally, there is no evidence that zero-based funding is the only tool that selects services best addressing funding priorities. It is rather the assessment of agencies' core competency and measurement of service outcomes that are instrumental to select the best services for funding. Such measures are applicable to other fund distribution principles, and are not unique to zero-based funding.

## **5. Conclusion**

Zero-based funding allocation allows donors and funders to direct their financial resources specifically to services related to their areas of concern. The level of control of purposes of funded services is high.

However zero-based allocation also causes many challenges to non-profit agencies which may adversely affects quality of services. In fact, there is lack of evidence showing that zero-based funding is the sole factor that elevates quality and quantity of funded programs.

Zero-based funding will significantly downplay UWYR as a community-based charity which, in addition to raise money and distribute funds, also builds community capacity. UWYR, failing to treat community agencies as stakeholders equally to donors, will be another quasi government funder. United Way's value to the community will be compromised.

UWYR should pursue new fund distribution principles which place balanced value to donors and agencies as primary stakeholders and at the same time closely adhere to funding priority areas. The following section will discuss this option.

### **Option 3: Allocation by Funding Priority – The Recommended New Principle**

#### **1. Common Features**

In consideration of the strengths and weaknesses of the existing fund distribution system as well as the advantages and disadvantages of the alternative fund distribution principles discussed earlier in the report, FDC focused on the study of the principle of allocation by funding priority. United Way of Peel (“UWP”) adopted this principle in 2003, and has developed a very sophisticated allocation tool. The implementation is very successful. In 2004, UWP allocated \$7 million from its “Community Priorities Fund” to 118 programs delivered by 57 agencies. All funded programs addressed at least one of UWP’s five priorities.

These are some common features of the principle of allocation by funding priority:

- Funders assess the most pressing needs of the community periodically and identify funding priorities.
- Funders announce the funding priorities and specific criteria to service agencies.
- Only services which are related to specific funding criteria under the current priorities of funders are supported. Objective scoring system is usually used.
- Funded services are renewable if:
  - The priorities which the programs respond to are still current;
  - The service providing agencies maintain their core competency;
  - Services delivered meet the planned outputs and outcomes;
  - Proposed service plans are sound.
- Opportunities for additional funding are available for agencies that perform well. Agencies that perform below standards do not have such opportunities. They will be monitored closely, and may risk losing funds.
- Once funders identify new priorities, service agencies have to re-apply for funding accordingly. Services which are not relevant to the new funding priorities will not be funded. However, ample notice will be given to agencies regarding the change of funding priorities. Transition plan will be in place.

#### **2. Implementation**

The following are illustrations of implementing allocation by funding priorities by UWYR.

New funding criteria developed according to the priorities adopted by the Board in 2004 will be announced to member agencies.

Agencies will submit applications for funding to support services that are relevant to at least one of the five priorities of UWYR. Agencies, based upon their capacity, are encouraged to create the most effective programs to address UWYR’s priorities.

Agencies’ applications will be reviewed. Relevancy to the current priorities together with core competency of agencies and quality of the program plans will be reviewed. Funding will be awarded to successful agencies for one year.

Agencies’ performance and application for funding renewal will be reviewed after the first year. Agencies that meet performance standards will be rewarded opportunities to apply for additional funding, e.g. new and expansionary program funding and cost of living increase.

Agencies that do not perform well will not be allowed to apply for extra funding, and will be monitored closely.

When UWYR sees the need to identify new priorities in response to the changing needs of the community, usually once every 5 years, currently funded services will be re-examined if they are relevant to the new priorities. The above steps will be repeated.

### **3. Advantages**

The introduction of new allocation principles has the following merits:

- All funded programs are relevant to address current funding priorities.
- Only agencies that perform well will be rewarded the opportunity to apply for extra funding, e.g. cost of living increase, new and expansionary program funding. Agencies that perform poorly will not be allowed to apply for extra funding, and may risk losing their UWYR funding at all.
- Agencies are encouraged to be innovative to propose services that address UWYR's current funding priorities.
- Agencies will enjoy certain level of funding stability as long as they perform according to the standards and their funded programs are relevant to UWYR's current funding priorities.
- UWYR will maintain its brand as a community-based charity that holds itself accountable to its donors as well as building the capacity of its member agencies.

### **4. Disadvantages**

UWYR should not face any noticeable disadvantage in implementing this fund distribution principle. Resource implications in implementing this principle should be about the same as status quo.

Agencies will have less funding stability comparing with status quo. Some agencies' mandates do not have any relevancy to UWYR's priorities. Agencies' resistance to the new principle is possible.

## FDC's Recommendations to the Board of Directors

This report has identified challenges of the status quo for improvement as well as accomplishments as foundation for changes. Three alternative fund distribution principles have also been examined. The following table compares the impacts arising from the implementation of the status quo and the 3 options:

| Impact  | Status quo | Option 1:<br>Agency<br>Core<br>Funding | Option 2:<br>Zero-Based<br>Funding | Option 3:<br>Allocation by<br>Funding<br>Priority |
|---|------------|--|------------------------------------|---|
| Relevancy of Funders' Priorities                        | -          | -                                      | +                                  | +   |
| Funders' Accountability to Donors /<br>Constituents     | -          | -                                      | +                                  | +   |
| Assuring Quality of Funded Services                     | +          | -                                      | +/-                                | +   |
| Maintaining Agencies' Infrastructure                    | +          | +                                      | -                                  | +   |
| Encouraging Agencies to Meet Current<br>Community Needs | -          | +/-                                    | +                                  | +   |
| Administrative Cost to Funders                          | +          | +                                      | -                                  | +   |
| Total Score (+ minus -)                                 | 0          | -1                                     | +1                                 | +6  |

Legend:        -        Unlikely to accomplish  
                   +        Likely to accomplish

Allocation by funding priorities will be most beneficial to UWYR, funded agencies and the community as illustrated by the above comparison.

Therefore, the FDC recommends the Board to consider the following motion:

***That the Board of Directors approves FDC's recommendation to adopt the new fund distribution principle of allocation by funding priorities, and the FDC is asked to proceed to develop details of the criteria and process of allocation by funding priorities for future approval by the Board.***



