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THE WALL STREET JOURNAL

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| • APRIL 4, 2009

Carl Schramm

Giving Capitalism Its Due

The head of the Kauffman Foundation on the importance of entrepreneurship.

By [NAOMI SCHAEFER RILEY](#)

Carl Schramm doesn't buy the idea that some businesses are "too big to fail." That notion, says the president of the Kansas City-based Kauffman Foundation, only creates obstacles for entrepreneurs. Instead, he sees the failure of big companies as the "moment when 1,000 flowers can bloom."

The Kauffman Foundation, known to National Public Radio listeners and a few others as "the foundation for entrepreneurship," is difficult to categorize, but its president seems to like it that way. Last Sunday afternoon at the largely deserted Harvard Club in New York, I sat down to talk with Mr. Schramm, an unassuming man with distinctive round spectacles who oversees an almost \$2 billion endowment.

Kauffman was founded in 1966 by pharmaceutical magnate Ewing Marion Kauffman. In 1950, he launched a drug company in the basement of his Kansas City home. Forty years later, when he sold the business to Merrell Dow, it had become a diversified health-care company with nearly \$1 billion in annual sales and more than 3,000 employees.

Kauffman gave a lot of thought to his journey from poverty to wealth, according to Mr. Schramm. "He saw this as the central theme of his life."

So what exactly is a foundation for entrepreneurship? Aren't foundations supposed to give money to charity? And aren't entrepreneurs supposed to get money from investors, not philanthropists?

On the theoretical level, Mr. Schramm, who started his own health-care company and merchant bank, believes that the foundation has a duty to foster an environment hospitable to entrepreneurship. And so, for instance, Mr. Schramm brags that Kauffman has "dragged economists into considering the importance of firm formation to the overall growth of the economy." The foundation has commissioned some 6,000 papers on this and related topics in the past several years.

Then there is the question of the public perception of entrepreneurship. In the most recent survey that the foundation sponsored, pollsters found that 63% of respondents "prefer giving individuals the incentives they need to start their own businesses as opposed to allowing the government to create new jobs directly." Conducted last month, the survey also showed that instead of the government's stimulus package, two-thirds of respondents would prefer "reducing legal barriers and red tape for new business development" as a way to jump-start the economy. Finally, 89% of respondents said that "capitalism is still the best economic system for our country."

Despite this popular attitude, Mr. Schramm worries that there is a tendency on the part of some citizens to want the

government to prevent market chaos. Prior to the financial meltdown this fall, "I think we were in full tide of entrepreneurial capitalism and now there's an introspection, where the vocabulary is all about regulation and the importance of the government to restart the economy," he says. While Mr. Schramm believes that the government has a role to play, he argues that "historically through the last seven recessions it's been entrepreneurs who essentially restarted the economy."

Kauffman is dedicated to cultivating such innovators. Mr. Schramm is intent on dispelling the common misperception that "If you don't have it done by the time you're 19 or 21, it ain't gonna happen," and according to Inc. magazine, he says, "the fastest growing firms in the United States are started by people who are 39 years old" on average.

In order to educate young people about the history of entrepreneurship in America, the foundation has partnered with 18 college campuses. "When I was in high school, the word entrepreneur was in zero use, it was not part of the American vocabulary. If you were to ask about inventors, they were pretty much dead people, you know, George Westinghouse and George Eastman." Today, Mr. Schramm thinks that kids do see more entrepreneurship around them with Internet startups and the like, but schools still don't encourage it. Even business schools, Mr. Schramm says, seem to offer only a "very rigid formalistic perspective about writing business plans."

Kauffman has tried to provide more direct and practical aid to those trying to start their own businesses. Through a program called FastTrac, for instance, Kauffman will help 1,000 current and new small-business owners in New York City over the course of the next year learn the skills they need to succeed.

FastTrac helps budding entrepreneurs with the important decision of picking a lawyer, for instance. "The bad choice of a lawyer at the start of a business or the bad choice of an accountant can screw the business up in a way that is fatal," says Mr. Schramm. The program also advises budding entrepreneurs never to let their lawyers or accountants invest in the company. "You have to develop your own sense of the value of the advice you're getting. And the minute people say well I want to own 25% of the company, all the alarm bells ought to go off."

Finally, the foundation goes out of its way to support minority entrepreneurship. Mr. Schramm doesn't use any social-justice lingo to explain the program, but reverts to a kind of charming nerd-speak. He says that after a lot of analysis, Kauffman has found that there is "the greatest delta among black males." In other words, for a given amount of entrepreneurial investment, that group will see the greatest improvement in its economic status. While there are many activists out there saying that foundations should give more to minorities, you won't find many who offer the Kauffman philosophy: "We should have a proportionate number of black billionaire owners of businesses as exists in the majority community," says Mr. Schramm.

In addition to encouraging entrepreneurship of all sorts, Mr. Schramm says the foundation itself is supposed to act entrepreneurially. In the past couple of decades, a veritable army of professional nonprofit workers has grown up. But Mr. Schramm was not among them. Before arriving at Kauffman, he taught at Johns Hopkins (he has a law degree and a doctorate in economics). When he applied to foundations for funding during his time as a professor, he recalls, "You had to be very good at using language to sound like you were out on the frontier, but in fact you couldn't go too far because . . . foundations are very cautious."

For a while, he wondered what was behind that tendency. He concluded that "the foundation culture had developed a sort of consensus": Foundation money is "quasi-public." In a prescient article that Mr. Schramm wrote for the Harvard Journal of Law and Public Policy in 2006, he notes that "the foundation appears to lack any coherent theory of its own role in

society and the economy." The result, he warned, is that "government can impose expectations that may destroy the foundation's ability to achieve the purposes for which it was conceived."

Lately, some in the government have been trying to do exactly that. A few members of Congress, including Rep. Xavier Becerra (D., Calif.), have recently suggested that foundations need to be giving a greater percentage of their dollars to minority groups and other "marginalized communities." And various activist groups, including the National Committee for Responsive Philanthropy and Greenlining, have made the case that philanthropic dollars really belong to the public since they are tax exempt. Mr. Schramm responds: "I don't think as a legal matter that it holds because under that theory my 401(k) is public money."

So who are the real stakeholders in foundations? Mr. Schramm can think of only one: the donor. "At Kauffman I think the trustees and I are very, very clear: We work for Mr. Kauffman," says Mr. Schramm, acknowledging that his boss passed away in 1993. Kauffman not only left extensive writings but also videotape of himself describing how he wanted the foundation to operate. Mr. Schramm says that one board member told him he was hired because he was the only candidate who had read Kauffman's book.

Despite, or perhaps because of, his familiarity with Kauffman's thought, Mr. Schramm did not have an easy time taking over the foundation in 2002. Over time Kauffman had grown unwieldy, with one of the highest overhead costs of any foundation in the country. And its mission had become diluted. For example, Mr. Schramm notes, Kauffman said he was interested in education. "What was read into it was he was really more interested in general youth development. So we found ourselves supporting sports programs." Kauffman owned the Kansas City Royals for a time and Mr. Schramm notes that "he loved sports, but when it came to his foundation, he was crystal clear about what he wanted to have done and the word 'sports' never shows up in hundreds of pages of discussion."

And so within a year of taking over, Mr. Schramm began a serious overhaul of the foundation. He laid off about half of its 150-person staff and cut off funding to some of its biggest grantees, many in Kansas City. There was a public outcry from local nonprofits and from some former members of the board. One told the New York Times that "Carl doesn't seem to understand that there isn't an 'I' in team." It reached the point where Missouri's then attorney general, Jeremiah Nixon, launched an extensive investigation. He determined that Mr. Schramm had not led the foundation astray. What ultimately saved his job, says Mr. Schramm, were the detailed writings that Kauffman left before his death.

"What happened was not atypical in foundations. Often around 10 years after the death of the donor there's a moment of truth." People who were close to the donor will say, "Yes, he said that but he didn't mean that." Mr. Schramm concludes: "If there was one piece of advice I'd give to someone who was starting a foundation it is this: Think very, very hard of the long term and write down what you want your foundation to look like in 30 years or 40 years."

Despite the fact that the foundation's endowment has fallen by \$722 million since the end of 2007, Mr. Schramm sees this as Kauffman's "moment." While "no one hopes for a recession," it's during economic crises that entrepreneurs "challenge companies that have gotten big and lazy." The downturn, he says, will even challenge Kauffman to "think about how we can do our work better, like every business." In fact, Mr. Schramm adds, "The only people immune from thinking hard in moments like this are in government."

Ms. Riley is the Journal's deputy Taste editor.

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