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## *The Resilient Sector: The State of Nonprofit America*

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When three hijacked planes crashed into the World Trade Center and the Pentagon on the morning of September 11, 2001, the police, fire, and military organs of New York City, Washington, D.C., and the U.S. government were not the only entities to respond with heroism and élan. The events of that horrific morning also triggered a spirited response from the vast, uncharted network of private voluntary institutions that forms the unseen social infrastructure of American life. In small towns and large cities, from the Florida Keys to northernmost Alaska, people rushed to offer assistance. In part, the responses were spontaneous and unstructured. But in far larger part, they were organized and orchestrated, mobilized by the vast assortment of organizations and institutions that compose what is increasingly recognized as a distinct, if not wholly understood, sector of our national life known variously as the nonprofit, the charitable, or the civil society sector.

Like the arteries of a living organism, these organizations carry a life force that has long been a centerpiece of American culture—a faith in the capacity of individual action to improve the quality of human life. They thus embody two seemingly contradictory impulses that form the heart of American character: a deep-seated commitment to freedom and individual initiative and an equally fundamental realization that people live in communities and consequently have responsibilities that extend beyond themselves. Uniquely among American institutions, those in the nonprofit sector blend these competing impulses,

creating a special class of entities dedicated to mobilizing *private initiative for the common good*.

The terrorists who crashed civilian jetliners into unarmed buildings on that fine September morning did not, therefore, assault a nation without the capacity to respond. That capacity extended well beyond the conventional and visible institutions of government. It embraced as well a largely invisible social infrastructure of private, charitable groups and the supportive impulses to volunteer and give that it has helped to nurture.

And respond it did. Within two months, individuals, corporations, and foundations had contributed \$1.3 billion in assistance to a wide array of relief efforts. Blood donations alone were estimated to have increased between 250,000 and 400,000 pints in the wake of the disaster.<sup>1</sup> Some of the institutions involved in mobilizing this response were household words—the Red Cross, the Salvation Army, and United Way. Others were established but less-well-known institutions like the New York Community Trust, the Community Service Society of New York, the Chicago Mercantile Exchange Foundation, and many more. Still others were created especially to deal with this crisis—the September 11 Fund, the Twin Towers Fund, Trial Lawyers Care (to assist victims with legal issues), and the Alaska Culinary Association (to benefit families of restaurant workers killed in the World Trade Center collapse). Altogether, some 200 charitable organizations reportedly pitched in to help directly with the relief and recovery effort in New York alone, and countless others were involved more indirectly. According to one recent survey, an astounding 70 percent of all Americans made some kind of contribution to this response.<sup>2</sup>

Revealing though this episode has been of the remarkable strengths of America's "third," or nonprofit, sector, however, it simultaneously revealed the sector's limitations as well. Private voluntary groups, though highly effective in mobilizing individuals to act, are far less equipped to structure the resulting activity. In short order, the fragile systems of nonprofit response were severely challenged by the enormity of the crisis they confronted in the aftermath of September 11. Individual agencies, concerned about their autonomy, resisted efforts to coordinate their responses, either with each other or with government authorities. Individuals in need of assistance had to navigate a multitude of separate agencies, each with its own eligibility criteria and targeted forms of aid. Inevitably, delays and inequities occurred; many individuals fell through the slats, while others benefited from multiple sources of assistance. What is more, misunderstandings arose between the donors, most of whom apparently intended their contributions to be used for immediate relief, and some agencies, most notably the Red Cross, that hoped to squirrel the funds away for longer-term recovery, general institutional support, and other, less-visible, disasters down the road. What began as an inspiring demonstration of the power of America's charitable community thus became a demonstration of its shortcomings as well.

In this, the story of the nonprofit sector's response to the crisis of September 11 is emblematic of its position in American life more generally. Long celebrated as a fundamental part of the American heritage, America's nonprofit organizations have suffered from structural shortcomings that limit the role they can play. This juxtaposition of strengths and limitations, in turn, has fueled a lively ideological contest over the extent to which we should rely on these institutions to handle critical public needs, with conservatives focusing laser-like on the sector's strengths and liberals often restricting their attention to its weaknesses instead. Through it all, though largely unheralded and perhaps unrecognized by either side, a classically American compromise has taken shape. This compromise was forged early in the nation's history, but it was broadened and solidified in the 1960s. Under it, nonprofit organizations in an ever-widening range of fields were made the beneficiaries of government support to provide a growing array of services—from health care to scientific research—that Americans wanted but were reluctant to have government directly provide.<sup>3</sup> More than any other single factor, this government-nonprofit partnership is responsible for the growth of the nonprofit sector as we know it today.

During the past twenty years, however, that compromise has come under considerable assault. At the same time, the country's nonprofit institutions have faced an extraordinary range of other challenges as well—significant demographic shifts, fundamental changes in public policy and public attitudes, new commercial impulses, massive technological developments, and changes in lifestyle, to cite just a few. Although nonprofit America has responded with creativity to many of these challenges, the responses have pulled it in directions that are, at best, poorly understood and, at worst, corrosive of the sector's special character and role.

Despite the significance of these developments, little headway has been made in tracking them systematically, in assessing the impact they are having both generally and for particular types of organizations, and in getting the results into the hands of nonprofit practitioners, policymakers, the press, and the public at large. This book is intended to fill this gap, to offer an overview of the state of America's nonprofit sector, and to identify the changes that might be needed to promote its long-term health. To do so, the book assembles a set of original essays prepared by leading authorities on key components of the American nonprofit scene and on the key trends affecting their evolution. The result is the first recent integrated account of a set of institutions that we have long taken for granted, but that the Frenchman Alexis de Tocqueville recognized more than 175 years ago to be “more deserving of our attention” than any other part of the American experiment.<sup>4</sup>

This chapter summarizes the basic story that emerges from this assessment. Given the diversity of America's nonprofit institutions and the multitude of forces impinging on its various parts, this is no mean task. From my perspective,

however, a dominant, if hardly universal, impression clearly emerges from the separate brush strokes of analysis offered in this book's chapters. Fundamentally, it is an impression of *resilience*, of a set of institutions and traditions facing enormous challenges but also important opportunities and finding ways to respond to both with considerable creativity and resolve. Indeed, nonprofit America appears to be well along in a fundamental process of "reengineering" that calls to mind the similar process that large segments of America's business sector have undergone since the late 1980s.<sup>5</sup> Faced with an increasingly competitive environment, nonprofit organizations have been called on to make fundamental changes in the way they operate. And that is just what they have been doing.

What is involved here, moreover, is not simply the importation of "business methods" into nonprofit organizations, although that is sometimes how it is portrayed.<sup>6</sup> While nonprofits are becoming more "business-like," the business methods they are adopting have themselves undergone fundamental change in recent years, and many of the changes have involved incorporating management approaches that have long been associated with nonprofit work—such as the emphasis on organizational mission, the ethos of service to clients, and the need to imbue staff with a sense of purpose beyond the maximization of profit. In a sense, these longtime nonprofit management principles have now been fused with business management techniques to produce a blended body of management concepts that is penetrating business and nonprofit management alike.

Like all processes of change, this one is far from even. Some organizations have been swept up in the winds of change, while others have hardly felt a breeze or, having felt it, have not been in a position to respond. What is more, it is far from clear which group has made the right decision or left the sector as a whole better off, since the consequences of some of the changes are far from certain and at any rate are mixed.

Any account of the "state of nonprofit America" must therefore be a story in three parts, focusing first on the challenges and opportunities America's nonprofit sector is confronting, then examining how the sector's institutions are responding to these challenges and opportunities, and finally, assessing the consequences of these responses both for individual organizations and subsectors and for nonprofit America as a whole. The balance of this chapter offers such an account. To set the stage, however, it may be useful to explain more fully what the nonprofit sector is and why it deserves our attention.

## **What Is the Nonprofit Sector and Why Do We Need It?**

The nonprofit sector is a vast and diverse assortment of organizations. It includes most of the nation's premier hospitals and universities, almost all of its orchestras and opera companies, a significant share of its theaters, all of its religious congregations, the bulk of its environmental advocacy and civil rights

organizations, and huge numbers of its family service, children's service, neighborhood development, antipoverty, and community health facilities. It also includes the numerous support organizations, such as foundations and community chests, that help to generate financial assistance for these organizations, as well as the traditions of giving, volunteering, and service they help to foster.

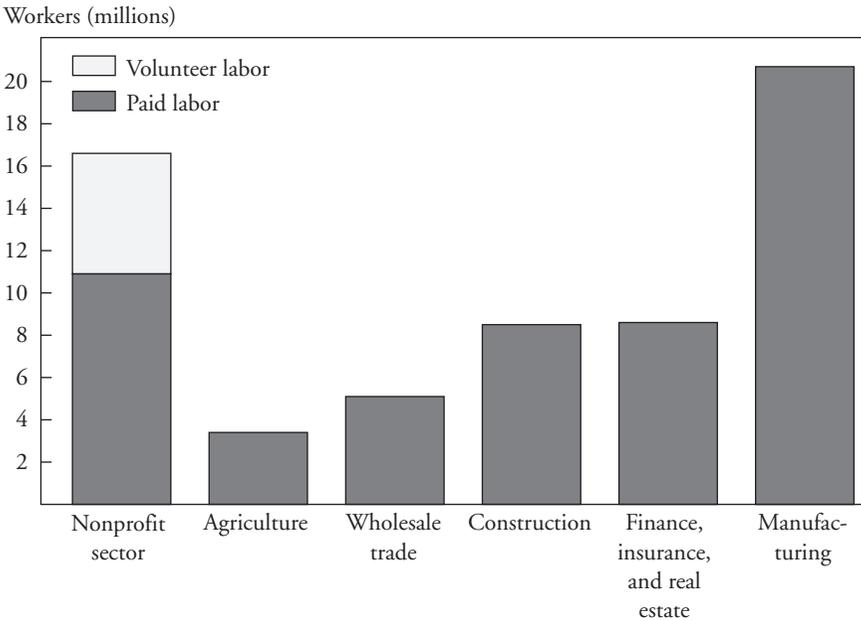
More formally, we focus here on organizations that are eligible for exemption from federal income taxation under Section 501(c)(3) of the tax code, plus the closely related "social welfare organizations" eligible for exemption under Section 501(c)(4) of this code. Included here are organizations that operate "exclusively for religious, charitable, scientific, or educational purposes" and that do not distribute any profits they may generate to any private shareholder or individual. Alone among the twenty-six types of organizations exempted from federal income taxation, the 501(c)(3) organizations are also eligible to receive tax-deductible contributions from individuals and businesses, a reflection of the fact that they are expected to serve broad public purposes as opposed to the interests and needs of the members of the organization alone.<sup>7</sup>

### *Scale*

No one knows for sure how many such nonprofit organizations exist in the United States, since large portions of the sector are essentially unincorporated and the data available on even the formal organizations are notoriously incomplete. A conservative estimate puts the total number of formally constituted 501(c)(3) and (c)(4) organizations at 1.2 million as of the mid-1990s, including an estimated 350,000 churches and other religious congregations.<sup>8</sup> As of 1998, these organizations employed close to 11 million paid workers, or over 7 percent of the U.S. work force, and enlisted the equivalent of another 5.7 million full-time employees as volunteers.<sup>9</sup> This means that paid employment alone in nonprofit organizations is three times that in agriculture, twice that in wholesale trade, and nearly 50 percent greater than that in both construction and finance, insurance, and real estate, as shown in figure 1-1. With volunteer labor included, employment in the nonprofit sector, at 16.6 million, approaches that in all branches of manufacturing combined (20.5 million).<sup>10</sup>

Most of this nonprofit employment is concentrated in three fields—health (43 percent), education (22 percent), and social services (18 percent). With volunteers included, the distribution of employment changes significantly, with the religious share swelling to 23 percent and health dropping to 34 percent (figure 1-2).

These large categories disguise, however, the huge array of separate services and activities in which nonprofit organizations are involved. A classification system developed by the National Center for Charitable Statistics, for example, identifies no fewer than twenty-six major fields of nonprofit activity and sixteen functions—from accreditation to fundraising—in each. Each of the major fields

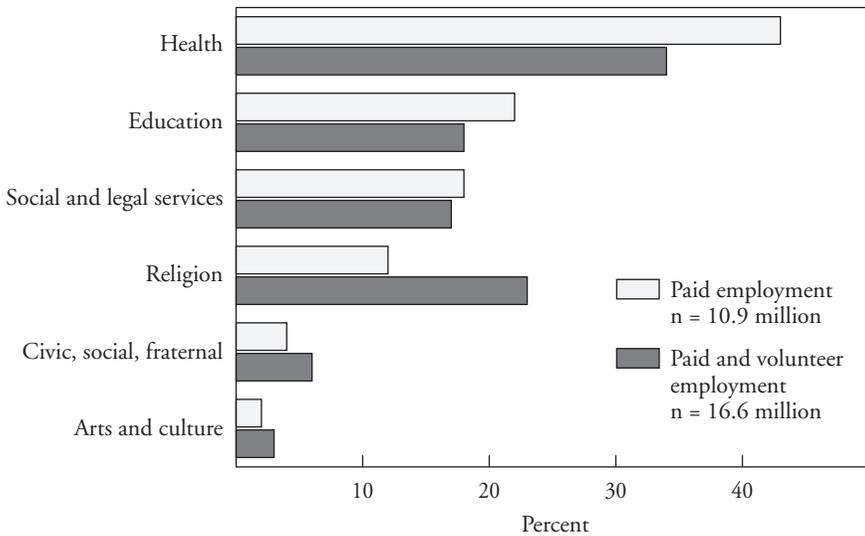
Figure 1-1. *Nonprofit Employment in Relation to Employment in Major U.S. Industries, 1998*

Source: Murray S. Weitzman, Nadine Tai Jalandoni, Linda M. Lampkin, and Thomas H. Pollack, *The New Nonprofit Almanac and Desk Reference* (San Francisco: Jossey-Bass, 2002), pp. 33, 23, 80; U.S. Census Bureau, *Statistical Abstract of the United States*, 120th ed. (Washington: U.S. Government Printing Office, 2000), p. 420.

is then further subdivided into subfields. Thus, for example, the field of arts, culture, and humanities has fifty-six subfields, and the field of education has forty-one. Altogether, this translates into several thousand potential different types of nonprofit organizations.<sup>11</sup>

Even this fails to do justice to the considerable diversity of the nonprofit sector. Most of the employment and economic resources of this sector are concentrated in large organizations. However, most of the organizations are quite small, with few or no full-time employees. Of the nearly 670,000 organizations recorded on the Internal Revenue Service's list of formally registered 501(c)(3) organizations (exclusive of religious congregations and foundations) in 1998, only about a third, or 224,000, filed the information form (Form 990) required of all organizations with expenditures of \$25,000 or more. The remaining two-thirds of the organizations were thus either inactive or below the \$25,000 spending threshold for filing.<sup>12</sup> Even among the filers, moreover, the top 4 percent accounted for nearly 70 percent of the reported expenditures, while the

Figure 1-2. *Distribution of Nonprofit Employment, Paid and Volunteer, by Field, 1998*



Source: Author's estimates based on data in Weitzman and others, *The New Nonprofit Almanac and Desk Reference* (San Francisco: Jossey-Bass, 2002); Virginia B. Hodgkinson and Murray S. Weitzman, *Nonprofit Almanac: 1996/97* (San Francisco: Jossey-Bass, 1996).

bottom 40 percent, with expenditures of less than \$100,000 each, accounted for less than 1 percent of the total.<sup>13</sup>

### *Roles and Functions*

Quite apart from their economic importance, nonprofit organizations make crucial contributions to national and community life.<sup>14</sup>

**THE SERVICE ROLE.** In the first place, nonprofit organizations are *service providers*: they deliver much of the hospital care, higher education, social services, cultural entertainment, employment and training, low-income housing, community development, and emergency aid services available in our country. More concretely, this set of organizations constitutes:

- Half of the nation's hospitals,
- One-third of its health clinics,
- Over a quarter of its nursing homes,
- Nearly half (46 percent) of its higher education institutions,
- Four-fifths (80 percent) of its individual and family service agencies,
- 70 percent of its vocational rehabilitation facilities,

- 30 percent of its daycare centers,
- Over 90 percent of its orchestras and operas,
- The delivery vehicles for 70 percent of its foreign disaster assistance.

While disagreements exist over how “distinctive” nonprofit services are compared to those provided by businesses or governments, nonprofits are well known for identifying and addressing unmet needs, for innovating, and for delivering services of exceptionally high quality. Thus nonprofit organizations pioneered assistance to AIDS victims, hospice care, emergency shelter for the homeless, food pantries for the hungry, drug abuse treatment efforts, and dozens more too numerous to mention. Similarly, many of the premier educational and cultural institutions in the nation are private, nonprofit organizations—institutions like Harvard, Princeton, Johns Hopkins, the Metropolitan Museum of Art, and the Cleveland Symphony, to name just a few. While public and for-profit organizations also provide crucial services, there is no denying the extra dimension added by the country’s thousands of private, nonprofit groups in meeting public needs that neither the market nor the state can, or will, adequately address.

**THE ADVOCACY ROLE.** In addition to delivering services, nonprofit organizations also contribute to national life by identifying unaddressed problems and bringing them to public attention, by protecting basic human rights, and by giving voice to a wide assortment of social, political, environmental, ethnic, and community interests and concerns. Most of the social movements that have animated American life over the past century or more operated in and through the nonprofit sector. Included here are the antislavery, women’s suffrage, populist, progressive, civil rights, environmental, antiwar, women’s, gay rights, and conservative movements. The nonprofit sector has thus operated as a critical social safety valve, permitting aggrieved groups to bring their concerns to broader public attention and to rally support to improve their circumstances. This advocacy role may, in fact, be more important to the nation’s social health than the service functions the sector also performs.

**THE EXPRESSIVE ROLE.** Political and policy concerns are not the only ones to which the nonprofit sector gives expression. Rather, this set of institutions provides the vehicles through which an enormous variety of other sentiments and impulses—artistic, religious, cultural, ethnic, social, recreational—also find expression. Opera companies, symphonies, soccer clubs, churches, synagogues, fraternal societies, book clubs, and Girl Scouts are just some of the manifestations of this expressive function. Through them, nonprofit organizations enrich human existence and contribute to the social and cultural vitality of community life.

**THE COMMUNITY-BUILDING ROLE.** Nonprofit organizations are also important in building what scholars are increasingly coming to call social capital—

those bonds of trust and reciprocity that seem to be crucial for a democratic polity and a market economy to function effectively.<sup>15</sup> Alexis de Tocqueville understood this point well when he wrote in *Democracy in America*:

Feelings and opinions are recruited, the heart is enlarged, and the human mind is developed, only by the reciprocal influence of men upon one another . . . these influences are almost null in democratic countries; they must therefore be artificially created and this can only be accomplished by associations.<sup>16</sup>

By establishing connections among individuals, involvement in associations teaches norms of cooperation that carry over into political and economic life.

VALUE GUARDIAN.<sup>17</sup> Finally, nonprofit organizations embody, and therefore help to nurture and sustain, a crucial national value emphasizing individual initiative in the public good. They thus give institutional expression to two seemingly contradictory principles that are both important parts of American national character: the principle of *individualism*—the notion that people should have the freedom to act on matters that concern them—and the principle of *solidarity*—the notion that people have responsibilities not only to themselves but also to their fellow human beings and to the communities of which they are part. By fusing these two principles, nonprofit organizations reinforce both, establishing an arena of action through which individuals can take the initiative not simply to promote their own well-being but to advance the well-being of others as well. This is not simply an abstract function, moreover. It takes tangible form in the more than \$200 billion in private charitable gifts that nonprofit organizations help to generate from the American public annually and in the 15.8 billion hours of volunteer time they stimulate for a diverse array of purposes.

## Challenges and Opportunities

Despite the important contributions they make, nonprofit organizations find themselves in a time of testing at present. To be sure, they are not alone in this. But the challenges facing nonprofit organizations are especially daunting, since they go to the heart of the sector's operations and raise questions about its very existence.

Nonprofit organizations have generally responded energetically and creatively to these pressures. What is more, they have taken ample advantage of the opportunities they also enjoy. But the responses have been uneven and not without risks. It is therefore necessary to look more closely at these challenges and opportunities and at the way nonprofit organizations have responded to them.

*Key Challenges*

Fundamentally, nonprofit America has confronted six critical challenges over the recent past. From all indications, moreover, these challenge seem likely to persist—and in some cases to intensify—in the years ahead.

**THE FISCAL CHALLENGE.** In the first place, America's nonprofit organizations have suffered from a persistent fiscal squeeze. To be sure, that squeeze was relieved in part in the aftermath of World War II, and particularly during the 1960s, thanks to a significant infusion of government support. Although it is not widely recognized, the government efforts to stimulate scientific advance and overcome poverty and ill health during this period relied heavily on nonprofit organizations for their operation.<sup>18</sup> By the late 1970s as a consequence, federal support to American nonprofit organizations outdistanced private charitable support by a factor of two to one, while state and local governments provided additional aid. What is more, this support percolated through a wide swath of the sector, providing needed financial nourishment to universities, hospital, clinics, daycare centers, nursing homes, employment and training organizations, family service agencies, and many more. Indeed, much of the modern nonprofit sector as we know it took shape during this period as a direct outgrowth of expanded government support.

This widespread government support to nonprofit organizations suffered a severe shock, however, in the early 1980s. Committed to a policy of fiscal restraint, and seemingly unaware of the extent to which public resources were underwriting private, nonprofit action, the Reagan administration attacked federal spending in precisely the areas where federal support to nonprofit organizations was most extensive—social and human services, education and training, community development, and nonhospital health. Although the budget cuts that occurred were nowhere near as severe as originally proposed, federal support to nonprofit organizations, outside of Medicare and Medicaid, declined by approximately 25 percent in real dollar terms in the early 1980s and returned to its 1980 level only in the late 1990s.<sup>19</sup> Although some state governments boosted their own spending in many of these fields, the increases were not sufficient to offset the federal cuts. Nonprofit organizations in the fields of community development, employment and training, social services, and community health were particularly hard-hit by these reductions. Although the government's fiscal pressure significantly eased in subsequent years, the experience of the 1980s and early 1990s has left a residue of anxiety that new budget pressures are now reviving.

Not just the amount, but also the form, of public sector support to the nonprofit sector changed during this period, moreover. Where earlier government offered grants and contracts to nonprofit organizations and gave nonprofits the

inside track, during the 1980s and 1990s government program managers were encouraged to promote for-profit involvement in government contract work, including that for human services.<sup>20</sup> More significantly, the use of grants and contracts itself gave way increasingly to forms of assistance such as vouchers and tax expenditures that channel aid to consumers rather than producers, thus requiring nonprofits to compete for clients in the market, where for-profits have traditionally had the edge.<sup>21</sup> Already by 1980, the majority (53 percent) of federal assistance to nonprofit organizations took the form of such consumer subsidies, much of it through the Medicare and Medicaid programs. By 1986 this stood at 70 percent, and it continued to rise into the 1990s.<sup>22</sup> In part, this shift resulted from the concentration of the budget cuts of the 1980s on the so-called discretionary spending programs, which tended to be supply-side grant and contract programs, while Medicare and Medicaid—both of them demand-side subsidies—continued to grow.<sup>23</sup> In part also, however, it reflected the ascendance of conservative political forces that favored forms of assistance that maximized consumer choice. The price of securing conservative support for new or expanded programs of relevance to nonprofit organizations in the late 1980s and 1990s, therefore, was to make them vouchers or tax expenditures. The new Childcare and Development Block Grant enacted in 1990 and then reauthorized and expanded as part of the welfare reform legislation in 1996 specifically gave states the option to use the \$5 billion in federal funds provided for daycare to finance voucher payments to eligible families rather than grants or contracts to daycare providers, and most states have pursued this option.<sup>24</sup> In addition, another \$2 billion in federal daycare subsidies is delivered through a special childcare tax credit. Nonprofit daycare providers, like their counterparts in other fields, have thus been thrown increasingly into the private market to secure even public funding for their activities. As a result, they have been obliged to master complex billing and reimbursement systems and to learn how to “market” their services to potential “customers.”

Not only did government support to nonprofit organizations change its form during this period, but so did important elements of private support. The most notable development here was the emergence of “managed care” in the health field, displacing the traditional pattern of fee-for-service medicine. Medicare provided an important impetus for this development by replacing its cost-based reimbursement system for hospitals in the early 1980s with a system of fixed payments for particular procedures. Corporations, too, responded to the rapid escalation of health care benefits for their workers by moving aggressively during the 1980s to replace standard fee-for-service insurance plans with managed care plans that featured up-front “capitation” payments to managed care providers. These providers then inserted themselves between patients and health care providers, negotiating rates with the providers and deciding which procedures were truly necessary. By 1997, close to 75 percent of the employees in medium

and large establishments, and 62 percent of the employees in small establishments, were covered by some type of managed care plan.<sup>25</sup> More recently, managed care has expanded into the social services field, subjecting nonprofit drug treatment, rehabilitation service, and mental health treatment facilities to the same competitive pressures and reimbursement limits as hospitals have been confronting.

Adding to the fiscal pressure nonprofits face has been the inability of private philanthropy to offset cutbacks in government support and finance expanded nonprofit responses to community needs. To be sure, private giving has grown considerably in recent years. Between 1977 and 1997, for example, total private giving grew by 90 percent after adjusting for inflation, roughly equivalent to the growth of gross domestic product. However, this lumps the amounts provided for the actual operations of charities in a given year with large endowment gifts to foundations, universities, and other institutions that are typically not available for use in a given year, as well as with gifts to religious congregations, most of which go to the upkeep of the congregations and clergy, as Mark Chaves shows in chapter 8 of this volume. When we focus on the private gifts available to support nonprofit human service, arts, education, health, and advocacy organizations in a given year, the growth rate was closer to 62 percent, still impressive but well below the 81 percent growth rate of gross domestic product.<sup>26</sup> Indeed, as a share of personal income, private giving has been declining steadily in the United States: from an average of 1.86 percent in the 1970s, down to 1.78 percent in the 1980s, and to 1.72 percent in the early 1990s. Especially distressing, as Virginia Hodgkinson notes in chapter 12, has been the disappointing rate of giving by the well-off, which has fallen considerably as a share of their income over the past decade or more, perhaps as a result of tax changes that lowered the tax rates of the wealthy and hence their financial incentives to give.<sup>27</sup> While giving as a share of personal income increased somewhat in the late 1990s, it did not return to its 1970s level; and the stock market sell-off and recession of 2000–02 have constrained its further growth despite the outpouring of support in response to September 11.

Although giving has grown in absolute terms, therefore, it accounted for only 8 percent of the growth of the nonprofit sector outside of religion between 1977 and 1997. As a share of total sector income, private giving actually lost ground, falling from 18 percent of the total in 1977 to 12 percent in 1997, and there is little evidence that this has changed substantially in recent years.<sup>28</sup> Indeed, many types of nonprofit organizations fear that September 11 may bring a decline in charitable support as resources are shifted to post-disaster relief and recovery.

**THE COMPETITION CHALLENGE.** In addition to a fiscal challenge, nonprofit America has also faced a serious competitive challenge as a result of the striking

Table 1-1. *Nonprofit and For-Profit Roles in Select Fields, 1982–97*

<i>Field</i>	<i>Percentage nonprofit</i>		<i>Percentage change in relative nonprofit share</i>
	1982	1997	
<i>Employment</i>			
Child daycare	52	38	-27
Job training	93	89	-4
Individual and family services	94	91	-3
Home health	60	28	-53
Kidney dialysis centers	22	15	-32
<i>Facilities, participation</i>			
Dialysis centers	58 <sup>a</sup>	32	-45
Rehabilitation hospitals	70 <sup>a</sup>	36	-50
Home health agencies	64 <sup>a</sup>	33	-48
Health maintenance organizations	65 <sup>a</sup>	26	-60
Residential treatment facilities for children	87 <sup>b</sup>	68	-22
Psychiatric hospitals	19 <sup>a</sup>	16	-16
Hospices	89 <sup>c</sup>	76	-15
Mental health clinics	64 <sup>b</sup>	57	-11
Higher education enrollments	96	89	-7
Nursing homes	20 <sup>b</sup>	28	+ 40
Acute care hospitals	58 <sup>a</sup>	59	+ 2

Source: U.S. Census Bureau, *U.S. Economic Census* (Washington: U.S. Census Bureau, 1999); Bradford Gray and Mark Schlesinger, chapter 2 of this volume, fig. 2-1; National Center for Education Statistics, *Digest of Education Statistics 2000* (Washington: Department of Education, National Center for Education Statistics, 2000), pp. 202–03, 209.

a. Initial year for data is 1985, not 1982.

b. Initial year for data is 1986, not 1982.

c. Initial year for data is 1992.

growth of for-profit involvement in many traditional fields of nonprofit activity, from health care and welfare assistance to higher education and employment training. This, too, is not a wholly new development. But the scope of competition appears to have broadened considerably in recent years, and in an increasing range of fields nonprofits have been losing “market share.” Thus, as shown in table 1-1, the nonprofit share of daycare jobs dropped from 52 to 38 percent between 1982 and 1997, a decline of some 27 percent. Similarly sharp declines in the relative nonprofit share occurred among rehabilitation hospitals, home health agencies, health maintenance organizations, kidney dialysis centers, mental health clinics, and hospices. In many of these fields, the absolute number of nonprofit facilities continued to grow, but the for-profit growth outpaced it. And in at least one crucial field—acute care hospitals—while the nonprofit *share* increased slightly, a significant reduction occurred in the *absolute number*

of nonprofit (as well as public) facilities, so that the for-profit share of the total increased even more.

The range of for-profit firms competing with nonprofits has grown increasingly broad, moreover. For example, the recent welfare reform legislation has attracted defense contractors like Lockheed-Martin into the social welfare field because it puts a premium on the information-processing and contract management skills they have developed as master contractors on huge military systems. Under many of these new arrangements, in fact, nonprofit providers are serving as subcontractors to for-profit firms hired by states or local governments to manage the welfare reform process. Even the sacrosanct field of charitable fundraising has recently experienced a significant for-profit incursion in the form of financial service firms such as Fidelity and Merrill Lynch, as Leslie Lenkowsky and Virginia Hodgkinson report in chapters 11 and 12, respectively, of this volume. By 2000, the Fidelity Charitable Gift Fund, established in 1991, had attracted more assets than the nation's largest community foundation and distributed three times as much in grants.<sup>29</sup>

The reasons for this striking pattern of for-profit success are by no means clear and vary from field to field. The shift in forms of public funding mentioned earlier has very likely played a role, however, forcing nonprofits to compete for subsidized customers in the marketplace, where for-profit firms have a natural advantage. The rise of health maintenance organizations and other "third-party payment" methods has had a similar effect, as Bradford Gray and Mark Schlesinger argue in chapter 2 of this volume, since such organizations emphasize price rather than quality or community roots in choosing providers, thus minimizing the comparative advantages of nonprofits. Technological developments have also given for-profit firms a strategic edge because technology puts a premium on access to capital and nonprofits have an inherent difficulty generating capital because their nonprofit status makes it impossible for them to sell shares in the equity markets. Nonprofits are therefore at a particular disadvantage in fields where rapid increases in demand or new technological innovations necessitate increased capital expenditures.<sup>30</sup>

**THE EFFECTIVENESS CHALLENGE.** One consequence of the increased competition nonprofits are facing has been to intensify the pressure on them to perform and to demonstrate that performance. The result is a third challenge: the effectiveness challenge. As management expert William Ryan has written, "Nonprofits are now forced to reexamine their reasons for existing in light of a market that rewards discipline and performance and emphasizes organizational capacity rather than for-profit or nonprofit status and mission. Nonprofits have no choice but to reckon with these forces."<sup>31</sup> This runs counter to long-standing theories in the nonprofit field that have emphasized this sector's distinctive advantage precisely in fields where "information asymmetry" makes it difficult

to demonstrate performance and where “trust” is consequently needed instead. Because they are not organized to pursue profits, it was argued, nonprofits are more worthy of such trust and therefore are more reliable providers in such difficult-to-measure fields.<sup>32</sup>

In the current climate, however, such theories have few remaining adherents, at least among those who control the sector’s purse strings. Government managers, themselves under pressure to demonstrate results because of the recent Government Performance and Results Act, are increasingly pressing their nonprofit contractors to deliver measurable results, too. Not to be outdone, prominent philanthropic institutions have jumped onto the performance bandwagon. United Way of America, for example, thus launched a bold performance measurement system in the mid-1990s complete with website, performance measurement manual, and video in order to induce member agencies to require performance measurement as a condition of local funding. Numerous foundations have moved in a similar direction, increasing their emphasis on evaluation both of their grantees and of their own programming.<sup>33</sup> Indeed, a new foundation affinity group, Grantmakers for Effective Organizations, has been formed, and a new “venture philanthropy” model is attracting numerous adherents.<sup>34</sup> The key to this model is an investment approach to grantmaking that calls on philanthropic institutions to invest in organizations rather than individual programs, to take a more active hand in organizational governance and operations, and to insist on measurable results.

The resulting “accountability environment” in which nonprofits are having to operate will doubtless produce many positive results. But it will also increase the pressures on hard-pressed nonprofit managers to demonstrate progress in ways that neither they, nor anyone else, may be able to accomplish, at least not without far greater resources than are currently available for the task. What is more, as Evelyn Brody shows in chapter 15, accountability expectations often fail to acknowledge the multiple stakeholders whose demands for accountability nonprofits must accommodate. The risk is great, therefore, that the measures most readily at hand, or those most responsive to the market test, will substitute for those most germane to the problems being addressed. That, at any rate, is the lesson of public sector experience with performance measurement, and the increased focus on price rather than quality or community benefit in third-party contracting with nonprofit health providers certainly supports this observation.<sup>35</sup>

**THE TECHNOLOGY CHALLENGE.** Pressures from for-profit competitors have also accelerated the demands on nonprofits to incorporate new technology into their operations. Indeed, technology has become one of the great wild cards of nonprofit evolution. Like the other challenges identified here, technology’s impact is by no means wholly negative. As Elizabeth Boris and Jeff Krehely argue in chapter 9 of this volume, new information technology is increasing the

capacity of nonprofits to advocate by reducing the costs of mobilizing constituents and connecting to policymakers and allies. This observation finds confirmation in Jeffrey Berry's careful analysis of the growing influence of citizen groups, which he attributes in important part to access to television news.<sup>36</sup> Technology is also opening new ways to tap charitable contributions. The September 11 tragedy may well have marked a turning point in this regard, since some 10 percent of the funds raised came via the Internet.<sup>37</sup>

Nonprofit education, health, and arts institutions are also benefiting from technological change. As Atul Dighe shows in chapter 16 of this volume, medical practice has already been transformed by new technology, but genetic engineering and the new field of bionics linking biosciences with electronics promise even more dramatic breakthroughs, making it possible to deliver medical services not only in one's home, but in one's body through the implantation of biosensors that can think and react. Digitization is having a similar effect in the arts world, as Margaret Wyszomirski points out in chapter 5 of this volume. Three on-site classical music websites are already in operation, providing live, streaming transmissions of orchestral concerts from around the world, and this is just the beginning. A project of the Mellon Foundation is digitizing the collections of hundreds of museums at a level of technical sophistication unmatched by anything even imagined before. Cultural institutions sit on vast stockpiles of cultural raw material that is potentially available for exploitation in the new digital era, and many institutions are taking advantage of the opportunities.

But enticing as the opportunities opened by technological change may be to the nation's nonprofit institutions, they pose equally enormous challenges. Most obvious, perhaps, are the financial challenges. As one recent study notes, "Information technologies are resource intensive. They entail significant purchase costs, require significant training and upkeep, and yet become obsolete quickly."<sup>38</sup> Because of the structural disadvantages nonprofits face in raising capital due to their inability to enter the equity markets, however, the massive intrusion of new technological requirements into their work puts them at a distinct disadvantage vis-à-vis their for-profit competitors. We have already seen the consequences of this in the health maintenance organization industry, where the lack of capital following the discontinuation of government funding led to the rapid loss of market share to for-profit firms, which were better able to capitalize the huge investments in information-processing equipment required to manage the large risk pools that make managed care viable. Similar pressures are now at work in the social services industry, where managed care is also taking root.

Not only does technology threaten to alter further the balance between nonprofits and for-profits, but also it threatens to alter the structure of the nonprofit sector itself, advantaging larger organizations over smaller ones. This is due in part to the heavy fixed costs of the new technology. Already, concerns about a "digital divide" are surfacing within the sector, as survey after survey reveals the

unequal distribution of both hardware and the capacity to adapt the hardware to organizational missions.<sup>39</sup> Although initially stimulating competition by giving even small startups access to huge markets, information technology also creates “network effects” that accentuate the advantages of dominant players.<sup>40</sup> Significant concerns have thus surfaced that e-philanthropy will allow large, well-known national nonprofits to raid the donor bases of local United Ways and operating charities and that information technology more generally will give exceptional advantages to large nationally prominent agencies in the competition for business partners, government funding, and foundation grants.

But the challenges posed by technology go far beyond financial or competitive considerations. Also at stake are fundamental philosophical issues that go to the heart of the nonprofit sector’s mission and modes of operation. As Wyszomirski shows in chapter 5, such issues have surfaced especially vividly in the arts arena where the new technology raises fundamental questions of aesthetics, creative control, and intellectual property rights. Similar dilemmas confront educational institutions that are tempted by the new technologies to “brand” their products and package them for mass consumption, but at the risk of alienating their professorate, losing the immediacy of direct student-faculty contact, and giving precedence to the packaging of knowledge rather than to its discovery. How these technological dilemmas are resolved could well determine how the nonprofit sector evolves in the years ahead.

**THE LEGITIMACY CHALLENGE.** The moral and philosophical challenges that American nonprofit organizations are confronting go well beyond those posed by new technology, however. Rather, a serious fault line seems to have opened in the foundation of public trust on which the entire nonprofit edifice rests. This may be due in part to the unrealistic expectations that the public has of these institutions, expectations that the charitable sector ironically counts on and encourages. Also at work, however, has been the strident indictment that conservative politicians and commentators have lodged against many nonprofit organizations over the past decade. The central charge in this indictment is that nonprofit charitable organizations have become just another special interest, regularly conspiring with government bureaucrats to escalate public spending and doing so not so much out of real conviction about the needs being served as out of a desire to feather their own nests. Heritage Foundation president Edward Feltner put this case especially sharply in 1996, criticizing charities for urging Congress to expand social welfare spending, while themselves “feeding at the public trough.”<sup>41</sup> Entire organizations have been formed, in fact, to “dehalo” the nonprofit sector in this way, charging that a “new kind of nonprofit organization” has emerged in recent years “dedicated not to voluntary action, but to an expanded government role in our lives.”<sup>42</sup> To remedy this, advocates of this view rallied behind the so-called Istook amendment, which sought to

limit the advocacy activity of nonprofit organizations by prohibiting any nonprofit organization receiving government support from using any more than 5 percent of its *total* revenues, not just its public revenues, for advocacy or lobbying activities.

Similar challenges to the legitimacy of nonprofit organizations have arisen from critics who take nonprofits to task for becoming *overly* professional and thus losing touch with those they serve. This line of argument has a long lineage in American social science, as evidenced by the brilliant analysis by historian Roy Lubove of the professionalization of social work, which led social workers away from social diagnosis, community organizing, and social reform toward a client-focused, medical model of social work practice.<sup>43</sup> More recently, critics on the left have charged nonprofit organizations generally with contributing to the over-professionalization of social concerns. By redefining basic human needs as “problems” that only professionals can resolve, these critics contend, this over-professionalization alienates people from the helping relationships they could establish with their neighbors and kin.<sup>44</sup> By embracing professionalism, nonprofit organizations destroy community rather than building it up, the critics note. On the right, critics have been equally derisive of the professionalized human service apparatus, charging it with inflating the cost of dealing with social problems by “crowding out” lower-cost alternative service delivery mechanisms that are at least as effective.<sup>45</sup>

These sentiments echo loudly in the Bush administration’s 2001 proposal to privilege “faith-based charities” in the distribution of federal assistance. A principal appeal of this idea is the prospect of replacing formal, professionalized nonprofit organizations with informal church groups staffed by dedicated volunteers. This reinforces a quaint nineteenth-century image of how charitable organizations are supposed to operate, an image that competitive pressures, accountability demands, and technological change have made increasingly untenable.

Coupled with a spate of high-profile scandals in the early 1990s, these criticisms seem to have shaken public confidence in charitable institutions. Surveys taken in 1994 and 1996 find only 33 and 37 percent of respondents, respectively, expressing “a great deal” or “quite a lot” of confidence in nonprofit human service agencies, well behind the proportions expressing similar levels of confidence in the military and small business (see table 1-2).<sup>46</sup> This improved considerably in the late 1990s, perhaps as a consequence of the perceived success of welfare reform. Yet, even at this latter date, while a substantial majority of respondents agreed that “charitable organizations play a major role in making our communities better places to live,” only 20 percent “strongly agreed” with this statement. And only 10 percent were willing to agree “strongly” that most charities are “honest and ethical in their use of donated funds.” All of this suggests that America’s nonprofit institutions are delicately balanced on a knife-

Table 1-2. *Public Attitudes toward Charitable and Other Organizations in the United States, 1992–99*

<i>Institutions</i>	<i>1992–96</i>			<i>1999</i>	
	<i>Percent expressing a great deal or quite a lot of confidence</i>			<i>Percent expressing confidence</i>	
	<i>1992</i>	<i>1994</i>	<i>1996</i>	<i>A great deal</i>	<i>A great deal or quite a lot</i>
Youth development	48	47	50	33	72
Human services	37	33	37	29	68
Religious organizations	47	50	55	32	61
Private higher education	49	48	57	23	59
Military	49	49	54	22	57
Small business	46	53	56	16	55
Health organizations	40	36	39	15	43
Local government	24	23	31	9	33
State government	19	21	26	8	31
Federal government	18	19	23	8	27
Major corporations	19	22	24	7	29

Source: Independent Sector, *Giving and Volunteering in the United States, 1999* (Washington: Independent Sector, 1999), pp. 3, 5.

edge of public support, with most people willing to grant them the benefit of the doubt, but with a strong undercurrent of uncertainty and concern.<sup>47</sup> As a consequence, a relative handful of highly visible scandals—such as the United Way scandal of the early 1990s, the New Era Philanthropy scandal of the mid-1990s, or the Red Cross difficulties in the wake of September 11—can have an impact that goes well beyond their actual significance.

**HUMAN RESOURCE CHALLENGE.** Inevitably, fiscal stress and public ambivalence toward the nonprofit sector have taken their toll on the sector's human resources. Experts in the child welfare field, for example, have recently identified "staff turnover" as "perhaps the most important problem" facing the field, citing "stress, . . . overwhelming accountability requirements, and concern over liability" as the principal causes.<sup>48</sup> As Shepard Forman and Abby Stoddard show in chapter 7, similar problems afflict the international relief field due to the explosion of complex humanitarian crises that blend enormous relief challenges with complicated political and military conflicts.

Especially difficult has been the recruitment and retention of frontline service workers for whom salary, benefit, and safety issues are particularly important, but retention of managerial personnel has also grown increasingly problematic. One study of graduates of public policy programs reports, for example, that the

proportion of these public-spirited young people who take their first job in nonprofit organizations doubled between the early 1970s and the early 1990s. However, the nonprofit sector's retention rate for these personnel has declined over time, with more turning to the for-profit sector as an alternative.<sup>49</sup> Of special concern is the turnover of talent and burnout at the executive director level. Executive directors who came into the field to pursue the social missions of their agencies find themselves expected to function instead as aggressive entrepreneurs leading outward-oriented enterprises able to attract paying customers, while retaining the allegiance of socially committed donors and boards, all of this in a context of growing public scrutiny and mistrust. According to one recent study, a surprising two-thirds of the executive directors in a national sample of nonprofit agencies were in their first executive director position, and over half of these had held the job for four years or less. Although most reported enjoying their job, a third indicated an intention to leave it within two years, and even among those likely to take another job in the nonprofit sector, only half indicated that their next job was likely to be as an executive director.<sup>50</sup> As Wyszomirski reports in chapter 5, leadership recruitment has become a particular challenge in the arts field, where the vacancy rate for art museum directors hit a fifteen-year high in 1999.

**SUMMARY.** In short, nonprofit America has confronted a difficult set of challenges over the recent past. Fiscal stress, increased competition, rapidly changing technology, and new accountability expectations have significantly expanded the pressures under which these organizations must work, and this has affected the public support these organizations enjoy and their ability to attract and hold staff.

### *Opportunities*

But challenges are not all that nonprofit America has confronted in the recent past. It has also had the benefit of a number of crucial opportunities, many of which seem likely to persist. Four of these in particular deserve special attention.<sup>51</sup>

**SOCIAL AND DEMOGRAPHIC SHIFTS.** In the first place, recent social and demographic shifts have created new demands for nonprofit services and new prospects for attracting the personnel these organizations will need. Included among these shifts are the following:

- The doubling of the country's elderly population between 1960 and 2000 and the prospect that there will be four times as many elderly Americans in 2025 as there were in 1960,

- The jump in the labor force participation rate for women, particularly married women, from less than 20 percent in 1960 to 64 percent in 1998,<sup>52</sup>

- The doubling of the country's divorce rate since the 1960s and the resulting sharp jump in the number of children involved in divorces,<sup>53</sup>

—A fivefold increase in the number of out-of-wedlock births, from roughly 225,000 in 1960 to more than 1.25 million per year by the mid-1990s,<sup>54</sup>

—The doubling of refugees admitted to the United States, from 718,000 between 1966 and 1980 to 1.6 million during the next fifteen years.<sup>55</sup>

Taken together, these and other sociodemographic changes have expanded the demand for many of the services that nonprofit organizations have traditionally provided, such as child daycare, home health and nursing home care, family counseling, foster care, relocation assistance, and substance abuse treatment and prevention. What is more, the demand for these services has spread well beyond the poor and now encompasses middle-class households with resources to pay for them, a phenomenon that one analyst has called “the transformation of social services.”<sup>56</sup> Indeed, the acceleration of modern life and the pressures on two-career families have led, as Dighe notes in chapter 16, to the “outsourcing” of key aspects of family life, from child daycare to tutoring and party arranging. Since nonprofit organizations are actively engaged in many of these fields, they stand to gain from this trend.

Equally important is the emergence of what Dighe, following demographer Paul Ray, calls the Cultural Creatives, a growing subgroup of the population that now numbers as many as 50 million people.<sup>57</sup> Cultural Creatives differ from both “Moderns” and “Traditionalists,” the two other dominant population groups in America, by virtue of their preference for holistic thinking, their cosmopolitanism, their social activism, and their insistence on finding a better balance between work and personal values than the Moderns seem to have found. Although they have yet to develop a full self-consciousness, Cultural Creatives are powerfully attracted to the mission orientation of the nonprofit sector and could well help to resolve some of the sector’s human resource challenges.

THE NEW PHILANTHROPY. Also working to the benefit of the nonprofit sector is a series of developments in private philanthropy. The first of these is the *intergenerational transfer of wealth* between the depression-era generation and the postwar baby boomers that is anticipated over the next forty years. Estimated to range anywhere from \$10 trillion to \$40 trillion or more, this wealth accumulated in the hands of the depression-era generation as a consequence of their relatively high propensity to save, their fortuitous investment during the 1950s and 1960s in relatively low-cost houses that then escalated in value, and the stock market surge of the 1980s and 1990s, which substantially boosted the value of their investments.<sup>58</sup>

A second development is the *new wealth* created by the dot-com economy and other powerful economic trends and policies during the 1980s and 1990s, substantially increasing income levels at the upper end of the income scale. Between 1979 and 1992, for example, the share of the nation’s wealth controlled by the top 1 percent of households climbed from 20 percent to over

40 percent. Indeed, one-third of the projected intergenerational transfer is expected to go to 1 percent of the baby boom generation, for an average inheritance of \$1.6 million per person among this select few.<sup>59</sup>

To be sure, lengthening life expectancy may dissipate much of this wealth in heavy health care and nursing home expenses. What is more, the stock market meltdown of 1999–2002 provides a powerful reminder of the ephemeral quality of much of the presumed new wealth. Nevertheless, with so much money “in play,” substantial opportunities likely exist for the expansion of charitable bequests. The fact that 60 percent of the mid-size and larger foundations in existence as of 1999 were created in the 1980s and 1990s certainly lends credence to this belief, although the phase-out of the estate tax enacted in 2001 may put a damper on the extent to which philanthropy will benefit from these developments by eliminating the major financial incentive for forming foundations.<sup>60</sup>

Also encouraging for nonprofit prospects are the new strategies of corporate social involvement that have surfaced in recent years and the *greater corporate willingness to engage in partnerships and collaborations with nonprofit organizations* that has resulted from them. Although corporate giving has proved far more disappointing than many hoped in the early 1980s, numerous corporations have begun integrating social responsibility activities into their overall corporate business strategies. This has been done in part out of altruistic motives, but in part also out of a recognition that such relationships can serve corporate strategic goals—by winning consumer confidence, ensuring corporations a “license to operate” in the face of increasingly mobilized consumer, environmental, and worker movements, and promoting employee loyalty and morale.<sup>61</sup> As such, they have a more secure base than altruism alone can provide. The result has been to make corporate managers available to nonprofit organizations, not simply as donors, but as allies and collaborators in a wide range of socially important missions, from improving the well-being of children to protecting natural resources. Although nonprofit reputations may be put at risk through such relationships, there are also intriguing possibilities for extremely productive partnerships.

**GREATER VISIBILITY AND POLICY SALIENCE.** Also working to the advantage of nonprofit organizations has been a spate of political developments that have substantially increased their visibility. For one thing, the policy environment ushered in by the elections of Margaret Thatcher in the United Kingdom and Ronald Reagan in the United States brought nonprofit organizations out of the obscurity to which the rise of the welfare state had consigned them over the previous half-century. Conservative politicians like Thatcher and Reagan needed an explanation for how social problems would be handled once government social welfare protections were cut, and the nonprofit sector offered a highly convenient one. Suddenly, attention to the nonprofit sector and philanthropy became a

central part of the policy dialogue, even though conservative politicians had to overlook the inconvenient fact that the nonprofit organizations they were championing were funded largely by the very government social welfare programs they were cutting. When the policy pendulum swung back to the left, as it did with the election of Tony Blair in the United Kingdom and Bill Clinton in the United States, nonprofit organizations remained very much on the policy screen, as evidenced by the “third way” rhetoric in the United Kingdom and similar formulations in Europe, which view active partnerships between government and the civil society sector as an alternative to relying solely on either the market or the state.<sup>62</sup>

Nonprofit organizations have also gained visibility as a result of the collapse of communism in Central Europe in the late 1980s and the proliferation of complex humanitarian crises in much of the developing world.<sup>63</sup> In both cases, nonprofit organizations have been prominently involved, stimulating change and offering alternative mechanisms of response. More recently, these organizations have benefited from growing concerns about the state of civic engagement in the United States. This is so because nonprofit organizations have been identified as crucial contributors to “social capital,” to the bonds of trust and reciprocity thought to be necessary to sustain civic involvement. Encouragement of a vital nonprofit sector thus has come to be seen as a critical prerequisite for a healthy democracy.<sup>64</sup>

Finally, the events of September 11 also increased the public’s recognition of the nonprofit sector. As noted earlier, nonprofit organizations were visible participants in the response to this tragedy. Beyond this, the September 11 events seem to have reawakened Americans to the importance of the functions that nonprofit institutions perform, functions such as serving those in need, building community, and encouraging values of care and concern.

**GROWTH OF GOVERNMENT SOCIAL WELFARE SPENDING.** Finally, and perhaps most important, government social welfare spending, which had stalled and in some cases reversed course in the early 1980s, resumed its growth in the late 1980s and into the 1990s. As noted in table 1-3, total public social welfare spending increased 36 percent in real, inflation-adjusted dollars between 1985 and 1995 compared to a 24 percent increase in the country’s real gross domestic product.<sup>65</sup> Particularly notable was the 69 percent growth in health spending, but significant increases were recorded in housing, education, and social service spending as well—trends that have continued in more recent years.

As reflected in the chapters by Steven Smith, Margaret Wyszomirski, Avis Vidal, and Bradford Gray and Mark Schlesinger, five factors seem to have been responsible for this growth:

—*Broadening of federal entitlement spending.* In the first place, spending under the basic government entitlement programs for health and income assistance

Table 1-3. *Growth in Real Government Social Welfare Spending*  
 Percentage change, 1985–95

<i>Function</i>	<i>Total</i>	<i>Federal</i>	<i>State and local</i>
Pensions	18	13	40
Income assistance	27	34	7
Health	69	67	73
Education	40	9	43
Elementary, secondary	-34	-34	-34
Higher	36	-23	31
Housing	54	63	-10
Social services	23	5	49
<i>Total</i>	36	30	45
Total without pensions, health	37	29	40

Source: U.S. Social Security Administration, *Annual Statistical Supplement to the Social Security Bulletin* (Washington: U.S. Department of Health and Human Services, Social Security Administration, 2000), pp. 119–222.

grew rapidly during this period, largely due to the steady broadening of eligibility. For example, coverage under the federal Supplemental Security Income (SSI) program, which was originally created to provide income support to the elderly poor, ballooned from 4.1 million recipients in 1980 to 6.6 million by 1999, largely as a result of aggressive efforts to enroll disabled people, including children and youth, in the program. The number of children covered by SSI increased from 71,000 in 1974 to over 1 million in 1996 as a consequence, boosting expenditures in real terms from \$16.4 billion in 1980 to \$30.2 billion in 1999.<sup>66</sup> And since SSI entitles participants to coverage under Medicaid—the federal health care financing program for the poor—this increase translated into Medicaid growth as well.

But this was not the only source of Medicaid eligibility expansion. Medicaid coverage was extended to fifty distinct subgroups during the late 1980s and early 1990s, including the homeless, newly legalized aliens, AIDS sufferers, recipients of adoption assistance and foster care, as well as broader categories of the disabled and the elderly. Between 1980 and 1998 as a consequence, Medicaid coverage jumped from 21.6 million people to 40.6 million.<sup>67</sup>

At the same time, the range of services these programs cover also expanded dramatically. Thus skilled nursing care, home health care, hospice care, and kidney dialysis services became eligible for Medicare coverage, while intermediate care for the mentally retarded, home health care, family planning, clinic care, child welfare services, and rehabilitation services were added to Medicaid. These changes, coupled with state options to add additional services (for example, physical therapy, medical social worker counseling, case management, trans-

Table 1-4. *Growth in Federal Entitlement Program Spending, 1980–99*

<i>Program</i>	<i>Spending (in billions of constant 1999 U.S. dollars)<sup>a</sup></i>		<i>Percentage change, 1980–99</i>
	<i>1980</i>	<i>1999</i>	
Medicare	79.9	212.0	+165
Medicaid <sup>b</sup>	56.8	189.5	+222
Supplemental Security Income <sup>b</sup>	9.5	30.9	+225
<i>Total</i>	146.2	432.4	+196
U.S. gross domestic product	4,900.9	8,856.5	+81

Source: U.S. House of Representatives, Committee on Ways and Means, *2000 Green Book: Background Material and Data on Programs within the Jurisdiction of the Committee on Ways and Means*, 106 Cong. 2 sess. (Washington, October 6, 2000), pp. 100, 912, 214; Council of Economic Advisers, *Economic Report of the President, 2002* (Washington: Executive Office of the President, Council of Economic Advisers, 2002), table B-2.

a. Based on chain-type price deflators for the service component of personal consumption expenditures.

b. Includes both federal and state spending.

portation),<sup>68</sup> transformed Medicaid from a relatively narrow health and nursing home program into a veritable social service entitlement program.

Reflecting these changes, as shown in table 1-4, spending on the major federal entitlement programs jumped nearly 200 percent in real terms between 1980 and 1999, more than twice the 81 percent real growth in the U.S. gross domestic product. Although reimbursement rates often still were not sufficient to cover the full costs of the services, the expansion in the pool of resources available was substantial.

—*New federal initiatives.* In addition to expanding existing programs, federal policymakers also created a variety of new programs to address long-standing or newly emerging social ills. For example, four federal childcare programs were enacted in 1988 and 1990 alone, and special programs were added as well for homeless people, AIDS sufferers, children and youth, people with disabilities, voluntarism promotion, drug and alcohol treatment, and home health care. Federal spending on the homeless, for example, went from virtually zero in 1986 to \$1.2 billion in fiscal 2000.<sup>69</sup>

—*Greater state activism.* Renewed federal activism was mirrored, and in some cases anticipated, by activism at the state and local level. In some cases, as Wyszomirski shows in the case of the arts, state and local governments replaced cuts in federal spending with their own new or expanded programs. In other cases, states found new veins of federal funding to tap as old ones ran dry. Under the “Medicaid maximization strategy,” for example, programs formerly funded entirely by the states, or by federal discretionary programs subjected to Reagan-era budget cuts, were reconfigured to make them eligible for funding under the

more-lucrative Medicaid or SSI programs. As Steven Smith reports in chapter 4 of this volume, mental health, mental retardation, maternal and child health rehabilitation, and AIDS services were special targets for this strategy, particularly as Medicaid expanded eligibility for pregnant women and children, and SSI (and hence Medicaid) expanded coverage for AIDS patients and the disabled.<sup>70</sup> Finally, a growing number of states opted to exploit the flexibilities built into the Medicaid program to extend care beyond the required minimum in order to address key social problems, such as teen pregnancy and drug abuse.<sup>71</sup> Taken together, these changes explain why state and local social welfare spending grew even faster than federal spending between 1985 and 1995 (45 versus 30 percent), as reflected in table 1-3.<sup>72</sup>

—*The welfare reform windfall.* A fourth factor contributing to the recent expansion of government spending in fields where nonprofits are active was the passage of the federal welfare reform legislation in 1996 and subsequent change in the welfare caseload. The Personal Responsibility and Work Opportunity Reconciliation Act (PRWORA) of 1996 essentially replaced the existing program of entitlement grants to states to help cover welfare payments to dependent children and families with a fixed federal grant that was guaranteed for six years, during which states were required to move welfare recipients into paying jobs. As part of this legislation, states were permitted to use a portion of these funds to finance not simply welfare payments but also a variety of work readiness, childcare, and human service activities. The result was to transform the existing welfare program into “a broad human services funding stream.”<sup>73</sup> When welfare rolls began to fall sharply in the late 1990s, thanks to the economic boom then in progress and the stringent work requirements built into the new law, states found themselves with a fiscal windfall since their welfare grants from the federal government were locked in at the preexisting levels, while their payments to recipients declined. States were thus able to invest the savings in a variety of service programs designed to prepare even more welfare recipients for work. By 1999, for example, spending on cash and work-based assistance under the welfare program had fallen to 60 percent of the total funds available, leaving 40 percent for a variety of childcare, work readiness, drug abuse treatment, and related purposes. As a result, the social welfare system was awash with funds.<sup>74</sup>

—*New tools.* Finally, given the prevailing climate of tax cuts and hostility to expanded government spending throughout the 1980s and early 1990s, policymakers increasingly responded to social welfare and related needs by relying more heavily on unconventional tools of government action, such as loan guarantees and tax subsidies, which do not appear as visibly on the budget.<sup>75</sup> The use of such tools is by no means entirely new, of course. The deduction for medical expenses and the exclusion of scholarship income, for example, have long been established features of the tax code. But the use of such tools in fields where nonprofits are active expanded considerably over the past decade or more

with the addition or extension of programs such as the childcare tax credit, the credit for student loan interest payments, the low-income housing tax credit, and the new market tax credit. As Kirsten Grønbjerg and Lester Salamon show in chapter 14, these alternative tools represented another \$315.2 billion in federal assistance in fields where nonprofits are active as of fiscal 2001. This represents a 123 percent increase in constant dollars over what was available through these tools a decade earlier, a rate of increase that exceeds even that achieved by the spending programs in these same fields. In many fields, such as daycare, the indirect subsidies available through the tax system now easily exceed those available through outright spending programs.<sup>76</sup> What is more, as noted earlier, the new tools generally deliver their benefits to consumers rather than producers, making it necessary for nonprofits to market their services in order to benefit from them.

To be sure, the expansion of government spending that occurred over the past decade did not affect all fields in which nonprofits are active. Public spending on higher education, for example, lost ground, although the creation of a direct student loan program and the continued expansion of tax and credit programs for higher education softened some of the blow. In addition, the shift in the character of public sector support from producer- to consumer-side subsidies meant that access to it grew more difficult, necessitating more intensive marketing efforts. Nevertheless, the increase that took place in government spending in fields where nonprofits are active has been striking, creating another important opportunity for the sector.

## **The Nonprofit Response: A Story of Resilience**

How has nonprofit America responded to the extraordinary combination of challenges and opportunities it has faced over the past decade and a half? Has the sector been able to cope with the challenges and take advantage of the opportunities? To what extent and with what consequences for its current health and character, and for its likely future evolution? It is to these questions that we now turn.

Based on the conventional wisdom about the responsiveness of nonprofit organizations, we should not expect very much. “Profit-making organizations are more flexible with respect to the deployment and redeployment of resources,” management experts Rosabeth Moss Kanter and David V. Summers wrote in 1987. “But the centrality of mission for nonprofit organizations places limitations on their flexibility of action.”<sup>77</sup> Nonprofits are not to be trusted, Professor Regina Herzlinger similarly explained to readers of the *Harvard Business Review* in 1996, because they lack the three basic accountability measures that ensure effective and efficient business operations: the self-interest of owners, competition, and the ultimate bottom-line measure of profitability.<sup>78</sup>

Contrary to these conventional beliefs, however, the past ten to fifteen years have constituted a period of extraordinary resilience and adaptability on the part of America's nonprofit sector. Although largely unheralded, nonprofit America has undergone a quiet revolution during this period, a massive process of reinvention and reengineering that is still very much under way. To be sure, the resulting changes are hardly universal: change has been more pronounced in some fields than in others, and even within fields substantial variation exists among agencies of different sizes and orientations. What is more, there are serious questions about whether the resulting changes are in a wholly desirable direction or whether they have exposed the sector to unacceptable risks. Although important shadings are needed to do justice to the considerable diversity that exists, however, there is no denying the dominant picture of extraordinary resilience, adaptation, and change. More specifically, ten threads of change are apparent.

### *Overall Sector Growth*

Perhaps the most vivid evidence of the nonprofit sector's resilience is the striking record of recent sector growth. Between 1977 and 1997, as shown in table 1-5, the revenues of America's nonprofit organizations increased 144 percent after adjusting for inflation, nearly twice the 81 percent growth rate of the nation's economy. Nonprofit revenue growth was particularly robust among arts and culture organizations, social service organizations, and health organizations, in each of which the rate of growth was at least twice that of the U.S. economy. However, even the most laggard components of the nonprofit sector (education and civic organizations) grew at a rate that equaled or exceeded the economy total.<sup>79</sup>

Table 1-5. *Real Growth in Nonprofit Revenue, by Subsector, 1977–97*

<i>Field</i>	<i>Percentage of total, 1977</i>	<i>Percentage change, 1977–97</i>	<i>Share of change, 1977–97</i>
Health	47	167	55
Education	25	82	14
Social services	9	213	14
Civic, social	4	79	2
Arts, culture	2	280	3
Religion	13	135	12
<i>Total</i>	100	144	100
U.S. gross domestic product		81	

Source: Data on nonprofit organizations adapted from Weitzman and others, *The New Nonprofit Almanac and Desk Reference* (San Francisco: Jossey-Bass, 2002), pp. 96–97; data on U.S. gross domestic product from Council of Economic Advisers, *Economic Report of the President, 2002* (Washington: Executive Office of the President, Council of Economic Advisers, 2002).

Evidence of the vibrancy of the nonprofit sector extends well beyond financial indicators, which are heavily influenced by the performance of the largest organizations. Equally revealing is the record of recent organizational formation. Between 1977 and 1997, the number of 501(c)(3) and 501(c)(4) organizations registered with the Internal Revenue Service increased 115 percent, or about 23,000 organizations a year.<sup>80</sup> By comparison, the number of business organizations increased only 76 percent during this same period. Moreover, the rate of nonprofit organization formation accelerated in more recent years, jumping from an average of 15,000 a year between 1977 and 1987 to more than 27,000 a year between 1987 and 1997, and this despite increased pressures for organizational mergers. Evidently, Americans are still finding in the nonprofit sector a convenient outlet for a wide assortment of social, economic, political, and cultural concerns.<sup>81</sup>

*Marketing to Paying Customers*

What accounts for this record of robust growth? One of the central explanations appears to be the success with which American nonprofits took advantage of the favorable demographic and social trends to market their services to a clientele increasingly able to afford them. Reflecting this, even with religious congregations included, fees and charges accounted for nearly half (47 percent) of the growth in nonprofit revenue between 1977 and 1997—more than any other source (see table 1-6).

To be sure, not all components of the nonprofit sector relied equally heavily on fees and charges to finance their operations during this period, as shown in table 1-7. What is striking about the past two decades of nonprofit development, however, is how extensively reliance on fee income has spread throughout the sector. After adjusting for inflation, fee income jumped 272 percent for arts and culture organizations, 220 percent for civic organizations, and over 500

Table 1-6. *Changing Structure of Nonprofit Revenue, 1977–97*

Revenue source	Percentage change, 1977–97	Share of total				Share of revenue growth, 1977–97	
		1977		1997		All	Without religion
		All	Without religion	All	Without religion		
Fees, charges	145	46	51	47	51	47	51
Government	195	27	31	33	37	37	42
Philanthropy	90	27	18	20	12	16	8
<i>Total</i>	144	100	100	100	100	100	100

Source: See table 1-5.

Table 1-7. *Growth of Nonprofit Fee Income, by Subsector, 1977–97*

<i>Field</i>	<i>Percentage change, 1977–97</i>	<i>Share of total revenue</i>		<i>Share of revenue growth, 1977–97</i>
		<i>1977</i>	<i>1997</i>	
Education	77	67	65	63
Social services	587	13	28	35
Civic	220	19	34	53
Arts, culture	272	47	46	46
Religion	163	14	16	17
<i>Total</i>	145	46	47	47
Total without religion	144	51	51	51

Source: See table 1-5.

percent for social service organizations between 1977 and 1997, thus accounting for 46, 53, and 35 percent, respectively, of the growth of these agencies. Even religious organizations boosted their commercial income during this period, largely, as Chaves shows in chapter 8 of this volume, through the sale or rental of church property.

Not only did nonprofits boost their fee revenues from existing clients, they also apparently pursued middle-class clientele into the Sun Belt and the suburbs. This is evident in the growing suburbanization of philanthropy during the 1980s reported by economist Julian Wolpert and in the geographic spread of nonprofit employment reported by the Johns Hopkins Nonprofit Employment Data Project.<sup>82</sup> Seventy percent of the substantial growth in nonprofit employment in the state of Maryland between 1989 and 1999, for example, took place in the Baltimore and Washington suburbs, whereas the city of Baltimore, which started the period with nearly half of the state's nonprofit employment, accounted for only 17 percent of the growth.

Clearly, market forces have penetrated into the nonprofit sector well beyond the fields of health and higher education to which they were formerly mostly confined. And the organizations in this broader array of fields have demonstrated an equal capacity to respond to them.

### *Successful Pursuit of Public Funds*

Not only have nonprofit organizations managed to adapt themselves to the new market opportunities they are facing, but also they have proved adept at coping with the new public funding terrain that has evolved in recent years. As a result, despite the rhetoric of retrenchment that characterized this period, one of the most striking recent developments has been an enormous growth in nonprofit revenue from public sector sources. As noted in table 1-6, government support

Table 1-8. *Growth in Nonprofit Revenue from Government, by Subsector, 1977–97*

<i>Field</i>	<i>Percentage change, 1977–97</i>	<i>Share of total revenue</i>		<i>Share of revenue growth, 1977–97</i>
		<i>1977</i>	<i>1997</i>	
Health	248	32	42	48
Education	94	18	19	21
Social services	200	54	52	51
Civic	8	50	30	5
Arts, culture	214	12	10	9
Religion	0	0	0	0
<i>Total</i>	195	27	33	37
Total without religion	195	31	37	42

Source: See table 1-5.

to the nonprofit sector increased 195 percent in real terms between 1977 and 1997, proportionally more than any other source, and these figures do not include the windfall from welfare reform discussed earlier. Government accounted for 37 percent of the sector's substantial growth during this period, boosting its share of the total from 27 percent in 1977 to 33 percent in 1997. And with religious congregations excluded (since they do not receive much government support), the government contribution to sector growth came to 42 percent, boosting government's share of the sector's revenue from 31 percent in 1977 to 37 percent in 1997.

Not all segments of the sector benefited equally from this expanding government support, of course. The major beneficiaries were nonprofit health, social service, and arts organizations, all of which received increased government support by 200 percent or more after adjusting for inflation (table 1-8). Government revenue growth was less robust for education organizations, although it still exceeded the overall growth of the domestic economy, while for civic organizations it barely kept pace with inflation, perhaps confirming fears that the real thrust of the budget cutting of the 1980s and early 1990s was to "defund the left."

The proximate cause of this extraordinary growth in nonprofit revenue from government was, of course, the expansion in government spending that occurred in fields where nonprofits are active. At least as important, however, has been the skill with which nonprofit organizations have adapted to the shifts they faced in the *forms* of public support. As Smith shows in chapter 4, social service agencies had to be particularly nimble in adjusting to the new realities as states shifted their social service spending from stagnant or declining discretionary grant programs to the rapidly growing Medicaid and SSI programs, both of which deliver their benefits to clients and therefore require agencies to master new marketing, billing, and reimbursement management

skills. That they did so is evident in the sizable 200 percent increase in public funding they achieved.

Similarly impressive was the success of nonprofit housing and community development organizations in taking advantage of the new low-income housing tax credit designed to stimulate the flow of private investment capital into low-income housing. As recounted by Avis Vidal in chapter 6 of this volume, this success was largely due to the role that a skilled set of nonprofit intermediary organizations played in packaging the resulting tax credits and marketing them to for-profit financial institutions, generating in the process a substantial flow of private capital into the hands of community-based organizations in this field. In view of the capital deficiencies facing nonprofit organizations in many fields, this record holds important lessons for the sector in general.

This significant expansion of government support has had its downsides, of course. Particularly problematic has been the tendency for Medicaid (and to some extent Medicare) reimbursement rates to fall behind the actual costs of delivering the services they are intended to support.<sup>83</sup> For-profit vendors can respond to these cuts by pulling out of the affected lines of business, but nonprofits often find this difficult. As a consequence, nonprofit organizations often end up using scarce private charitable resources to subsidize federally funded services.

Even so, the success with which nonprofit organizations have adapted to the new government funding realities is another demonstration of the sector's recent resilience and adaptability. More than that, it provides another indication of the sector's growing "marketization," since so much of the government aid now takes the form of "consumer-side" subsidies. When this voucher-type government support is added to the fee income that nonprofits receive, as it is in the data on "program service revenue" that nonprofit organizations report to the Internal Revenue Service, it turns out that two-thirds (67 percent) of the reported income of nonprofit 501(c)(3) organizations as of 1998 came from such "commercial" sources. And with investment income included as well, the commercial total is over 75 percent. Even among human service nonprofits, the combination of consumer-side government subsidies and fee income accounted for over half (54 percent) of total revenue in 1998.<sup>84</sup>

### *The Revolution in Charitable Fundraising*

Accompanying the growing sophistication that nonprofit organizations have demonstrated in pursuing fee income and tapping government support has been the increased creativity they have displayed in raising charitable contributions. As the chapters by Hodgkinson, Lenkowsky, and Young and Salamon show in more detail, the past twenty years have witnessed a growing professionalization of charitable fundraising and, with it, a proliferation of mechanisms for generating charitable resources. One reflection of this is the emergence and growth of

specialized organizations catering to the new fundraising profession—the National Society of Fund-Raising Executives, now the Association of Fund-Raising Professionals (AFP), the Council for the Advancement and Support of Education, the Association for Healthcare Philanthropy, and the National Committee for Planned Giving. As recently as 1979, AFP, the largest of these organizations, boasted only 1,899 members. By 1999 it claimed more than 20,000, and the National Committee for Planned Giving, a more specialized body, itself had 11,000.

This growth of a fundraising profession has had the fortuitous result, as Hodgkinson shows in chapter 12, of helping to democratize charitable giving, moving it from an almost exclusive focus on the wealthy to a much broader base. The vehicle for this has not been individual solicitors standing on street corners in the old Salvation Army model. Rather, the technology of charitable giving has been transformed through the development of devices such as workplace solicitation, telethons, direct mail campaigns, telephone solicitation, and, most recently, e-philanthropy. Entire organizations have surfaced to manage this process of extracting funds. Included here are entities such as United Way, various health appeals (for example, the American Cancer Society, the American Heart Association), and the nation's growing network of community foundations. As noted, for-profit businesses also have gotten into the act.<sup>85</sup> The new actors have been financial service companies that have capitalized on their mastery of finance to popularize a variety of relatively new “planned giving” mechanisms. These instruments allow donors to earn tax-sheltered income on funds deposited in special “split income” or “charitable remainder” trusts during their lifetime or the lifetime of designated beneficiaries and then to contribute the remaining assets to charities at their death without having to pay estate taxes. The for-profit investment firms have also actively promoted a variety of “donor-advised funds,” which give donors the opportunity to retain control over assets deposited for charitable purposes, while securing tax advantages at the full appreciated value of the contributed assets at the time of contribution. By 2000, the largest of these operations, the Fidelity Charitable Gift Fund managed by the Boston-based for-profit investment firm Fidelity Investments, reported assets of \$2.4 billion. Partly in response to this competition, nonprofit community foundations and federated funding organizations have also intensified their use of these instruments, boosting the reported assets in donor-advised funds to an estimated \$10.4 billion as of 2000.<sup>86</sup> Along with new “donor option” arrangements in traditional federated charitable appeals like United Way and the new “venture philanthropy,” this explosion of donor-advised funds suggests the emergence of what Lenkowsky in chapter 11 of this volume sees as an alternative entrepreneurial model of institutional philanthropy modeled on the decentralized, entrepreneurial firms that have been the source of much of the new-economy wealth now being channeled into charitable activity. As such, it

differs from the more bureaucratic forms found in the larger staffed foundations, which grew out of the hierarchic enterprises of an earlier era.

This revolution in the technology of charitable fundraising doubtless boosted charitable giving above what it might otherwise have been. It did not, however, counter the effects of other developments, including tax and other policies, working to dampen the growth in giving. For one thing, the new forms of charitable fundraising are often more costly, requiring heavier administrative expenditures to raise a given quantity of charitable resources. For another, some of the new vehicles delay the transfer of wealth into charitable uses. Donor-advised funds and charitable remainder trusts are essentially holding vats for charitable dollars, and some in the charitable community bewail the resulting reduction in direct contributions to operating charities and in direct contact between donors and recipient organizations that these devices also produce.<sup>87</sup> Whatever the reason, despite the innovations in fundraising techniques, the growth of private charitable giving, while substantial, has not kept pace with the growth of nonprofit revenue more generally. Thus, as shown in table 1-6, charitable giving increased 90 percent between 1977 and 1997, well below the growth rate for the other major sources of nonprofit revenue. Philanthropy accounted for only 16 percent of the growth of the sector as a consequence, and much of this was due to the growth of contributions to religious congregations. With that portion of private giving excluded, philanthropy accounted for only 8 percent of the sector's growth, and its share of sector income declined from 18 to 12 percent.<sup>88</sup>

As with the other sources of income, the growth in giving varied by subsector, as shown in table 1-9. Especially notable was the above-average growth of private giving in the fields of religion, civic activity, and arts and culture, where private giving accounted for over 40 percent of total revenue growth during this twenty-year period. By contrast, philanthropic support to the nation's social service agencies grew much more slowly. As a result, the philanthropic share of social service organization income fell from 33 percent in 1977 to 20 percent twenty years later. Philanthropy, it appears, became even more amenities-oriented over this twenty-year period, a trend that is potentially troubling, as Diaz argues in chapter 17 of this volume. Although the events of September 11 may ultimately reverse this trend, the evidence as of this writing is hardly encouraging.

### *Expanded Venture Activity*

A fifth manifestation of the nonprofit sector's recent resilience has been its increased involvement in commercial ventures. Such ventures differ from the collection of fees for standard nonprofit services in that they entail the creation and sale of products and services primarily for a commercial market. Examples here include museum gift shops and on-line stores, church rentals of social halls, and licensing agreements between research universities and commercial firms. Existing law has long allowed nonprofit organizations to engage in such com-

Table 1-9. *Growth in Nonprofit Revenue from Philanthropy, by Subsector, 1977-97*

<i>Field</i>	<i>Percentage change, 1977-97</i>	<i>Share of total revenue</i>		<i>Share of revenue growth, 1977-97</i>
		<i>1977</i>	<i>1997</i>	
Health	3	14	6	0
Education	91	15	16	17
Social services	91	33	20	14
Civic	106	31	36	42
Arts, culture	307	41	44	45
Religion	131	86	84	83
<i>Total</i>	90	27	20	16
Total without religion	62	18	12	8

Source: See table 1-5.

mercial activities so long as they do not become the primary purpose of the organization. Since 1951 the income from such ventures has been subject to corporate income taxation unless it is “related” to the charitable purpose of the organization.

Solid data on the scope of this activity are difficult to locate since much of it is considered “related” income and buried in the statistics on fees, but the clear impression from what data exist suggests a substantial expansion over the past two decades. One sign of this is the growth in so-called “unrelated business income” reported to the Internal Revenue Service. Although the Internal Revenue Service has been notoriously liberal in its definition of what constitutes unrelated, as opposed to related, business income, the number of charities reporting such income increased 35 percent between 1990 and 1997, and the amount of income they reported more than doubled.<sup>89</sup> As of 1997, gross unrelated business income reported by nonprofit organizations reached \$7.8 billion, an increase of 7 percent over the previous year, following increases of 30 percent a year over the previous two years.

Cultural institutions seem to have been especially inventive in adapting venture activities to their operations, perhaps because they have the clearest “products” to sell. The Guggenheim Museum has even gone global, with franchises in Italy, Germany, and Spain, while elaborate touring exhibitions and shows have become standard facets of museum, orchestra, and dance company operations. Cultural institutions are also actively exploiting the new digitization technologies, often in collaboration with commercial firms. In the process, as Wyszomirski notes, arts organizations are being transformed from inward-oriented institutions focused primarily on their collections to outward-oriented enterprises competing for customers in an increasingly commercial market.

Other types of nonprofit organizations are also increasingly involved in commercial-type ventures. Thus hospitals are investing in parking garages, universities are establishing joint ventures with private biotechnology companies, and social service agencies are operating restaurants and catering businesses. The business activities of nonprofit hospitals have grown especially complex, with elaborate purchasing and marketing consortia linking hospitals, medical practitioners, insurance groups, and equipment suppliers.<sup>90</sup>

Perhaps the most interesting facet of this development is the recent tendency of some nonprofit organizations to utilize business ventures not simply to generate income but also to carry out their basic charitable missions. This reflects a broader transformation in prevailing conceptions of the causes of poverty and distress from one focused on providing individuals with needed services to one focused on getting them to work. Thus, as Dennis Young and Lester Salamon discuss in chapter 13 of this volume, rather than merely training disadvantaged individuals and sending them out into the private labor market, a new class of “social-purpose enterprises,” or “social ventures,” has emerged to employ former drug addicts, inmates, or other disadvantaged persons in actual businesses as a way to build skills, develop self-confidence, and teach work habits. Examples here include the Greyston Bakery in Yonkers, New York, which trains and hires unemployable workers in its gourmet bakery business; Pioneer Human Services, a nonprofit in Seattle, Washington, that operates an aircraft parts manufacturing facility, food buying and warehousing services, and restaurants;<sup>91</sup> and Bikeable Communities in Long Beach, California, which promotes bicycle use by offering valet and related services to cyclists. The result is a thoroughgoing marriage of market means to charitable purpose and the emergence of a new hybrid form of nonprofit business.

### *Adoption of the Enterprise Culture*

These developments point, in turn, to a broader and deeper penetration of the market culture into the fabric of nonprofit operations. Nonprofit organizations are increasingly “marketing” their “products,” viewing their clients as “customers,” segmenting their markets, differentiating their output, identifying their “market niche,” formulating “business plans,” and generally incorporating the language, and the style, of business management into the operation of their agencies. Management expert Kevin Kearns argues that nonprofit executives are now “among the most entrepreneurial managers to be found anywhere, including the private for-profit sector.”<sup>92</sup>

How fully the culture of the market has been integrated into the operations, as opposed to the rhetoric, of the nonprofit sector is difficult to determine. Certainly the appetite for materials has been robust enough to convince commercial publishers like John Wiley and Sons to invest heavily in the field, producing a booming market in “how-to” books offering nonprofit managers training in

“strategic planning,” “financial planning,” “mission-based management,” “social entrepreneurship,” “street-smart financial basics,” “strategic communications,” “high-performance philanthropy,” and “high-performance organization,” to cite just a handful of recent titles.<sup>93</sup> The Drucker Foundation’s *Self-Assessment Tool*, with its market-oriented stress on the five questions considered most critical to nonprofit-organization performance (What is our mission? Who is our customer? What does the customer value? What are our results? What is our plan?), was reportedly purchased by more than 10,000 agencies in the first five years following its publication in 1993, suggesting the appetite for business-style management advice within the sector.<sup>94</sup>

More concretely, there is growing evidence that the market culture is affecting organizational practices, organizational structures, and inter-organizational behavior. Hospitals, for example, are increasingly advertising their capabilities, universities are investing in off-campus programs, museums and symphonies are establishing venues in shopping centers, and even small community development organizations are engaging in complex real estate syndications. Significant changes are also occurring in the basic structure and governance of nonprofit organizations. Boards are being made smaller and more selective, substituting a corporate model for a more community-based one. Similarly, greater efforts are being made to recruit business leaders onto boards, further solidifying the dominant corporate culture. In addition, the internal structure of organizations is growing more complex. To some extent this is driven by prevailing legal restrictions. Thus, as Boris and Krehely note in chapter 9, many nonprofit advocacy organizations have created 501(c)(4) subsidiaries to bypass existing restrictions on their lobbying activity as 501(c)(3) charities. Similarly, nonprofit residential care facilities are segmenting their various programs into separate corporate entities to build legal walls around core operations in case of liability challenges. And universities, freed by the Bayh-Dole act and subsequent legislation to patent discoveries developed with federal research funds, are turning to complex consortium arrangements to help market the products of university-based scientific research.<sup>95</sup> Behind the comforting facade of relatively homey charities, nonprofit organizations are being transformed into complex holding companies, with multiple nonprofit and for-profit subsidiaries and offshoots, significantly complicating the task of operational and financial management and control.

### *New Business Partnerships*

As the culture of the market has spread into the fabric of nonprofit operations, old suspicions between the nonprofit and business sectors have significantly softened, opening the way for nonprofit acceptance of the business community not simply as a source of charitable support but also as a legitimate partner for a wide range of nonprofit endeavors. This perspective has been championed by charismatic sector leaders, such as Billy Shore, who urge nonprofits to stop

thinking about how to get donations and start thinking about how to market the considerable assets they control, including particularly the asset represented by their reputations.<sup>96</sup> This has meshed nicely with the growing readiness of businesses to forge strategic alliances with nonprofits in order to generate “reputational capital.” The upshot has been a notable upsurge in strategic partnerships between nonprofit organizations and businesses.

One early manifestation of this approach was the American Express invention of “cause-related marketing” in the early 1980s. Under this technique, a nonprofit lends its name to a commercial product in return for a share of the proceeds from the sale of that product. Research has demonstrated that such arrangements bring substantial returns to the companies involved, boosting sales, enhancing company reputations, and buoying employee morale. Coca Cola, for example, experienced a 490 percent spurt in the sales of its products at 450 Wal-Mart stores in 1997 when it launched a campaign promising to donate 15 cents to Mothers Against Drunk Driving for every soft drink case it sold. More generally, a 1999 Cone/Roper survey finds that two-thirds of Americans have greater trust in companies aligned with a social issue and that more than half of all workers wish their employers would do more to support social causes. This evidence has convinced a growing number of corporations to associate themselves and their products with social causes and the groups actively working on them. Apparel retailer Eddie Bauer thus has entered cause-related marketing arrangements with American Forests, Evian with Bill Shore’s Share our Strength, Liz Claiborne with the Family Violence Prevention Fund, Mattel with Girls Incorporated, Timberland with City Year, and many more. By 1998, such arrangements were generating \$1.5 billion in marketing fees for the nonprofit organizations involved.<sup>97</sup>

Increasingly, moreover, cause-related marketing relationships have evolved into broader partnerships that mobilize corporate personnel, finances, and know-how in support of nonprofit activities. The most successful of these efforts deliver benefits to both the corporation and the nonprofit. Thus, for example, when the Swiss pharmaceutical manufacturer Novartis contributed \$25 million to the University of California at Berkeley for basic biological research, it secured in the bargain the right to negotiate licenses on a third of the discoveries of the school’s Department of Plant and Microbial Biology, whether it paid for these discoveries or not.<sup>98</sup> Management expert Rosabeth Moss Kanter even argues that businesses are coming to see nonprofits not simply as sources of good corporate images, but as the “beta site for business innovation,” a locus for developing new approaches to long-standing business problems, such as how to recruit inner-city customers to the banking system or how to locate and train entry-level personnel for central-city hotels.<sup>99</sup> In these and countless other ways, nonprofit organizations and businesses have begun reaching out to each other across historic divides of suspicion to forge interesting collaborations of value to

both, leading the Aspen Institute's Nonprofit Sector Strategy Group to "applaud the new strategic approach that businesses are bringing to societal problem-solving and the expansion of business partnerships with nonprofit groups to which it has given rise."<sup>100</sup>

### *Building a Nonprofit Infrastructure*

In addition to absorbing significant aspects of the dominant market culture, however, nonprofit America has been busy developing its own institutional infrastructure, building on the solid base established by the Charity Aid Societies of the late nineteenth century and the subsector organizations representing particular industries (for example, hospitals, higher education, museums) created in the early part of the twentieth century. But as Alan Abramson and Rachel McCarthy point out in chapter 10, the past twenty to twenty-five years have witnessed a considerable filling out of this structure and a fundamental change in its character with the emergence of a new class of infrastructure organizations devoted not to a particular nonprofit industry, but to the nonprofit sector as a whole. This has reflected the enormous growth of the sector, the growing pressures for professionalization of the sector's operations, and the sector's increased involvement with government, which has necessitated more effective representation. Indeed, according to historian Peter Hall, the nonprofit sector was literally "invented" as a concept during this period.<sup>101</sup>

The result has been a substantial enlargement of the organizational apparatus providing services, support, and representation for the nonprofit sector as a whole. Independent Sector, the largest and most visible of the sectorwide infrastructure groups, created in 1980, now numbers more than 700 foundations, corporations, and nonprofit umbrella organizations among its members. Other organizations have been formed to represent organized philanthropy (for example, the Council on Foundations, the Association of Small Foundations, the National Network of Grantmakers, the Forum of Regional Associations of Grantmakers), nonprofit organizations in particular states (for example, the Maryland Association of Nonprofit Organizations), and organizations serving low-income and disfranchised populations (for example, the National Committee for Responsive Philanthropy). In addition, the research and educational apparatus of the sector has filled out remarkably, with nonprofit research centers established at Yale University, Johns Hopkins University, Indiana University, Harvard University, the Urban Institute, and elsewhere; nonprofit degree or certificate programs created in close to 100 colleges and universities; and more than 700 unaffiliated management support organizations offering nondegree instruction and technical assistance to nonprofit managers. To serve this expanding network of experts, new professional associations have come into existence or been enlarged (for example, the Association for Research on Nonprofit Organizations and Voluntary Action), professional journals have been launched or

revamped (for example, *Nonprofit and Voluntary Sector Quarterly*, *Nonprofit Management and Leadership*); special nonprofit sections have been added to existing journals (for example, the *Harvard Business Review*); and a nonprofit press has been created (*The Chronicle of Philanthropy*, *Nonprofit Times*, *The Nonprofit Quarterly*). What was once a scatteration of largely overlooked institutions has thus become a booming cottage industry dedicated to the proposition that nonprofit organizations are distinctive institutions with enough commonalities, despite their many differences, to be studied, represented, networked, serviced, and trained as a group.

### *Meeting the For-Profit Competition*

Nonprofits have also begun to hold their own in the face of the rising tide of for-profit competition. To be sure, the credit for this does not belong to nonprofits alone. Rather, the for-profit sector has proved to be far less formidable a competitor in many of the spheres where both operate than initially seemed to be the case. As Gray and Schlesinger point out in chapter 2 of this volume, a “life cycle” perspective is needed to understand the competitive relationship between nonprofit and for-profit organizations in the health field, and a similar observation very likely applies to other fields as well. For-profit firms have distinct advantages during growth spurts in the life cycles of particular fields, when new services are in demand as a result of changes either in government policy or in consumer needs. This is so because these firms can more readily access the capital markets to build new facilities, acquire new technology, and attract sophisticated management. In addition, they are better equipped to market their services and achieve the scale required to negotiate favorable terms with suppliers (for example, pharmaceutical companies). However, once they become heavily leveraged, the continued success of these enterprises comes to depend heavily on the expectation of continuing escalation of their stock prices. When this expectation is shaken, as it often has been thanks to shifts in government reimbursement policies for Medicare and Medicaid, the results can be catastrophic and precipitous. In such circumstances, for-profit firms have shown a distressing tendency to engage in fraudulent practices. In the 1990s, for example, for-profit nursing homes, squeezed by new state policies designed to reduce Medicaid costs, turned to misleading billing practices to sustain their revenues and ultimately got caught. A similar scenario played out in the hospital field twice in the past two decades—first in the late 1980s and again in the mid-1990s. In both cases, overly optimistic for-profit entrepreneurs found it impossible to sustain the growth paths that their stock valuations required and ended up being discredited when government agencies and private insurers found that they had fraudulently inflated their costs and overbilled for services.<sup>102</sup> This boom and bust cycle seems to operate as well in the social service field, particularly where government support is a crucial part of the demand structure of agencies. For-

profit involvement grows in response to increased public funding, but then suffers a shakeout when government reimbursement contracts.

All of this demonstrates why nonprofit involvement is so crucial, especially in fields where the public has a vital stake in maintaining a reasonable level of quality care. At the same time, such involvement is far from guaranteed, even where nonprofits pioneer the service. Given the intensity of competition at the present time and the expanded access of for-profits to government support, nonprofits can hold their own only where they have well-established institutions, where they can secure capital, where they manage to identify a meaningful market niche and a distinctive product, where they respond effectively to the competitive threat, and where individual consumers or those who are paying on their behalf value the special qualities that nonprofits bring to the field. The fact that nonprofits have continued to expand substantially in the face of competition suggests that many nonprofits have been up to this challenge, although recent reports indicating problems for nonprofit hospitals in generating capital to respond to a surprising spurt in admissions make it clear that serious challenges remain.<sup>103</sup>

### *Meeting the Political Competition*

In addition to fending off for-profit competition in the economic sphere, nonprofit organizations have also demonstrated unusual, and growing, effectiveness in the political sphere. This achievement is especially surprising in view of the role that money has come to play in American politics, the serious economic pressures under which organizations are operating, and the apparent decline in civic participation identified by scholars such as Robert Putnam.<sup>104</sup> It is all the more remarkable in light of the legal limitations on nonprofit political action—limitations that bar nonprofit organizations from engaging in electoral activity, from contributing to political campaigns, and from devoting more than a limited share of their resources to “lobbying.”<sup>105</sup> Indeed, as Boris and Krehely report in chapter 9, only 1.5 percent of all nonprofit 501(c)(3) organizations that filed the required Form 990 with the Internal Revenue Service in 1998 reported any expenditures on lobbying, and the amount they spent represented less than one-tenth of 1 percent of their expenditures.

Despite these limitations, however, nonprofits have amassed an extraordinary recent record of advocacy achievements. One manifestation of this has been the sizable number of social and political “movements” that have taken form within the nation’s nonprofit institutions. More generally, the past twenty to thirty years have witnessed the growing capacity of a variety of citizen groups to influence the policy process, as reflected in Jeffrey Berry’s careful analysis of the role of such groups in shaping the congressional agenda between the early 1960s and the early 1990s.<sup>106</sup> With only 7 percent of the Washington interest group universe throughout this period, these groups accounted for anywhere from 24 to

32 percent of the congressional testimony, generated between 29 and 40 percent of the press coverage of pending legislation, and were nearly 80 percent as effective in passing legislation they favored as the business lobbies against which they were often arrayed. As Berry points out,

In every measurement taken so far, liberal citizen groups have demonstrated that they are effective and tenacious Washington lobbies. . . . Even if business remains more powerful, liberal citizen groups have proved that they are worthy adversaries capable of influencing policymakers.<sup>107</sup>

Not only have nonprofit citizen groups proved effective in national political advocacy, but also these organizations have recently extended their reach upward to the international level and downward to states and localities. The same new communications technologies that have facilitated the rise of global corporations have permitted the emergence of transnational advocacy networks linking nonprofit citizen groups across national borders. This “third force” is rapidly transforming international politics and economics, challenging government policies on everything from land mines to dam construction and holding corporations to account in their home markets for environmental damage or labor practices they may be pursuing in far-off lands.<sup>108</sup> Indeed, the recent eagerness that multinational corporations have shown for cause-related marketing arrangements and broader strategic partnerships with nonprofit organizations has been driven in important part by the threat these networks pose to their “license to operate” and to their reputations among both consumers and their own staff. Similarly, nonprofits have forged advocacy coalitions at the state level to make sure that devolution does not emasculate policy gains achieved nationally. The expansion of state social welfare and arts spending cited earlier can probably be attributed in important part to this nonprofit policy advocacy at the state level.

That nonprofit citizen groups have been able to develop such clout is due in part to changes in public attitudes and in political circumstances—the declining influence of political parties, the growing public concern for amenities such as a healthy environment, and the end of the cold war. But at least as important has been the capacity and effectiveness of the citizen organizations themselves—their ability to attract resources and talented personnel, the dedication and seriousness with which they have approached their work, and the effectiveness they have shown in utilizing the resources at their command. As Boris and Krehely show in chapter 9, nonprofit advocacy organizations have blossomed into highly complex organizations commanding millions of dollars of resources. The Sierra Club, for example, has sixty-five chapters throughout the United States, with 550,000 members, a separate Sierra Club Foundation, and a Sierra Club Political Action Committee. The Nature Conservancy is now a holding company for

five nonexempt and four exempt organizations, including a Nature Conservancy Action Fund, and oversees 300 state and local organizations. Not only are many of these organizations large and complex, however, they also seem to be increasingly well managed. As Berry shows, these groups have built substantial donor bases, earned a reputation for doing their homework, and enjoy at least as much credibility as their business opponents.<sup>109</sup>

## Summary and Implications

Nonprofit America has thus responded with extraordinary creativity and resilience to the challenges and opportunities it has confronted over the past twenty years. The sector has grown enormously as a consequence—in numbers, in revenues, and in the range of purposes it serves. In addition, it seems to have expanded its competencies and improved its management, although these are more difficult to gauge with precision. To be sure, not all components of the sector have experienced these changes to the same degree or even in the same direction. Yet what is striking is how widespread the adaptations seem to have been.

In large part, what allowed nonprofit organizations not only to survive, but to thrive, during this period was that they moved, often decisively, toward the market. Nonprofit organizations took active advantage of the growing demand for their services, expanded their fee income, launched commercial ventures, forged partnerships with businesses, adopted business-style management techniques, mastered new consumer-side forms of government funding, reshaped their organizational structures, incorporated sophisticated marketing and money-management techniques into even their charitable fundraising, and generally found new ways to tap the dynamism and resources of the market to promote their organizational objectives. This move toward the market has by no means been universal. Nor is it entirely new. What is more, it did not exhaust the range of responses the sector made to the challenges it faced. Yet it has clearly been the dominant theme of the decade, and its scope and impact have been profound, affecting all parts of the sector to some extent. As a result, the nonprofit sector that is entering the twenty-first century is not “your father’s nonprofit sector.” Rather, it has been substantially reengineered, and this process is still very much under way, although it has yet to be fully appreciated by the sector itself or by the nation at large.

On balance, these changes seem to have worked to the advantage of the nonprofit sector, strengthening its fiscal base, upgrading its operations, enlisting new partners and new resources in its activities, and generally improving its reputation for effectiveness. But they have also brought significant risks, and the risks may well overwhelm the gains. Before drawing the final balance sheet on the state of nonprofit America, therefore, it is necessary to weigh the gains against these risks.

*The Risks*

More specifically, the nonprofit sector's response to the challenges of the past twenty years, creative as it has been, has exposed the sector to at least five important risks.

**GROWING IDENTITY CRISIS.** In the first place, the nonprofit sector is increasingly confronting an identity crisis as a result of a growing tension between the market character of the services it is providing and the continued nonprofit character of the institutions providing them. As Gray and Schlesinger show in chapter 2, this tension has become especially stark in the health field, where third-party payers, such as Medicare and private health maintenance organizations, refuse to consider values other than actual service cost in setting reimbursement rates, and where bond rating agencies discount community service in determining what nonprofit hospitals have to pay for the capital they need to expand. Left to their own devices, nonprofit institutions have had little choice but to adjust to these pressures, but at some cost to the features that make them distinctive. Under these circumstances, it is no wonder that scholars have been finding it so difficult to detect real differences between the performance of for-profit and nonprofit hospitals and why many nonprofit health maintenance organizations and hospitals have willingly surrendered the nonprofit form or sold out to for-profit firms.<sup>110</sup> Private universities are similarly experiencing increasing strains between their mission to propagate knowledge and the expansion of their reliance on corporate sponsorship, which has brought with it demands for exclusive patent rights to the fruits of university research.<sup>111</sup> Marketing pressures are also intruding on the operations of nonprofit arts and cultural institutions, limiting their ability to focus on artistic quality and transforming them, as Wyszomirski notes in chapter 5, into social enterprises more attentive to market demands. So intense has the resulting identity crisis become, in fact, that at least some scholars are beginning to reject the long-standing notion that nonprofits are reluctant participants in the market, providing only those "private goods" needed to support their "collective goods" activities, and are coming to see many of them functioning instead as essentially commercial operations dominated by "pecuniary rather than altruistic objectives."<sup>112</sup>

**INCREASED DEMANDS ON NONPROFIT MANAGERS.** These tensions have naturally complicated the job of the nonprofit executive, requiring these officials to master not only the substantive dimensions of their fields but also the broader private markets within which they operate, the numerous public policies that increasingly affect them, and the massive new developments in technology and management with which they must contend. They must do all this, moreover, while balancing an increasingly complex array of stakeholders that

includes not only clients, staff, board members, and private donors but also regulators, government program officials, for-profit competitors, and business partners and while also demonstrating performance and competing with other nonprofits and with for-profit firms for fees, board members, customers, contracts, grants, donations, gifts, bequests, visibility, prestige, political influence, and volunteers.<sup>113</sup> No wonder that burnout has become such a serious problem in the field, despite the excitement and fulfillment the role entails.

**INCREASED THREAT TO NONPROFIT MISSIONS.** Inevitably, these pressures pose threats to the continued pursuit of nonprofit missions. Nonprofit organizations forced to rely on fees and charges naturally begin to skew their service offerings to clientele who are able to pay. What start out as sliding fee scales designed to cross-subsidize services for the needy become core sources of revenue essential for agency survival. Organizations needing to raise capital to expand are naturally tempted to locate new facilities in places with a client base able to finance the borrowing costs. When charity care, advocacy, and research are not covered in government or private reimbursement rates, institutions have little choice but to curtail these activities.

How far these pressures have proceeded is difficult to say with any precision. As Diaz shows in chapter 17, support for the poor has never been the exclusive, or the primary, focus of nonprofit action. Nor need it be. What is more, many of the developments identified above have usefully mobilized market resources to support genuinely charitable purposes. Yet the nonprofit sector's movement toward the market is creating significant pressures to move away from those in greatest need, to focus on amenities that appeal to those who can pay, and to apply the market test to all facets of their operations.<sup>114</sup> The move to the market may thus be posing a far greater threat to the nonprofit sector's historic social justice and civic mission than the growth of government support before it.

**DISADVANTAGING SMALL AGENCIES.** A fourth risk resulting from the nonprofit sector's recent move to the market is to put smaller agencies at an increasing disadvantage. Successful adaptation to the prevailing market pressures increasingly requires access to advanced technology, professional marketing, corporate partners, sophisticated fundraising, and complex government reimbursement systems, all of which are problematic for smaller agencies. Market pressures are therefore creating not just a digital divide, but a much broader "sustainability chasm" that smaller organizations are finding it increasingly difficult to bridge. Although such agencies can cope with these pressures in part through collaborations and partnerships, these devices themselves often require sophisticated management and absorb precious managerial energies.<sup>115</sup> As the barriers to entry, and particularly to sustainability, rise, the nonprofit sector is

thus at risk of losing one of its most precious qualities—its ease of entry and its availability as a testing ground for new ideas.

**POTENTIAL LOSS OF PUBLIC TRUST.** All of this, finally, poses a further threat to the public trust on which the nonprofit sector ultimately depends. Thanks to the pressures they are under and the agility they have shown in responding to them, American nonprofit organizations have moved well beyond the quaint Norman Rockwell stereotype of selfless volunteers ministering to the needy and supported largely by charitable gifts. Yet popular and press images remain wedded to this older image, and far too little attention has been given to bringing popular perceptions into better alignment with the realities that now exist and to justifying these realities to a skeptical citizenry and press. As a consequence, nonprofits find themselves vulnerable when highly visible events, such as the September 11 tragedy, let alone instances of mismanagement or scandal, reveal them to be far more complex and commercially engaged institutions than the public suspects. The more successfully nonprofit organizations respond to the dominant market pressures they are facing, therefore, the greater the risk they face of sacrificing the public trust on which they ultimately depend. This may help to explain the widespread appeal of the Bush administration's faith-based charities initiative. What makes this concept so appealing is its comforting affirmation of the older image of the nonprofit sector, the image of voluntary church groups staffed by the faithful solving the nation's problems of poverty and blight, even though, as Chaves shows in chapter 8, this image grossly exaggerates both the capacity and the inclinations of most congregations to engage in meaningful social problem solving.

### *Resetting the Balance: The Task Ahead*

What all of this suggests is that a better balance may need to be struck between what Gray and Schlesinger term the nonprofit sector's "distinctiveness imperative"—the things that make nonprofits special—and the sector's "survival imperative"—the things nonprofits need to do in order to survive. To be sure, these two imperatives are not wholly in conflict. Nevertheless, the tensions between them are real, and there is increasing reason to worry that the survival imperative may be gaining the upper hand. To correct this, steps will be needed in both domains, and the steps will require support from many different quarters.

**THE DISTINCTIVENESS IMPERATIVE.** Actions to address the nonprofit sector's distinctiveness imperative are perhaps the most urgent. Several different types of action may be useful here.

—*Rethinking community benefit and charitable purpose.* In the first place, action is needed in the realm of values and ideas. In a sense, nonprofit organiza-

tions have been so busy coping with the powerful market forces they are facing that they have allowed the market definitions of value to dominate the public discourse and even their own behavior. Largely lacking, as *The Nonprofit Quarterly* recently noted, is “agreement around a powerful affirmation of identity distinguishing [the nonprofit sector] from the other two social sectors.” To the extent that any consensus exists on this point, as reflected in court decisions, legislative proposals, and popular accounts, it focuses on care for the poor as the chief, or exclusive, rationale justifying nonprofit status. But this is far too narrow a ground for the sector to defend successfully given the survival demands it also confronts and the other functions it performs. Nonprofits must therefore develop a broader and more coherent statement of “the nature of [their] game.”<sup>116</sup> This will require a serious rethinking of the central concepts of charitable purpose and community benefit that justify the nonprofit sector’s existence, a task that, Abramson and McCarthy point out in chapter 10, the sector’s infrastructure organizations have not yet adequately addressed.

Illustrative of the direction this might take is the suggestion by Gray and Schlesinger in chapter 2 to extend the concept of community benefit for nonprofit hospitals to embrace not only charity care but also a broader commitment to community health and to the production of collective goods such as trained medical professionals and scientific advance. Similar insights can be found in Forman and Stoddard’s discussion in chapter 7 of the recent efforts of nonprofit humanitarian assistance agencies to forge new principles of humanitarian aid that take account of the complex humanitarian and military crises increasingly common around the world. More generally, nonprofit America must give broader and more concrete meaning to its claims to serve the public good by stressing the sector’s commitments to reliability, to trustworthiness, to quality, to equity, to community, and to individual and community empowerment. These are powerful rationales in a society that values pluralism and freedom but wishes to balance them with a sense of solidarity and responsibility for others. But they must be more forcefully and concretely articulated and then be more fully interpreted and applied in the context of particular agencies and fields.

—*Improving public understanding.* As efforts go forward to clarify the nonprofit sector’s vision and rationale, parallel efforts must be made to communicate this vision to the public and reconcile it with how the sector actually works. This must go beyond the ritualistic celebrations of charitable giving and voluntarism that currently form the heart of the sector’s public relations effort, important though these may be. Rather, the public must be introduced to the broader realities of current nonprofit operations, to the remarkable resilience that the sector has shown in recent years, and to the full range of special qualities that make nonprofit organizations worth protecting. This will require a better public defense of the sector’s long-standing partnership with government, clarification

of the special ways in which nonprofits are enlisting market means to promote nonprofit ends, and the further development and dissemination of codes of conduct to help nonprofits and the public understand the delicate balance nonprofits have to strike between their survival and their distinctiveness.

—*Policy shifts.* Changes may also be needed in public policy to make sure that the sector's commitments to community benefit and charitable purpose are given effective incentives and are reinforced. This may require challenging the narrow conceptions of charitable purpose embodied in some legal opinions. But it may also require some tightening of the legal provisions under which nonprofits operate. At a minimum, this could involve more stringent policing of the existing unrelated business income tax provisions to ensure that nonprofit organizations pay income taxes on business activities that stray too far from their charitable purposes. Beyond this, it could involve shifting from the current system of tax-exempt *organizations* to a system of tax-exempt *activities* under which organizations earn exemptions from taxes only for those activities that support valid public, or community, purposes. Under such a system, nonprofit organizations would have to justify their exemptions in annual tax filings that identify the share of their income that goes to support such purposes. Such a system would provide more regular reinforcement of the community benefits that nonprofits are supposed to provide and help to reassure the public that these benefits are actually being provided.

THE SURVIVAL IMPERATIVE. For this effort to promote the “distinctiveness imperative” of nonprofit organizations to work, however, steps will also be needed to ease the survival imperative under which they labor. Three of these deserve particular mention here.

—*Capitalizing the sector.* In the first place, additional steps are needed to correct the structural impediments the nonprofit sector faces in generating investment capital because of its lack of access to the equity markets. More than any other single cause, these impediments explain the difficulty nonprofit organizations have faced in responding to technological change and maintaining their market niche during periods of rapid expansion of demand. The experience of nonprofit hospitals and higher education institutions demonstrates, however, that nonprofit organizations can often hold their own in such circumstances when they can gain access to the needed capital at competitive rates. In both of these cases, special tax incentives were provided to subsidize bonds issued to finance nonprofit facilities. The recent example of nonprofit involvement in low-income housing described by Vidal in chapter 6 tells a similar story in a context characterized by smaller-scale institutions. Here the provision of special tax advantages for investors was supplemented by the emergence of nonprofit intermediary institutions that package the tax breaks for sale to investors.

Many nonprofit organizations, particularly in the human service field, still lack access to such tax breaks and the capital funds they can leverage, however. As a consequence, they are at a competitive disadvantage in keeping up with rapid technological change and meeting increases in demand. To correct this, a broader nonprofit investment tax credit could usefully be enacted. Such a measure would create a more level playing field for nonprofit agencies, ease the survival pressures they face, and thus allow them to continue performing their distinctive roles.

—*Buy-in by third-party payers.* By itself, improved access to capital for nonprofit organizations will still not give nonprofits the financial leeway they need to address their distinctive missions unless steps are also taken to relieve the fiscal squeeze these organizations face. That squeeze, in turn, is increasingly shaped by the reimbursement policies of third-party payers—private insurance companies, health maintenance organizations, corporate benefit administrators, and government voucher programs like Medicare and Medicaid. Whether nonprofit hospitals can continue to support their teaching and research functions, for example, is significantly affected by whether Medicare considers this function vital enough to justify an adjustment in the normal hospital reimbursement rate. Increasingly, third-party payers have been ratcheting down the kinds of functions they are willing to support in this way, requiring the providers of health care, clinic care, nursing home care, drug abuse treatment, and many other services to shave costs to the bone. To reverse this trend, nonprofit organizations, possibly with help from the public sector, will have to convince third-party payers that these activities are both worthy of support and able to be supported. Blue Shield of California's recent adoption of an incentive system that takes account of quality, and not just cost, in setting hospital reimbursement rates is promising in this regard, but there clearly is still a long way to go.<sup>117</sup>

—*Encouragement of private giving for priority community benefits.* The nonprofit survival imperative can also be eased through continued and expanded encouragement of charitable giving and volunteering, particularly that targeted on community benefit activities. One way to do this would be to replace the existing tax deduction system with one based on tax "credits." Unlike deductions, which deliver more tax benefits per dollar of contribution to upper-income taxpayers than to lower-income ones, tax credits provide the same tax benefits to all taxpayers regardless of their income.<sup>118</sup> What is more, the scale of the credits can be geared to the particular community benefits being promoted simply by varying the share of the contribution that can be used to offset taxes for various types of contributions. American charitable giving has been stuck below 2 percent of personal income for some time. It is worth considering radical approaches that might boost this level in the future, and a system of tax credits instead of deductions might well be one of those worth trying.

## Conclusions

It has been said that the quality of a nation can be seen in the way it treats its least advantaged citizens. But it can also be seen in the way it treats its most valued institutions. Americans have long paid lip service to the importance they attach to their voluntary institutions, while largely ignoring the challenges these institutions face. During the past decade and a half, these challenges have been extraordinary. But so, too, has been the nonprofit sector's response. As a result, the state of nonprofit America is surprisingly robust as we enter the new millennium, with more organizations doing more things more effectively than ever before.

At the same time, the movement to the market that has made this possible has also exposed the sector to enormous risks. What is more, the risks go to the heart of what makes the nonprofit sector distinctive and worthy of public support—its basic identity, its mission, and its ability to retain the public's trust.

Up to now, nonprofit managers have had to fend for themselves in deciding what risks it was acceptable to take in order to permit their organizations to survive. Given the stake that American society has in the preservation of these institutions and in the protection of their ability to perform their distinctive roles, it seems clear that this must now change. Americans need to rethink in a more explicit way whether the balance between survival and distinctiveness that nonprofit institutions have had to strike in recent years is the right one for the future and, if not, what steps might now be needed to shift this balance for the years ahead.

The argument here is that some adjustments are needed, that America's nonprofit institutions require broader support in preserving the features that make them special. Whether others agree with this conclusion remains to be seen. What seems clear, however, is that better public understanding of the state of nonprofit America is needed if such judgments are to be possible. Our hope is that this book will contribute to such understanding. That, at any rate, is our goal.

## Notes

1. Gilbert M. Gaul and Mary Pat Flaherty, "Red Cross Collected Unneeded Blood: Resources Lacking to Freeze Surplus," *Washington Post*, November 11, 2001, p. A1.

2. AAFRC Trust for Philanthropy, "What Do Crises Mean for Philanthropy?" *Giving USA Update*, vol. 4 (2001), p. 3.

3. For a fuller discussion of this partnership, see Lester M. Salamon, "Partners in Public Service," in Walter W. Powell, ed., *The Nonprofit Sector: A Research Handbook* (Yale University Press, 1987), pp. 99–117; and Lester M. Salamon, *Partners in Public Service: Government-Nonprofit Relations in the Modern Welfare State* (Johns Hopkins University Press, 1995).

4. Alexis de Tocqueville, *Democracy in America*, vol. 2, the Henry Reeve text as revised by Francis Bowen (New York: Vintage Books, 1945 [1835]), p. 118.

5. On the reengineering movement in the corporate sector, see Michael Hammer and James Champy, *Reengineering the Corporation: A Manifesto for Business Revolution*, rev. ed. (London: Nicholas Brealey, 1994); Michael Hammer and James Champy, *Reengineering the Corporation: A Manifesto for Business Revolution* (London: Nicholas Brealey, 1993); David K. Carr and Henry J. Johnson, *Best Practices in Reengineering: What Works and What Doesn't in the Reengineering Process* (New York: McGraw-Hill, 1995).

6. See, for example, Kevin P. Kearns, *Private Sector Strategies for Social Sector Success: The Guide to Strategy and Planning for Public and Nonprofit Organizations* (San Francisco: Jossey-Bass, 2000).

7. Section 501(c)(4) organizations share these basic purposes but are permitted to pursue them more extensively through "lobbying" efforts, something 501(c)(3) organizations can do only to a limited extent. However, contributions to the 501(c)(4) organizations are not tax deductible. This distinction between 501(c)(3) and 501(c)(4) organizations is a notoriously slippery one, depending on the definition of the term "lobbying" and the meaning of the restriction on the former organizations not to engage in such activity to a substantial extent. Recent laws have attempted to clarify this distinction by specifying more precisely what falls within the domain of lobbying and what exactly is meant by "substantial." Fundamentally, lobbying means direct or indirect efforts to influence the passage of particular pieces of legislation or particular administrative rules, whereas "substantial" has come to mean roughly 20 percent or more of agency expenditures. In addition to sections 501(c)(3) and 501(c)(4), the U.S. tax code contains over twenty other subsections under which organizations can be granted tax exemptions. These include business associations, labor unions, and social clubs. None of these types of organizations is eligible to receive tax-deductible gifts, however, because they primarily serve their members rather than the public at large. See Bruce R. Hopkins, *The Law of Tax Exempt Organizations*, 6th ed. (New York: John Wiley and Sons, 1992), pp. 327–52.

8. Based on data presented in Lester M. Salamon, *America's Nonprofit Sector: A Primer*, 2d ed. (New York: Foundation Center, 1999), pp. 22 and 41, note 2. Religious congregations are not required to register for tax-exempt status, although many do.

9. Murray S. Weitzman, Nadine Tai Jalandoni, Linda M. Lampkin, and Thomas H. Pollack, *The New Nonprofit Almanac and Desk Reference* (San Francisco: Jossey-Bass, 2002), p. 21.

10. U.S. Census Bureau, *Statistical Abstract of the United States: 2000*, 120 ed. (Washington: U.S. Government Printing Office, 2000), p. 420.

11. Virginia B. Hodgkinson and Murray S. Weitzman, *Nonprofit Almanac: 1996/1997* (San Francisco: Jossey-Bass, 1996), pp. 271–309.

12. Weitzman and others, *New Nonprofit Almanac*, p. 125. See also Internal Revenue Service, *Statistics of Income Bulletin*, Publication 1136 (Washington: Internal Revenue Service, February 1997), table 21.

13. Elizabeth Boris, "The Nonprofit Sector in the 1990s," in Charles T. Clotfelter and Thomas Ehrlich, eds., *Philanthropy and the Nonprofit Sector in a Changing America* (Indiana University Press, 1999), pp. 16–17.

14. The discussion here draws heavily on Salamon, *America's Nonprofit Sector*, pp. 15–17.

15. See, for example, James S. Coleman, *Foundations of Social Theory* (Harvard University Press, 1990), pp. 300–21; Robert Putnam, *Making Democracy Work: Civic Traditions in Modern Italy* (Princeton University Press, 1993), pp. 83–116, 163–85.

16. De Tocqueville, *Democracy in America*, vol. 2, p. 117.

17. This term was first used by Ralph Kramer to describe one of the crucial roles of nonprofit organizations. Kramer used it to refer most squarely to volunteering, but it has a broader meaning as well. Ralph Kramer, *Voluntary Agencies in the Welfare State* (University of California Press, 1981), pp. 193–211.

18. For a more complete analysis of this system of government-nonprofit relations and the broader pattern of “third-party government” of which it is a part, see Salamon, “Partners in Public Service,” pp. 99–117; and Salamon, *Partners in Public Service*. For a discussion of the federal government’s support of nonprofit research universities, see Don K. Price, *The Scientific Estate* (Harvard University Press, 1965). This pattern of government support to nonprofit organizations did not begin in the postwar period, however. Rather, its roots lie deep in American history. For example, Harvard College, the first nonprofit, was financed in important part by an earmarked tax on corn levied by the colonial government of Massachusetts beginning in the seventeenth century. Similarly, subsidies for nonprofit human service were a standard feature of American urban life in the 1880s and 1890s. By the mid-1890s, in fact, more public welfare aid in New York, Pennsylvania, Connecticut, Maryland, and even the District of Columbia went to support private institutions than to public ones, and far more of the income of private nonprofit organizations in a wide variety of fields came from government than from private philanthropy. One early study showed, for example, that in New York City, 69 percent of the income of a group of prominent nonprofit children’s agencies came from public subsidies. On higher education, see John S. Whitehead, *The Separation of College and State: Columbia, Dartmouth, Harvard, and Yale* (Yale University Press, 1973), pp. 3–16. On social services, see Amos Warner, *American Charities: A Study in Philanthropy and Economics* (New York: Thomas Y. Crowell, 1894), pp. 400–05.

19. Lester M. Salamon and Alan J. Abramson, “The Federal Budget and the Nonprofit Sector: Implications of the *Contract with America*,” in Dwight F. Burlingame, William A. Diaz, Warren F. Ilchman, and Associates, eds., *Capacity for Change? The Nonprofit World in the Age of Devolution* (Indianapolis: Indiana University Center on Philanthropy, 1996), pp. 8–9; Alan J. Abramson, Lester M. Salamon, and C. Eugene Steurle, eds., “The Nonprofit Sector and the Federal Budget: Recent History and Future Directions,” in Elizabeth T. Boris and C. Eugene Steurle, eds., *Nonprofits and Government Collaboration and Conflict* (Washington: Urban Institute, 1999), pp. 110–12.

20. Office of Management and Budget, *Enhancing Governmental Productivity through Competition: A New Way of Doing Business within the Government to Provide Quality Government at Least Cost* (Washington: Office of Management and Budget, August 1988), p. 15, quoted in Donald Kettl, *Shared Power: Public Governance and Private Markets* (Washington: Brookings, 1993), p. 46.

21. Vouchers essentially provide targeted assistance to eligible recipients in the form of a certificate or a reimbursement card that can be presented to the provider of choice. The provider then receives payment for the certificate or reimbursement from the government. Tax expenditures use a similar method, except that no actual certificate is used. Rather, eligible taxpayers are allowed to deduct a given proportion of the cost of a particular service (for example, daycare) either from their income (tax deduction) or from the taxes they owe (tax credit). For a discussion of vouchers, tax expenditures, and other tools of public action, see Lester M. Salamon, ed., *The Tools of Government: A Guide to the New Governance* (New York: Oxford University Press, 2002).

22. Salamon, *Partners in Public Service*, p. 208. Both Medicare and Medicaid are essentially voucher programs since consumers are entitled to choose the provider they wish and the government then reimburses the provider for the cost.

23. Spending on Medicaid, for example, swelled more than fourfold in real dollar terms between 1975 and 1998, while discretionary spending stagnated or declined. Computed from data in U.S. House of Representatives, Committee on Ways and Means, *2000 Green Book: Background Material and Data on Programs within the Jurisdiction of the Committee on Ways and Means*, 106 Cong. 2 sess. (Washington, October 6, 2000), pp. 912, 923.

24. U.S. House of Representatives, Committee on Ways and Means, *2000 Green Book*, pp. 599, 617. As of 1998, well over 80 percent of the children receiving daycare assistance under this program were receiving it through such voucher certificates.

25. Of these, 40 percent of the large-establishment employees and 35 percent of the small-establishment employees were covered by preferred provider plans, and the balance of employees were covered by true health maintenance organizations. U.S. Census Bureau, *Statistical Abstract of the United States, 2000* (Washington: U.S. Census Bureau, 2000), table 180, p. 119.

26. Author's estimates based on data in Weitzman and others, *New Nonprofit Almanac*, pp. 96–97.

27. Generally speaking, the higher the rate of tax, the lower the out-of-pocket “cost” of a gift since the taxpayer would have to pay more to Uncle Sam if he or she chose not to give. Paradoxically, therefore, higher tax rates increase the financial incentive to give, and lower tax rates reduce this incentive.

28. Computed from data in Weitzman and others, *Nonprofit Almanac*, pp. 96–97. These figures exclude giving to religious organizations for religious purposes but include the portion of religious giving that goes to support other charitable purposes, such as social welfare and education. With all religious giving included, the decline in giving's total share of sector income was slightly less pronounced—from 26 percent in 1977 to 18.5 percent in 1997. See chapter 16 by Atul Dighe.

29. The Fidelity Gift Fund recorded assets of \$2.2 billion as of early 2000 and made grants of \$374 million in the 1998–99 fiscal year. By comparison, the New York Community Trust reported assets of \$2.0 billion as of the end of 1999 and grants during 1999 of \$130.7 million. AAFRC Trust for Philanthropy, *Giving USA 2001: The Annual Report on Philanthropy for the Year 2001* (Indianapolis Center on Philanthropy, 2001), p. 53; Foundation Center, *Foundation Yearbook of Facts and Figures on Private, Corporate, and Community Foundations, 2001*, Foundation Today Series (New York: Foundation Center, 2001), pp. 67–68.

30. For a discussion of recent problems that nonprofit hospitals have encountered in generating capital, see Reed Abelson, “Demand, but No Capital, at Nonprofit Hospitals,” *New York Times*, June 21, 2002, p. B1.

31. William P. Ryan, “The New Landscape for Nonprofits,” *Harvard Business Review*, vol. 77 (January/February 1999): 128.

32. Henry Hansmann, “The Role of Nonprofit Enterprise,” *Yale Law Journal*, vol. 89, no. 5 (April 1980): 835–901.

33. See, for example, Michael Porter and Mark R. Kramer, “Philanthropy's New Agenda: Creating Value,” *Harvard Business Review*, vol. 77 (November/December 1999): 121–30; Gar Walker and Jean Grossman, “Philanthropy and Outcomes,” in Clotfelter and Ehrlich, eds., *Philanthropy and the Nonprofit Sector in a Changing America*, pp. 449–60.

34. Christine W. Letts, William Ryan, and Allen Grossman, “Virtuous Capital: What Foundations Can Learn from Venture Capitalists,” *Harvard Business Review*, vol. 75 (March/April 1997): 36–44, especially pp. 2–7.

35. H. George Frederickson, “First There's Theory. Then, There's Practice,” *Foundation News and Commentary*, vol. 42, no. 1 (March/April 2001): 38. See also Doug Easterling, “Using Outcome Evaluation to Guide Grant Making: Theory, Reality, and Possibilities,” *Nonprofit and Voluntary Sector Quarterly*, vol. 29, no. 3 (September 2000): 482–86; Walker and Grossman, “Philanthropy and Outcomes.”

36. Jeffrey Berry, *The New Liberalism: The Rising Power of Citizen Groups* (Washington: Brookings, 1999), especially pp. 12–130.

37. Nicole Wallace, "Online Giving Soars as Donors Turn to the Internet Following Attacks," *Chronicle of Philanthropy*, October 4, 2001, p. 22.

38. Andrew Blau, *More than Bit Players: How Information Technology Will Change the Ways Nonprofits and Foundations Work and Thrive in the Information Age*, a report to the Surdna Foundation (New York: Surdna Foundation, May 2001), p. 10.

39. A survey by the Association of Arts Agencies cited by Margaret Wyszomirski in chapter 5, for example, found that 34 percent of arts organizations had only one or no computers and 46 percent had no website. See, more generally, Stephen Greene, "Astride the Digital Divide: Many Charities Struggle to Make Effective Use of New Technology," *Chronicle of Philanthropy*, January 11, 2001.

40. Andrew Blau, *More than Bit Players*, p. 9.

41. Edwin Feulner, "Truth in Testimony," Heritage Foundation Testimony (Washington: Heritage Foundation, August 22, 1996).

42. Capital Research Center, "Our Mission," available at [www.capitalresearch.org](http://www.capitalresearch.org) [November 1996].

43. Roy Lubove, *The Professional Altruist* (Harvard University Press, 1965).

44. John McKnight, *The Careless Society: Community and Its Counterfeits* (New York: Basic Books, 1995), p. 10.

45. Stuart Butler, *Privatizing Federal Spending* (New York: Universe Books, 1985); Martin Anderson, *Imposters in the Temple: American Intellectuals Are Destroying Our Universities and Cheating Our Students* (Englewood Cliffs, N.J.: Simon and Schuster, 1992).

46. Independent Sector, *Giving and Volunteering, 1999* (Washington: Independent Sector, 1999), chap. 3, pp. 3, 5.

47. Similar evidence of public ambivalence emerges from a survey conducted for the Maryland Association of Nonprofit Organizations. Only 38 percent of the respondents in this survey indicated that they think private charitable organizations are "very trustworthy," only 29 percent "strongly agree" that the money they donate to charities is being used as they expect it to be, and 87 percent expressed worry that they are being "scammed" by telephone solicitations. Maryland Association of Nonprofit Organizations, *Protecting the Public Trust: Revisiting Attitudes about Charities in Maryland* (Baltimore: Maryland Association of Nonprofit Organizations, 2002).

48. Phillip Howe and Corinne McDonald, "Traumatic Stress, Turnover, and Peer Support in Child Welfare" (Washington: Child Welfare League of America, 2001), available at [www.cwla.org/programs/trieschman/2001\\_fbwPhilHowe.htm](http://www.cwla.org/programs/trieschman/2001_fbwPhilHowe.htm) [August 14, 2002].

49. Thus among public policy program graduates in the classes of 1973, 1974, 1978, and 1979, an average of 14 percent took their first job in the nonprofit sector and 14 percent remained employed in the nonprofit sector in the mid-1990s. By contrast, an average of 16 percent of these graduates took their first job in the private business sector, and 33 percent were employed in the business sector as of the mid-1990s. Computed from data in Paul Light, *Making Nonprofits Work: A Report on the Tides of Nonprofit Management Reform* (Washington: Brookings, 2000), p. 10.

50. Jeanne Peters and Timothy Wolfred, *Daring to Lead: Nonprofit Executive Directors and Their Work Experience* (San Francisco: CompassPoint Nonprofit Services, August 2001), pp. 13–14, 20–21.

51. The discussion here draws heavily on Salamon, *America's Nonprofit Sector*.

52. U.S. Census Bureau, *Statistical Abstract of the United States, 2000*, pp. 408–09.

53. U.S. Census Bureau, *Statistical Abstract of the United States, 2000*, table 144, p. 101.

54. 1960 and 1980 figures from U.S. Census Bureau, *Statistical Abstract of the United States, 1982/3*, table 97, p. 66; figures for 1990s from U.S. Census Bureau, *Statistical Abstract of the United States, 2000*, table 88, p. 71.

55. U.S. House of Representatives, Committee on Ways and Means, *2000 Green Book*, p. 1363.

56. Neil Gilbert, "The Transformation of Social Services," *Social Services Review*, vol. 51, no. 4 (December 1977): 624–41.

57. Paul Ray and Sherry Ruth Anderson, *Cultural Creatives: How 50 Million People Are Changing the World* (San Francisco: Harmony, 2000).

58. Robert V. Avery and Michael S. Rendell, "Estimating the Size and Distribution of the Baby Boomers' Prospective Inheritances" (Cornell University, Department of Consumer Economics, 1990). For more recent estimates, see John J. Havens and Paul G. Schervish, "Millionaires and the Millennium: New Estimates of the Forthcoming Wealth Transfer and the Prospects for a Golden Age of Philanthropy" (Boston College, Social Welfare Research Institute, October 1999).

59. *Top Heavy* (New York: Twentieth Century Fund, 1995), table A-1. For a summary of the thinking on this intergenerational wealth transfer, see Harvey D. Shapiro, "The Coming Inheritance Bonanza," *Institutional Investor*, vol. 38, no. 6 (June 1994): 143–48.

60. Foundation Center, *Foundation Yearbook, 2001*, p. 43.

61. Craig Smith, "The New Corporate Philanthropy," *Harvard Business Review*, vol. 72 (May/June 1994): 105–16, especially p. 107; Jane Nelson, *Business as Partners in Development: Creating Wealth for Countries, Companies, and Communities* (London: Prince of Wales Business Leaders Forum, 1996); Reynold Levy, *Give and Take: A Candid Account of Corporate Philanthropy* (Harvard Business School, 1999).

62. As "third way" theorist Anthony Giddens has put it, "The fostering of an active civil society is a basic part of the politics of the third way." Anthony Giddens, *The Third Way: The Renewal of Social Democracy* (Cambridge, U.K.: Polity, 1998), p. 78.

63. The number of natural disasters tripled between the 1960s and the 1990s, while the number of armed conflicts, many of them civil wars, jumped from an average of twenty-three per year in the 1960s to over forty per year in the 1990s. See chapter 7 by Shepard Forman and Abby Stoddard.

64. Robert Putnam, *Bowling Alone: The Collapse and Revival of American Community* (New York: Simon and Schuster, 2000).

65. U.S. Social Security Administration, *Annual Statistical Supplement to the Social Security Bulletin* (Washington: U.S. Department of Health and Human Services, Social Security Administration, 2000), pp. 119–22.

66. U.S. House of Representatives, Committee on Ways and Means, *2000 Green Book*, p. 214. Expenditures are adjusted for inflation and expressed in 1999 dollars.

67. U.S. House of Representatives, Committee on Ways and Means, *2000 Green Book*, pp. 892–93; Teresa A. Coughlin, Leighton Ku, and John Holahan, *Medicaid since 1980: Costs, Coverage, and the Shifting Alliance between the Federal Government and the States* (Washington: Urban Institute Press, 1994), p. 2.

68. U.S. House of Representatives, Committee on Ways and Means, *2000 Green Book*, pp. 924, 927.

69. U.S. House of Representatives, Committee on Ways and Means, *2000 Green Book*, pp. 597, 953–54.

70. Coughlin, Ku, and Holahan, *Medicaid since 1980*, p. 87. For further detail, see chapter 4 by Stephen Smith.

71. As of 1998, for example, thirty-five states as well as the District of Columbia had agreed to extend coverage to the so-called "medically needy"—that is, individuals who are otherwise eligible for Medicaid coverage but who exceed the Medicaid income limits; twenty-two agreed to offer hospice care, twenty-six agreed to cover skilled nursing facilities for individuals under twenty-one, and thirty-one agreed to provide rehabilitative

services. U.S. House of Representatives, Committee on Ways and Means, *2000 Green Book*, p. 927.

72. Computed from data in U.S. Social Security Administration, *Social Security Bulletin* (Washington: U.S. Department of Health and Human Services, Social Security Administration, 1997 and 1990).

73. U.S. House of Representatives, Committee on Ways and Means, *2000 Green Book*, p. 354.

74. The number of people on "welfare" fell by half between 1994 and 1999, from 14.2 million in 1994 to 7.2 million in 1999. In addition, the portion of those remaining on the rolls requiring full cash grants also declined because more of them were working. States were guaranteed federal grants under the new temporary assistance for needy families (TANF) program at their peak levels of the early 1990s and were also obligated to maintain their own spending on needy families at 75 percent of their previous levels. U.S. House of Representatives, Committee on Ways and Means, *2000 Green Book*, pp. 376, 411.

75. For a general discussion of these "alternative tools" of public action, see Lester M. Salamon, "The New Governance and the Tools of Public Action: An Introduction," in Salamon, ed., *Tools of Government*, pp. 1–47. For a discussion of tax expenditures and loan guarantees, see Christopher Howard, "Tax Expenditures," in Salamon, ed., *Tools of Government*, pp. 410–44; and Thomas H. Stanton, "Loans and Loan Guarantees," in Salamon, ed., *Tools of Government*, pp. 381–409.

76. The \$3.56 billion in subsidies made available to middle-income and lower-middle-income families through the daycare tax credit thus exceeds the roughly \$3 billion in subsidies provided to poor families through the childcare and development block grant.

77. Rosabeth Moss Kanter and David V. Summers, "Doing Well While Doing Good: Dilemmas of Performance Management in Nonprofit Organizations and the Need for a Multiple-Constituency Approach," in Walter W. Powell, ed., *The Nonprofit Sector: A Research Handbook* (Yale University Press, 1987), p. 154.

78. Regina Herzlinger, "Can Public Trust in Nonprofits and Governments Be Restored?" *Harvard Business Review*, vol. 9 (March/April 1996): 98.

79. Data assembled by Independent Sector, the national umbrella organization representing the nonprofit sector, suggest a considerable slowing of the rate of revenue growth for most components of the nonprofit sector during the most recent 1992–97 period. However, data generated from Form 990s filed by nonprofit organizations fail to confirm this slowdown. Thus, for example, while the Independent Sector data indicate real, inflation-adjusted growth rates of 2.7, 1.8, and 3.8 percent a year for all nonprofit organizations, for health organizations, and for social service organizations, respectively, during 1992–97, the Form 990 data show real increases of 4.4, 2.9, and 7.2 percent a year, or nearly twice as great, for similar classes of organizations during virtually the same period, 1992–98. See Weitzman and others, *New Nonprofit Almanac*, pp. 102–03, 144–45.

80. Internal Revenue Service, *Data Book* (Washington: Internal Revenue Service, various years); Weitzman and others, *New Nonprofit Amanac*, pp. 4–5. Nonprofit organizations are not required to incorporate or register with the Internal Revenue Service unless they have annual gross receipts of \$5,000 or more and wish to avail themselves of the charitable tax exemption. Religious congregations are not required to register even if they exceed these limits, although many do. It is therefore likely that more organizations exist than are captured in Internal Revenue Service records. It is also possible that some of the new registrants are organizations that have long existed but have chosen to register only in recent years. Because the legal and financial advantages of registration are substantial, however, it seems likely that the data reported here represent real growth in the number of organizations despite these caveats.

81. This same picture of organizational vitality emerges from detailed scrutiny of the Form 990s that registered nonprofit organizations are obliged to file with the Internal Revenue Service. Because these forms are only required of organizations with \$25,000 or more in revenue, it might be assumed that older and larger organizations would dominate the reporting agencies. Yet a recent analysis of these reporting organizations reveals that most of those in existence as of 1998 had been founded since 1985, and half of these had been founded since 1992. Weitzman and others, *New Nonprofit Almanac*, p. 129.

82. Julian Wolpert, *Patterns of Generosity in America: Who's Holding the Safety Net?* (New York: Twentieth Century Fund, 1993), pp. 7, 27, 39–40. Sarah Dewees and Lester M. Salamon, "Maryland Nonprofit Employment: 1999," Johns Hopkins Nonprofit Employment Bulletin 3 (Baltimore, Johns Hopkins University, Institute for Policy Studies, Center for Civil Society, May 2001).

83. See, for example: Raymond Hernandez, "A Broad Alliance Tries to Head off Cuts in Medicare," *New York Times*, May 13, 2001, p. A1.

84. Weitzman and others, *New Nonprofit Almanac*, 2002, pp. 136, 168.

85. In one of the special ironies of the nonprofit field, the principal generator of data on private charitable giving in the United States has long been the trade association representing the nation's leading *for-profit* fundraising firms, the American Association of Fund-Raising Counsel.

86. Harvey Lipman, "Survey Finds Rapid Rise in Assets and Grants of Donor-Advised Funds," *Chronicle of Philanthropy*, May 31, 2001, p. 10.

87. See, for example, Thomas J. Billitteri, "A Run for the Money: Growth in Donor-Advised Accounts Spurs Fierce Competition for Funds," *Chronicle of Philanthropy*, April 20, 2000, p. 1.

88. Philanthropy did better in the most recent period (1992–97) than earlier, and there is some hope that this more recent pattern will hold, although the stock market decline of 2000–02 makes this somewhat doubtful.

89. Harvey Lipman and Elizabeth Schwinn, "The Business of Charity: Nonprofit Groups Reap Billions in Tax-Free Income Annually," *Chronicle of Philanthropy*, October 18, 2001, p. 25.

90. See, for example, Mary Williams Wals, "Hospital Group's Link to Company Is Criticized," *New York Times*, April 27, 2002, p. B1; Walt Bogdanich, "Two Hospital Fundraising Groups Face Questions over Conflicts," *New York Times*, March 24, 2002, p. A1.

91. Roberts Enterprise Development Fund, *Social Purpose Enterprises and Venture Philanthropy in the New Millennium* (San Francisco: Roberts Enterprise Development Fund, 1999); [www.independentsector.org/pathfinder](http://www.independentsector.org/pathfinder) [August 29, 2002], a website created by the Pathfinder Project of Independent Sector and the University of Maryland.

92. Kearns, *Private Sector Strategies for Social Sector Success*, p. 25.

93. Based on recent offerings from John Wiley and Sons' website, [www.wiley.co.uk/products/subject/business/nonprofit/management.html](http://www.wiley.co.uk/products/subject/business/nonprofit/management.html) [August 14, 2002].

94. Frances Hesselbein, "Foreword," in Peter Drucker, *The Drucker Foundation Self-Assessment Tool*, rev. ed. (San Francisco: Jossey-Bass, 1999), p. vi.

95. See, for example, Walter W. Powell and Jason Owen-Smith, "Universities as Creators and Retailers of Intellectual Property," in Burton Weisbrod, ed., *To Profit or Not to Profit: The Commercial Transformation of the Nonprofit Sector* (Cambridge University Press, 1998), pp. 169–93.

96. Tracy Thompson, "Billy Shore Wants to Help Nonprofit Institutions Link Their Charitable Works with Profit-Making Enterprises," *Washington Post Magazine*, December 19, 1999, pp. 7–22; Bill Shore, *Revolution of the Heart: A New Strategy for Creating Wealth and Meaningful Change* (New York: Riverhead Books, 1995).

97. Susan Gray and Holly Hall, "Cashing in on Charity's Good Name," *Chronicle of Philanthropy*, July 20, 1998, p. 26; Business for Social Responsibility Education Fund, *Cause-Related Marketing* (San Francisco: Business for Social Responsibility Education Fund, 1999).

98. Eyal Press and Jennifer Washburn, "The Kept University," *Atlantic Monthly* (March 2000): 39–40.

99. Rosabeth Moss Kanter, "Innovation and Change: From Spare Change to Real Change: The Social Sector as Beta Site for Business Innovation," *Harvard Business Review*, vol. 77, no. 3 (May/June 1999): 122–32.

100. Aspen Institute, Nonprofit Sector Strategy Group, *The Nonprofit Sector and Business: New Visions, New Opportunities, New Challenges* (Washington: Aspen Institute, 2001).

101. According to Hall, this invention was undertaken to protect the institution of the private foundation and other charitable institutions supported by wealthy individuals from the onslaught of populist reformers worried about the antidemocratic influence these institutions wielded over the national economy and national life. Peter Hall, *Inventing the Nonprofit Sector and Other Essays on Philanthropy, Voluntarism, and Nonprofit Organizations* (Johns Hopkins University Press, 1992), pp. 66–80.

102. See, for example, Kurt Eichenwald, "Columbia/HCA Fraud Case May Be Widened, U.S. Says," *New York Times*, February 28, 1998; and chapter 2 in this volume by Bradford Gray and Mark Schlesinger.

103. Since the beginning of 2000, Moody's Investors Service has downgraded the bonds of 121 nonprofit hospitals, affecting \$24 billion in bonds. See Reed Abelson, "Demand, but No Capital, at Nonprofit Hospitals," *New York Times*, June 12, 2002, p. B1.

104. Putnam, *Bowling Alone*.

105. As detailed more fully in chapter 9 by Elizabeth Boris and Jeff Krehely, lobbying differs from advocacy in that it is directed at specific pieces of legislation or regulatory actions.

106. Berry, *The New Liberalism*.

107. Berry, *The New Liberalism*, p. 119.

108. See, for example, Margaret E. Keck and Kathryn Sikkink, *Activists beyond Borders: Advocacy Networks in International Politics* (Cornell University Press, 1999); Anne M. Florini, ed., *The Third Force: The Rise of Transnational Civil Society* (Washington: Japan Center for International Exchange and the Carnegie Endowment for International Peace, 2000).

109. Berry, *The New Liberalism*, pp. 119–52.

110. A classic statement of this tension, focusing on a much earlier period, can be found in David Rosner, *A Once Charitable Enterprise: Hospitals and Health Care in Brooklyn and New York, 1885–1915* (Princeton University Press, 1982). For more recent analyses, see Regina Herzlinger and William S. Krasker, "Who Profits from Nonprofits?" *Harvard Business Review*, vol. 65 (January/February 1987): 93–106; David S. Salkever and Richard G. Frank, "Health Services," in Charles T. Clotfelter, ed., *Who Benefits from the Nonprofit Sector?* (University of Chicago Press, 1992), pp. 24–54.

111. Press and Washburn, "The Kept University." See also Donald Stewart, Pearl Rock Kane, and Lisa Scruggs in chapter 3 of this volume.

112. Estelle James, "Commercialism among Nonprofits: Objectives, Opportunities, and Constraints," in Weisbrod, ed., *To Profit or Not to Profit*, p. 273. For the alternative theory, see Burton Weisbrod, "Modeling the Nonprofit Organization as a Multiproduct Firm: A Framework for Choice," in Weisbrod, ed., *To Profit or Not to Profit*, pp. 47–64.

113. Evelyn Brody, "Agents without Principals: The Economic Convergence of the Nonprofit and For-Profit Organizational Forms," *New York Law School Law Review*, vol. 40, no. 3 (1996): 457–536. See also chapter 15 in this volume by Evelyn Brody.

114. James, "Commercialism among Nonprofits," p. 279.

115. Chapin Hall Strategic Restructuring Study.

116. "Please, Allow Us to Introduce Ourselves," *Nonprofit Quarterly*, vol. 8, no. 3 (July 2001): 3, quoting a Rolling Stones 1968 refrain.

117. Milt Freudenheim, "Quality Goals in Incentives for Hospitals," *New York Times*, June 24, 2002, p. C1.

118. Under the existing tax deduction system, taxpayers are allowed to subtract their charitable contributions from their taxable income if they itemize their deductions. Since higher-income taxpayers face higher tax rates, however, the resulting deductions are "worth" more to them than to lower-income taxpayers or those who do not itemize their deductions. Tax credits, however, are deducted from the actual taxes a taxpayer owes. Credits can be set equal to the contribution or at some fraction of the contribution (for example, 40 percent of the contribution can be deducted from the tax bill).

