

NONPROFIT SECTOR STRATEGY GROUP

Market  
The Nonprofit Sector  
and the Market:  
Opportunities &  
Challenges

A STATEMENT  
FOR PUBLIC  
DISCUSSION



THE ASPEN INSTITUTE

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## Nonprofit Sector Strategy Group

The Aspen Institute's Nonprofit Sector Strategy Group (NSSG) is a leadership forum that is addressing the most pressing issues facing the nonprofit sector in America. Formed in 1997, the NSSG convenes meetings to explore innovative ways in which the business, government and nonprofit sectors might work together to address shared concerns and promote a healthy civil society and democracy.

The NSSG is an initiative of The Aspen Institute's Nonprofit Sector and Philanthropy Program, which seeks to improve the operation of the nonprofit sector and philanthropy through research and dialogue focused on public policy, management, and other important issues affecting the nonprofit sector.

Other NSSG publications include, "The Nonprofit Contribution to Civic Participation and Advocacy" and "The Nonprofit Sector and Business: New Visions, New Opportunities, New Challenges."

This pamphlet provides an introduction to the work of the NSSG, followed by the group's statement, "The Nonprofit Sector and the Market: Opportunities and Challenges."

We welcome your comments on this publication. To share comments, request more information, or order NSSG publications, please contact:

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## Introduction: The Mission of the Nonprofit Sector Strategy Group

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*By carefully examining the most important challenges and opportunities facing America's private nonprofit organizations, the Nonprofit Sector Strategy Group is working to stimulate a new consensus about the nonprofit sector's roles and responsibilities, and offer practical recommendations to enhance policy, practice, research, and public education on this crucial set of institutions.*

America's private nonprofit sector has long played a critical role in American life.<sup>1</sup> Its 1.5 million organizations and associations provide services to meet an extraordinary range of human needs: ministering to the sick through visiting nurses associations, hospitals, clinics, and nursing homes; educating tens of millions in its schools and universities, as well as in community tutoring programs; providing human services such as day care, meals on wheels, adoption, job placement, domestic abuse prevention, and relief for the poor; strengthening spiritual life through churches and religious associations; and promoting arts and cultural activities of all kinds.

Nonprofit organizations also connect Americans to unique opportunities: to volunteer, to advocate for public policy, to promote democratic values, to participate in decision-making processes, and—in doing so—to shape a more just and prosperous democracy.

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### RESPONDING TO A CHANGING LANDSCAPE

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In the past 15 years, the nonprofit sector, like business and government, has had to respond to a dramatically new social and political landscape.

The contours of this landscape include: a new and constantly evolving mix of peoples and cultures; instant and interactive technology in all arenas of life; downsized and devolved governments; a global marketplace; a commercial presence that reaches into almost every aspect of life; and a surging, volatile economy that is benefiting many but not all.

These new realities pose a complex mix of opportunities and challenges for nonprofit organizations. On the one hand, they

open up the possibility of productive new partnerships between nonprofit organizations and businesses and new sources of revenues that nonprofit organizations can tap. On the other hand, however, they bring for-profit competitors into traditional nonprofit fields and create commercial pressures that can threaten the ability of nonprofit organizations to remain focused on their public-service missions.

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### THE WORK OF THE NONPROFIT SECTOR STRATEGY GROUP

This changed environment gives rise to fundamental questions: What are the unique contributions of nonprofit organizations? What traditional nonprofit roles should endure and what new roles need to be imagined? What are the sector's major strengths and weaknesses? How can needed changes best be encouraged?

In 1997, The Aspen Institute, an international nonprofit educational institution headquartered in Washington, D.C., organized the Nonprofit Sector Strategy Group (NSSG) to address these questions, to examine the sector's most important opportunities and challenges and bring constructive ideas and recommendations to public attention. Funded by grants from the W. K. Kellogg Foundation and The Ford Foundation, the NSSG focuses its attention primarily on the public-benefit portion of the nonprofit sector, which encompasses those organizations whose primary mission is to serve a broad public rather than their own members.

The NSSG convenes participants from a variety of backgrounds and institutions—including individuals from business, government, academia, nonprofit organizations, foundations, and the media. In addition to gathering participants for regular deliberations, the NSSG shares its findings with and seeks comments from a broad range of opinion leaders, policymakers, academic institutions, nonprofit and business groups, and journalists.

The following pages contain points of agreement that surfaced during an NSSG meeting on a critical issue facing the nonprofit sector: the sector's increasing involvement in market or commercial relationships. We circulate this document in the hope that it will add to the ongoing dialogue on this topic and provide helpful suggestions for future action.

# The Nonprofit Sector and the Market: Opportunities and Challenges

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## Summary of Principal Conclusions

### BACKGROUND

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#### **1. Market relationships have grown increasingly important to American nonprofit organizations over the past two decades.**

- *Nonprofit reliance on income from fees and charges for services, already substantial, has grown considerably over the past two decades.* Fees and charges accounted for well over half of the considerable growth that the nonprofit sector experienced over the past 20 years and now provides over half of all nonprofit income. While clearly more important in some portions of the sector than others, such income has also spread in recent years well beyond its traditional significant presence in health and higher education to penetrate additional arenas of nonprofit activity, such as social services. Income from philanthropy also grew during this period, but at a slower pace. Thus, in the last 20 years, philanthropy has declined as a share of total nonprofit income.
- *While nonprofit organizations have come to rely increasingly on fees and charges, for-profit firms have moved actively into arenas once occupied almost exclusively by nonprofit providers.* For-profits have captured much of the growth in the hospital field over the past two decades and disproportionate shares of the growth in such fields as home health, day care, and social services. In addition, welfare reform has created a vast new market for caseload management and human service provision that for-profits have moved into aggressively and successfully, sometimes displacing or altering the roles of nonprofit providers in the process.
- *New forms of nonprofit organizations have also recently made their appearance, mobilizing for-profit means in the pursuit of nonprofit ends.* The resulting "social ventures" produce goods and services for the market, yet do so in ways that serve charitable purposes (e.g. equipping the homeless with skills by putting them to work in catering operations) with the income raised.

- *Finally, some business corporations have formed productive partnerships with nonprofit organizations that serve business purposes while also promoting nonprofit goals.*

**2. These developments open important opportunities, but also raise important issues, for the future evolution of the American nonprofit sector and its ability to promote the public good.** Of particular concern are the implications that increased commercial activity and growing market pressures may have for the willingness and ability of nonprofit organizations to serve those in greatest need and to perform a variety of social functions—such as advocacy, community empowerment, and research—that the market has traditionally undervalued.

**3. To date, however, little explicit attention has been devoted to the trade-offs that may be posed by this increased commercial involvement on the part of nonprofit organizations.** Therefore to explore these issues in greater depth, The Aspen Institute's Nonprofit Sector Strategy Group took up the question of the relationship between the nonprofit sector and the market at a special meeting on August 12-16, 1999. This statement records the major points of agreement that surfaced in this discussion.

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## KEY CONCLUSIONS

**1. *Benefits.*** Nonprofit involvement in the market can bring considerable benefits to the nonprofit sector and to society at large. Among these possible benefits are the following:

- A reliable flow of resources for the promotion of charitable purposes and the public good;
- Incentives for greater efficiency and innovation as a result of increased competition;
- Better targeting of services to client needs;
- Increased legitimacy for charitable activities resulting from association with the assumed efficiency of the market;
- Attraction of funds into charitable activities from donors committed to new enterprise approaches to social problem-solving; and
- Possible greater accountability to the public through the adoption of enterprise-type performance indicators and the "market test."

**2. Risks.** At the same time, nonprofit involvement in the market can pose significant risks for the nonprofit sector, the people it serves, and American society more generally. These potential risks take a number of forms:

- Displacement of the social mission of the nonprofit sector as a result of pressures to shift attention away from the non-marketable aspects of nonprofit operations—such as the promotion of civic participation, advocacy, the building of community, and service to the needy;
- Pricing certain populations out of the market for key services;
- Loss of public support for nonprofit tax exemptions due to growing confusion over the extent to which nonprofit organizations differ from business corporations;
- Discouragement of private philanthropy;
- Pressures to increase the scale of operations, which can lead to a loss of the flexibility and closeness to the people served, which are hallmarks of nonprofit operations;
- Loss of a critical infrastructure of sustainable nonprofit agencies in communities across the country as a result of displacement by for-profit firms that may ultimately disappear if market conditions change;
- Discouragement of volunteers and, potentially, of paid staff attracted to nonprofit sector work because of its distinctive social mission;
- Challenges to the capabilities and energies of agency staff, which are increasingly called on not only to promote the charitable missions of their organizations but also to run complex businesses in an increasingly competitive business environment;
- Conflicts of interest within agencies between those engaged in income-generating activities and those engaged in non-income-generating activities; and,
- Loss of the "charitable endowment" of agencies—i.e. the accumulated assets represented by agency goodwill, good name, physical resources, and capital endowment—as a result of their transfer to for-profit businesses.

**3. A Reasonable Trade-off.** After balancing the risks and benefits, the Strategy Group concluded that the recent trend toward greater involvement in the market by nonprofit organizations can usefully serve the public good that nonprofit organizations are designed to promote. In coming to this conclusion, Strategy Group participants took explicit note of the fact that for-profit firms also engage in activities that have social value, including advocacy, and that market means can therefore be



employed to advance public purposes.

**4. *Appropriate Precautions.*** More specifically, to take appropriate advantage of the benefits that nonprofit involvement with the market can bring while minimizing the risks it poses, a number of steps can usefully be taken. Fundamentally, these steps should seek to ensure that a suitable balance continues to be struck between the special advantages that nonprofit organizations enjoy by virtue of their tax-exempt status and the contributions that they make to the public good. Among these steps are the following:

*(a) With regard to fee-for-service income:*

- Ensure through charitable and public-sector support, and through the design of fee structures, that those most in need have equal access to services;
- Develop outcome measures and consumer protection mechanisms to help clients make effective judgments about the services they receive;
- Encourage nonprofit organizations that are heavily dependent on fee-for-service revenue to retain their commitment to the public good by expecting some documentation of social mission activity as a condition for retaining their special tax treatment;
- Avoid excessive compensation of nonprofit executives; and,
- Increase the base of knowledge that exists about the use and consequences of fee-for-service income by nonprofit agencies in different fields.

*(b) With regard to for-profit competition:*

- Ensure that nonprofits are on a level playing field vis-à-vis for-profit firms by providing them better access to capital and information;
- Encourage government to reimburse more quickly on purchase-of-service contracts and thereby reduce the capital needs for those bidding on such contracts;
- Where appropriate, create a special "set-aside for small providers" in government human service procurement programs modeled on the existing set-aside for small businesses to ensure the preservation of a basic infrastructure of needed human service agencies in local communities despite the vagaries of the market;
- Enforce quality standards for both for-profit and nonprofit firms involved in basic human service provision, including requirements for equal access and

minimum levels of charity care;

- Improve accountability and transparency requirements for both nonprofit and for-profit firms operating in the human service field, especially those funded in part through public-sector resources; and,
- Increase the base of knowledge about the consequences of for-profit extension into key service fields.

*(c) With regard to social ventures:*

- Ensure that existing law at the federal, state, and local levels permits valid social venture activity, i.e., ventures that maintain a reasonable balance between the tax and related benefits they receive and the social purposes they pursue;
- Make information and legal assistance available to social venture entrepreneurs to assist in adapting this form of nonprofit operation to the existing legal framework;
- Encourage social ventures to develop effective measures of the "social benefits" they produce and utilize a "double bottom line"—one commercial and the other social—to assess their performance;
- Encourage foundations to consider "social ventures" as potential recipients of foundation support and appropriate partners with which to work;
- Encourage foundations and other charitable institutions to work with private financial institutions to fashion new forms of capital assistance for social ventures (e.g. foundation-guaranteed loans, subsidized loans);
- Improve the training of potential "social venture entrepreneurs" who can combine commitment to mission with solid business experience and who can help facilitate the leadership succession that successful social ventures will require;
- Encourage businesses to share knowledge and forge alliances with social venture entrepreneurs, and with other nonprofit organizations; and,
- Improve the base of knowledge about social ventures and how they can be managed most effectively.

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## CONCLUSION

Ultimately, society values nonprofit organizations because they produce benefits that go well beyond the provision of goods and services. These benefits include contributions to the general welfare, to our sense of community, and to the building of democracy. While a shift to the market may help nonprofits achieve these benefits, it may also put them at risk by focusing agency attention and energy on those aspects of its operations that can yield market returns.

Therefore, the pursuit of desirable social purposes can no more be taken for granted in the case of nonprofit organizations than it can for any other type of organization. Rather, as a society, we must put in place mechanisms and protections to ensure that in reaping the positive benefits that the market offers, nonprofit organizations are not enticed or forced to surrender the essential social value contributions that they are particularly equipped to provide. It is this type of balance that this statement seeks to encourage.

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## NOTES

1. *The nonprofit sector consists of a broad range of organizations that qualify for exemption from federal income taxes under any of 26 different sections of the Internal Revenue Code. A common characteristic of these organizations is that they do not distribute any profits they might generate to those who control and/or support them. As noted below, the particular focus of the Nonprofit Sector Strategy Group, and hence of this statement, is on a subset of these tax-exempt organizations—namely, those that are eligible for exemption under either Section 501(c)(3) or 501(c)(4) of the tax code. For further detail on the definition of nonprofit organizations, see: Bruce Hopkins, *The Law of Tax-Exempt Organizations* (New York: John Wiley and Sons, Inc., 1992).*

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The Aspen Institute is a global forum for leveraging the power of leaders to improve the human condition. Through its seminar and policy programs, the Institute fosters enlightened, morally responsible leadership and convenes leaders and policy-makers to address the foremost challenges of the new century.

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