

Practitioner note - Unrestricted funding and nonprofit capacities: developing a conceptual model

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Introduction

Unrestricted or flexible funding practices are increasingly popular among funders. There is initial empirical support for the assumption that unrestricted funding has positive outcomes for nonprofit capacities, including the ability to better deal with external shocks such as presented by the COVID-19 crisis. However, academic literature on the effects of unrestricted funding is scarce, scattered and lacks an overarching theoretical basis. In our article, we build a conceptual model showing how unrestricted funding relates to nonprofit capacities and consequently effectiveness. We focus on nonprofit capacities, rather than capacity, to show the multifaceted nature of nonprofit capacity building.

Methods and findings

To examine the current state of knowledge around the effects of flexible, unrestricted funding on nonprofit capacities, we started with an extensive review of both the academic literature as well as practitioner reports. We supplemented this with 20 in-depth interviews with grantees who have lived experience of receiving multi-year unrestricted funding as a substantial part of their funding portfolio, some as long as since 1989. This information resulted in a proposed conceptual model, which shows how unrestricted funding may affect seven different nonprofit capacities: (1) financial management; (2) operational capacity; (3) staff management; (4) adaptive capacity; (5) strategic planning; (6) mission orientation; and (7) innovation.

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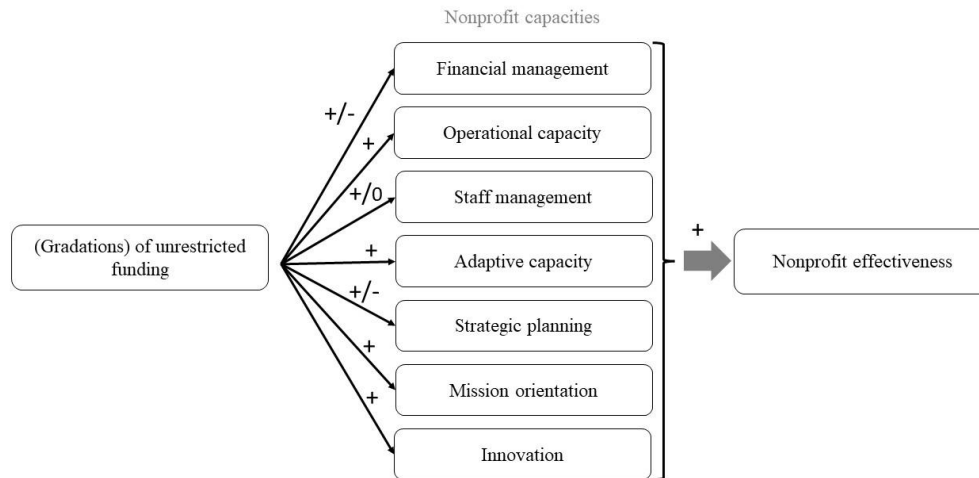


Figure 1: Proposed mechanisms linking (gradations of) unrestricted funding with nonprofit capacities and nonprofit effectiveness.

Note: +: expected positive effect; -: expected negative effect; 0: no effect expected

Box: Nonprofit capacities

The nonprofit capacities in the conceptual model are largely derived from the existing literature, specifically Shumate et al. (2017) and Wu (2021). In this literature these nonprofit capacities are defined as follows:

Financial management refers to how well a nonprofit manages their accounts.

Operational capacity relates to an organization's internal procedures, and its ability to set program goals and assess their outcomes.

Staff management relates to how well an organization's staff and management are equipped to do their jobs effectively.

Adaptive capacity refers to how nonprofit organizations are able to adapt to changes in their environment.

Strategic planning relates to an organization's deliberative and planned approach to decisions that determine the actions the organization takes and the rationale behind these actions.

Mission orientation refers to the common orientation of donors, community members, clients or beneficiaries towards an organization's mission.

Innovation refers to organization's ability to develop new solutions to (social) problems.

Sources: Shumate, M., Cooper, K. R., Pilny, A., & Pena-y-lillo, M. (2017). The Nonprofit Capacities Instrument. *Nonprofit Management and Leadership*, 28(2), 155–174.

Wu, V. C. S. (2021). Community leadership as multi-dimensional capacities: A conceptual framework and preliminary findings for community foundations. *Nonprofit Management and Leadership*, 32(1), 29–53.

Our conceptual model shows that *financial management* may be increased when organizations use multiyear, unrestricted funding to fill gaps between projects and to acquire other (project) grants, showing the importance of having at least some share of unrestricted funds in the revenue mix. A possible downside, reflected by the minus sign in Figure 1, is organizations becoming too dependent of multiyear, unrestricted funding, or the funders providing this type of funding. In terms of *operational capacity*, unrestricted funding may contribute to hiring and retaining high-quality personnel. Being selected as a grantee of unrestricted funding may affect *staff management* by improving organizational culture and atmosphere, especially when this resource stream is secured for a longer term. However, the role of unrestricted funding in job training and management practices is unclear based on our study, which is reflected by the zero in the model. Unrestricted funding can play an important role in developing *adaptive capacity*, specifically enabling both service provision and advocacy organizations to quickly respond to changing needs. *Strategic planning* is reported in the literature to be hampered by donor-imposed restrictions. Our interview data indeed support the idea that organizations can plan more strategically and use unrestricted funding to develop projects which are uncertain or difficult to fund by other funders. Unrestricted funding may bring with it a danger of becoming less critical about strategic choices, however, which we include in the model as a minus sign depicting a possible drawback of unrestricted funding. In terms of *mission orientation*, unrestricted revenues could make organizations less donor-driven and allow them to be critical towards funders, especially governments and companies. Our interview data show this not only holds for advocacy organizations, but also for some service providers. As a final capacity we add *innovation* to the model. Both in practitioner reports and our interview data, innovation and risk-taking surfaced as a theme in which unrestricted funding can play a key role.

Implications for practice

Based on our conceptual model, what can funders and nonprofit organizations take away from this study?

For funders:

- It could be relevant for funders to think more about aligning their funding strategy with their mission and/or theory of change. Many funders want to achieve big change and to

solve complex systemic problems, but typically provide short-term restricted project funding, which makes it hard for the receiving nonprofits to work towards solving these complex issues. Providing multi-year unrestricted funding to strengthen the capacities of nonprofits working on the ground could prove a fruitful strategy towards funders' own mission achievement.

- When providing unrestricted funding to nonprofit organizations, remain aware of power differences, and the unintended consequences these power difference can have. Take (lots of) time to build a collaborative relationship with the grantee, in which there is mutual respect and understanding. Make expectations for both you as a funder and for the grantee explicit, and try to uncover any implicit assumptions. See also [this paper in the Foundation Review](#) for more information on the topic of power and trust in funder-grantee organizations.
- Review the relevance of unrestricted funding for a grantee's role (for example advocacy or service provision) and sector (for example social services or arts) and the stage of development of the grantee organization. Organizations in the early development stages could likely benefit from building different capacities than more mature organizations. The same holds for organizations working in different roles in society and in different sectors. Some capacities, including financial management, operational capacity and staff management, appear to be important in some way for every nonprofit organization.

For nonprofit organizations:

- Nonprofit organizations could strengthen their organizations by diversifying their funding sources not just in terms of types of funding sources (e.g., diversify income from institutional, government and private funders), but also in terms of restrictiveness of funding. If a nonprofit has multiple sources of unrestricted funding, our model predicts that this will strengthen their capacities and consequently they will be more effective in working towards their mission.
- Second, nonprofits that receive unrestricted funding may want to consider investing this funding in a selection of the seven capacities identified in our conceptual model. Receiving unrestricted funding provides an opportunity to (re)consider and support long-

term organizational needs. Decisions on how to spend these means may require some time and effort – in that sense, unrestricted revenues are not necessarily “easy money”.

We hope that our conceptual model can function as a much-needed starting point to support academics and nonprofit leaders to better understand how unrestricted funding relates to nonprofit capabilities and consequently nonprofit effectiveness.