

SUBMISSION TO PRODUCTIVITY COMMISSION IN RESPONSE TO ITS ISSUES PAPER *CONTRIBUTION OF THE NOT FOR PROFIT SECTOR*

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This submission

Most of this submission addresses the first two terms of reference: the contribution of nonprofit organisations and the possibilities of measuring these contributions.

- Because definition is at the heart of measurement, **Part 1** draws attention to the distorting effect on measurement caused by a unilateral decision by the Australian Taxation Office (ATO) to define as nonprofits only tax exempt organisations.
- **Part 2** reviews the many literatures that include claims about the effects or impacts of nonprofit organisations.
- **Part 3** identifies the different groups who are interested in the measurement of Australia's nonprofit organisations and suggests that the main priority will be to focus on providing current input measures in far greater detail.
- **Part 4** identifies a range of ways in which nonprofit organisations contribute to economy, society and polity, but also warns against exaggerating these impacts and taking into account the negative impact that some nonprofits can have.
- **Part 5** touches on misunderstandings associated with the funding of certain nonprofits by governments and suggests that there are three basic funding models each one being the most appropriate in particular circumstances.
- Finally, **Part 6** contributes brief remarks on the measurement of volunteers and on regulatory reform.

PART 1: Definitions.

Before addressing the contribution of “not-for-profit” organisations it is important to be clear about the organisations that should be included in any assessment of the contribution and measurement of nonprofit organisations.

My preference is for the term nonprofit organisation, a term that is widely used internationally and a term that holds within it a clear indication of the drivers of that class of organisation's behaviour. Like many descriptors it is a short hand; in this case for private, nonprofit distributing organisations. The term “private” distinguishes nonprofit organisations from government owned and controlled organisations; “nonprofit distributing” distinguishes these organisations from that other set of private organisations, namely for-profit organisations, conventionally called businesses, which are free to distribute any surplus to owners.

By willingly choosing to prevent the annual distribution of profits to the members, persons or organisations which control the nonprofit, its founders are indicating that

its purpose is to serve those members (through the provision of services, facilities, competitions or opportunities for various activities such as hobbies or worship), or a wider public.

In addition, those that serve a wider public generally prohibit the distribution of any net assets on winding-up; some member serving nonprofits (mutuals) do also, but others do not. Those that chose to prohibit the distribution of net assets on winding-up specify distribution to a nonprofit with similar prohibition in its constitution and pursuing a similar purpose. It is worth noting that in September 2007 the Federal Court (in the Coleambally Irrigation Mutual Cooperative Ltd case) ruled that to meet the legal test for a mutual or member serving nonprofit, an organisation must be able to distribute net assets to members on winding up.

What shapes the behaviour of nonprofit organisations and distinguishes them from the behaviour of for-profits is the prohibition on distribution of annual profit, not the prohibition on the distribution of net assets. Yet the *Issues Paper* mistakenly conflates the second and first prohibition and talks of “bodies corporate and finance and insurance mutuals being typically excluded from the sector on the grounds that they can distribute surpluses to members” (Box 1). The only time that they can distribute surpluses (strictly speaking net assets) to members is on winding up. In most cases if they wind up it will be because they are insolvent and will have no net assets to distribute. In other cases (and with government encouragement there have been many) they will be converted to a for-profit and convert collectively owned assets into shares for members. They then cease to be a mutual but until that moment they are a mutual and for all but perhaps the last few months when this change of status is being considered by board and senior management they will behave as a mutual. Until the moment of conversion they should be counted as nonprofit mutual organisations (if not what are they? – clearly not a for-profit entity).

The *Briefing Note on Measurement* is more precise and claims that finance and insurance mutuals are excluded because while they do not distribute profits they allow distribution of assets to members in event of winding up. That is not grounds for excluding them from the universe of nonprofit organisations. I have already explained that it is only the first prohibition that shapes organisational behaviour. As well, it is only the prohibition on distribution of annual profits that is used to define nonprofits internationally. There are other reasons why certain nonprofits are excluded from influential attempts to define the nonprofit universe but they are more to do with tradition and prejudice. These will be touched on below, but first let us examine the source of Australian confusion about what is a nonprofit organisation.

The major source of the Australian confusion about what constitutes a nonprofit organisation lies with the ATO which asserts that only organisations to which it gives full tax exempt status can be called nonprofit organisations.

To qualify for income tax exemption (via any of the 34 ways available), and for most other tax breaks available for nonprofit organisations, the Australian Taxation Office requires nonprofit organisations to have both prohibitions in their constitution. This is perfectly reasonable as they are the recipients of indirect public support. However, to claim as does the ATO that to qualify for the description of nonprofit (or not-for-profit) an organisation must have both prohibitions in their constitution is nonsense.

It is the prohibition on annual profit alone that shapes behaviour different to that of a for-profit.

A further problem with the ATO practice is that it makes comparisons, either historical or internationally, impossible. This is because no other country adopts the criteria of the Income Tax Assessment Act (ITAA) to define a nonprofit organisation and because that criteria changes over time as governments amend the act to grant tax exemption to additional nonprofits.

The insistence by the ATO that the term non-profit be applied only to those organisations that have the two prohibitions on profit distribution is behind the decision to omit certain nonprofits from the *1999-2000 Nonprofit Institutions Satellite Account* and restricts the capacity of the ABS to identify the full range of economically significant nonprofit organisations.

The organisations in question are not only those in the finance and insurance services industry, including credit unions, the few remaining cooperative building societies and mutual insurance funds, mainly found in health insurance (but there too a shrinking group). They also include the numerous but mainly economically insignificant strata title bodies corporate and many other organisations that are invariably viewed as nonprofits, such as hobby groups, political parties, many interest/advocacy groups, and community development organisations. There is no point to them having a clause prohibiting distribution of nett assets, as they are not eligible for full tax exemption; indeed, according to the Federal Court's Coleambally Cooperative judgement, if they are to qualify for tax concessions available to mutuals (exemption of revenue earned trading with members), they must not have such a prohibition.

The larger of these mutuals will appear on the ATO register because they seek an ABN and register for GST. If the ATO prohibit these mutuals from nonprofit status to suit its unique definition, then it reduces the size of the nonprofit sector.

The case of registered clubs demonstrates the confusion the ATO has created, and also that it uses full tax exemption as a proxy for nonprofit status. Under the ITAA the ATO allows registered clubs associated with a sport (eg Rugby League, bowls) to claim full tax exemption. These are listed on the ATO maintained register and counted by the ABS as part of the nonprofit organisations. Many other registered clubs (eg Workers clubs, RSL clubs) are not so listed and are treated as for-profit entities. They are not counted as part of the nonprofit sector, because they are not fully tax exempt (they are partly tax exempt because they can exempt mutual income from taxation). Yet, under the Registered Clubs Act in NSW (at least) they are required to have both prohibitions (on the distribution of profits and nett assets) written into their constitution.

As noted already, other countries use the prohibition of annual profit to define a nonprofit organisation. If the narrower ATO definition of nonprofit is used in Australia it will make international comparisons impossible.

Recommendations:

The ATO should be urged to adopt international practice in defining what constitutes a nonprofit organisations.

The way the ATO flags nonprofit organisations on its register should be examined to ensure its conflation of tax exempt status with nonprofit status have not removed genuine nonprofits from being so identified on the register.

However, adding to the confusion, another reason for omitting nonprofit organisations in the finance and insurance services industry from the Nonprofit Institutions Satellite Account is because they are excluded by the United Nations *Handbook on Non-profit Institutions in the System of National Accounts*. This exclusion has nothing to do with whether or not they allow distribution of nett assets on winding-up. Rather it is a consequence of compromises reached in the first attempt to define nonprofit organisations and collect data on a comparative basis. These compromises were then incorporated in the UN *Handbook*.

The first attempts to define, measure and compare nonprofit organisations cross-nationally were made in the early 1990s as part of the Johns Hopkins' University's Comparative Nonprofit Project. The US/UK leaders of this project tended to emphasise charities as the heart of the nonprofit sector and in the earliest iteration of what became the ICNPO, they excluded finance and insurance mutuals, unions, political parties and religious organisations from inclusion. Credit unions could be included if they were part of a community development strategy (as in many Southern countries) rather than being long established financial institutions as in Australia and most of Europe (thought not the UK). In the second round of the Hopkins' study, European (and Australian) members of the consortium insisted that these exclusions made no sense and so religious organisations, unions and political parties were added back, but, to salve US pride, finance and insurance mutuals remained excluded (as financial institutions the measurement of their contribution posed other problems). As an indication of the different outlook of most European countries, the European Union's statistical agency, Eurostat, is developing a satellite account for the social economy which, along with conventional nonprofits associations and foundations, includes finance and insurance mutuals and also trading cooperatives that distribute a dividend (based on use) which they include as part of the social economy.

If Australia is to prepare a nonprofit institutions satellite account according to UN standards, it will continue to omit finance and insurance mutuals from the estimates. But this will be because of tradition or convention, not because they are not nonprofit organisations.

Recommendation:

The Productivity Commission should ensure that the reason given for the omission of finance and insurance mutuals from the Satellite Account is because of convention or tradition, not because they are not nonprofit organisations.

PART 2: Contributions

The question of the contribution or impact of nonprofit organisations has sometimes exercised scholars internationally and in Australia. Scholarly attention has largely

followed several streams. And while there has been collaboration between these it has not developed to the extent that there is a clearly articulated and widely accepted theory of nonprofit organisations that, inter alia, identifies the various ways nonprofit organisations contribute to the wider social formation in which they are embedded. Nonetheless these efforts have provided a number of useful insights into the various contributions of various nonprofits to economy, society and the political system. A brief account of the various streams illustrates this. The account also illustrates the way that insights into the contribution of nonprofit organisations emerge from other research interests. It is clear that understanding the contributions of this unique but varied set of organisations is a work in progress.

One stream, the best developed theoretically, is economic. A good deal of research and theorising was devoted to this class of organisations in the United States in the 1980s and 90s. The focus of this attention was on why they existed at all. It was proposed that they were a sign of both market and government failure, and that they possessed characteristics that advantaged them in certain environments, namely that they were more trustworthy (Rose Ackerman 1986; Weisbrod 1988; Hansmann 1996). For the most part they were demand side explanations, though James developed a supply side theory based on analysis of cross-national data.

Several streams have emerged from political science. One of the earliest took as its starting point the question of why fascism emerged in some previously democratic nations and the growth of communist dictatorships (Almond and Verba 1963). Its initial interest was in the apparent correlation between high levels of volunteering, political participation and strong democratic political systems. Later it went on to explore in great depth the contribution of membership of nonprofit associations as a major spur to participation in the United States political system of disadvantaged peoples such as Afro-Americans (Verba and Nie 1972; Verba et al 1995). The importance, or weakness of voluntary associations was an important point of difference between those arguing a pluralist account of political power in American cities (eg Dahl 1961) and those arguing for control by a power elite (Mills, 1956).

This debate drew on and invigorated an older interest in community structure, decision making and power. Community studies in North America, Europe and Australia all gave attention to the presence of voluntary associations, often offering rich descriptions of their workings and sometimes drawing them into a wider theory. In Australia, for example Wild (1981) argues that voluntary associations were part of, and helped sustain the structure of social stratification.

Another stream also emerging in the 1940s was mainly developed within sociology and social work disciplines was interested in the contribution of what they called voluntary action and voluntary associations. From this grew an interest in the role of voluntary associations in the provision of social services (Beveridge 1948; Sills 1957). Others tried to incorporate voluntary associations within wider theories, for example of complex organisations (Etzioni 1961)

Then, in the 1990s, from out of the political science tradition but drawing on social theories developed by the sociologist James Coleman, the political scientist Robert Putnam argued for the crucial role of social capital and the importance of voluntary associations in reproducing social capital. Initially he invoked the strength of

voluntary associations to explain why certain regions of Italy successfully embraced the new level of decentralised regional government that Italy had introduced a few years earlier (Putnam 1993). He then applied these insights to the United States and claimed to find there a decline in voluntary association membership coinciding with a decline in social capital (Putnam 2000). The study of social capital became very popular but while it advanced some way theoretically, lack of agreement about what it was has led to a decline in its standing. In the scholarly controversies that marked the rise and fall of social capital, the contribution of nonprofit associations to social capital and through that to the provision of wider social contributions was clarified to a limited degree but did not advance far.

Also in the 1980s and 1990s, other political scientists and anthropologists were rediscovering the importance of voluntary, cooperative agreements among users for the management of common pool resources such as water or fish (Ostrom 1990).

Beginning in the 1950s another stream of political scientists, historians and sociologists began writing about social movements as an explanation for massive social changes that had been wrought in the 20th century. A particular focus was on the labour movement but also the first wave of feminism and the temperance movement also received attention. The emergence in the 1960s and 1970s of a range of “new” social movements such as the civil rights movement, the second wave of feminism and the environment movement generated further considerable academic output. Oddly, although nonprofit organisations were at the organisational heart of social movements, this was never acknowledged and social movement theory has yet to interact creatively with theorising about nonprofit organisations. However there are certain insights to be gained from social movement theory, particularly around the importance of nonprofit associations for bringing about political and social change and the importance of associations to the expression of identity (Zald 2004).

A further interest in voluntary associations emerged in the 1980s with the renewed interest in civil society. This current interest in civil society initially began as a product its adoption in the 1980s by activists in Eastern Europe, Latin America and Asia who were struggling against oppressive communist regimes or military dictatorships. They referred to ‘civil society’ to describe what they were and what they were trying to enlarge. Civil society was people acting as citizens, freely, collectively and for a wider good; it was also the sphere where such citizen activity took place (Lyons 2009).

The success of these activists led to the popularity of the term not only in those societies but in the United States, both among social science academics and many US foundations. In this process, civil society came to be associated with the nonprofit sector, and used interchangeably with nonprofit sector (Salamon et al 1999). It also acquired a normative dimension; it became something to be encouraged. It became entangled with the discovery of social capital and tied in with wider projects to extend tolerance, democracy and good governance and to end corruption. For a time, it was adopted by the World Bank. It came to be seen as a pre-requisite for successful social and economic development. For some it acquired a global dimension, representing a vision of a less violent world and the organisations, institutions and processes that might bring that about. Along the way there emerged two attempts to measure and compare civil society in various countries. While these relied to various degrees on

measures of the nonprofit sector, they also introduced other measures, such as the extent to which the legal system encouraged the formation of associations (Lyons 2009).

These various preoccupations animating scholars from different disciplines largely prevented systematic and collective thinking about the effect nonprofit organisations have on society and the contributions they make. But they also make it clear that insights arise from the pursuit of research into different and wider questions and from within a variety of theoretical frameworks. This in turn suggests that efforts to frame a theory of nonprofit impact will require a good deal of research into varied literatures and an ability to negotiate and bring together a variety of disciplinary frames and bodies of theory. Efforts so far do not meet those requirements.

The first explicit attempt to identify and measure the impact of nonprofit organisations emerged from the first attempt to measure the size of nonprofit organisations in a cross-national comparative context. In 1998, Salamon proposed a framework based on a reading of the literature of nonprofit organisations as an add-on to the second phase of the Comparative Nonprofit Project. It identified roles that nonprofit organisations played: service, innovation, advocacy, expressive and community building (Chinnock and Salamon 2002). In 2001, Virginia Hodgkinson, who had headed research for the Independent Sector for many years but had moved to Georgetown University and a colleague Patrice Flynn edited a book, *Measuring the Impact of the Nonprofit Sector* (Flynn and Hodgkinson 2001). In it Kenneth Land included a chapter reviewing the state of the social indicators movement and proposing social indicators for assessing the impact of the nonprofit sector of society. He argued that different organisation needed different measures and proposed dividing organisations according to their mission into a four way typology: service, charitable, philanthropy and fellowship (Land 2001).

In my 2001 *Third Sector: The Contribution of Nonprofit and Cooperative Enterprises in Australia* (Lyons 2001), I attempted to summarise major contributions of the nonprofit sector in two chapters: “making an economic contribution” and “making a social and political contribution”. These chapters largely summarised the bodies of research referred to above.

In 2007 an important study by the Allen Consulting Group for the Victorian government’s Strengthening Community Organisations Project drew on Land to develop a four-way classification of the objectives of nonprofit organisations: service delivery, advocacy, philanthropy and fellowship. Around this division of nonprofits according to their objects they created a four level framework for measurement. What would be measured for organisations with these different objective functions were organisational inputs, outputs, intended outcomes and unintended outcomes (Allen Consulting Group 2007).

The Productivity Commission appears to have adopted a similar framework for its attempt to identify and measure the contribution of the nonprofit sector. The main differences are that while the Productivity Commission has retained four levels of measurement, with the last two slightly modified: outcomes and impacts rather than intended and unintended outcomes, it has used a variety of terms to describe variations within each of these. For example, outputs are divided into services,

connecting the community, advocacy and social endowments while outcomes are split into service outcomes, connection outcomes, advocacy outcomes, existence outcomes and consumption outcomes.

While there is a certain heuristic value in creating frameworks like these, they run the risk of closing off possibilities. They miss, for example, the contribution of nonprofit organisations to solving common pool resource problems or bringing about wide ranging social change (to take two of the bodies of work referred to above). They also ignore the organisation of religious worship that is invariably done through nonprofit organisations.

They also risk overlooking the multiple effects that a nonprofit organisation can have in addition to whatever may be its predominate purpose. For example, the same nonprofit organisation may generate several of the Productivity Commission's outcomes. In addition, the level of abstraction in some of the titles of outcomes (eg "existence outcomes", "consumption outcomes") conceal more than they reveal.

Earlier in this section the various disciplinary contributions to understanding the nonprofit sector were identified. Each of these started from within a particular theoretical framework. Accounts of the contribution of nonprofit organisations need to describe how these work and by implication reveal their larger theoretical assumptions. We need a great deal more research and discussion to develop an understanding of the contribution of nonprofit organisations including efforts to measure these. The risk of putting everything into a framework is that it wrongly suggests closure: that all contributions have been identified leaving only the measurement task. If the Productivity Commission wishes to retain its framework as a heuristic device, it should make more clear that it is that and that it is incomplete and that a lot more work needs to be done. Proposing a set of targeted research grants to encourage research and thinking about these matters over the next 5 years might be in order.

PART 3: Measurement

There are two important aspects to the any consideration of improving the measurement of nonprofit organisations.

One is the difficulty of measuring many of the outputs of nonprofit organisations and the very great difficulty, some would say impossibility, of measuring outcomes and impacts (to use the Productivity Commission's distinctions). The great difficulty with measuring outcomes is that many of those that are sought are not evidenced for many years. And even those that are more immediate are not always simply attributable to the activities of nonprofit organisations. Such measures are not open to systematic specification and data gathering.

A second aspect is the purpose of measuring: who is interested in measurements? A suggestion of some of the actors and their possible interests is given below.

Who is interested in measuring the nonprofit sector?

Governments have long relied on nonprofit institutions for the provision of many services. Understandably, their focus has been exclusively on those organisations they fund. They know little of the nonprofit sector overall. This has sometimes led to policy confusion, as occurred with the introduction of the GST. Reflecting overseas trends, Australian governments are coming slowly to recognise the wider contribution of all nonprofit organisations, especially their overall contribution to sustaining strong communities. They have sought to encourage volunteering and philanthropic giving. Such policy initiatives need reliable and regular data if their effectiveness is to be evaluated. But this interest is still embryonic. State and territory governments lack any detail of the configuration of the sector within their jurisdictions. Lack of data on the nonprofit part of the economy stands in marked contrast with the level of data collected to monitor the health of the business economy, and to report the performance of governments.

Within the *nonprofit sector*, there is a growing interest in obtaining data on the size and composition of the sector in its various components and along its various dimensions. For example, the National Roundtable of Nonprofit Organisations brings together peaks from most fields of significant nonprofit activity. It defines its major role as being to draw the attention of the Australian public to the contribution of the sector to Australia's economy, society and political life. Nonprofit organisations are also seeking to improve their management and governance and to reposition themselves in an increasingly competitive environment. Their leaders are looking for data on the average performance of nonprofits in similar industries to provide them with benchmarks against which to assess their own performance. Improvement in the management of larger nonprofit organisations depends on the availability of better comparative financial data.

Academic interest in the nonprofit sector and associated phenomena such as volunteering and social capital has been growing over the past decade. A research association was formed almost twenty years ago and has over one hundred members in more than twenty universities. Nonprofit institutions and philanthropic behaviours are of interest to all major social science disciplines and to those in professional disciplines such as accounting, marketing, management and law. University researchers need reliable trend data on the dimensions of nonprofit organisations and related phenomena. This will provide a basic framework within which they can collect and generalise from more specialised data to test and build theories of nonprofit behaviour.

Business interest in the nonprofit sector is growing also. Businesses recognise nonprofit organisations as a market for specialist services and need data on the dimensions of the sector to develop their business plans. Many businesses are also looking to convert their support for nonprofit institutions into more enduring partnerships. They expect to be able to assess potential partners against industry averages. High wealth individuals are becoming more interested in philanthropy and, once again, specialist firms are seeking to assist them with high quality advisory services that in turn require good quality data.

What sort of data is most sought?

The basic demand is for comprehensive and detailed input data. This is the sort of data that can be provided in a fully elaborated satellite account and industry surveys. The items of data (eg employment, sources of revenue) collected by the ABS and included in the satellite account (or the 2006-07 survey results), with minor modifications, are satisfactory. What is lacking at present is the degree of detail and the frequency to enable comparisons to be drawn. All that is required is that where the ABS needs to rely on survey data rather than data from administrative collections, it is sufficiently well funded to draw a sample large enough for it to report data by ICNPO subgroup (for international comparisons), and by industry groups using ANZSIC, and to be able to do this by state and territory. Release of detailed data such would potentially be contained in a fully elaborated satellite account on a triennial basis should be sufficient; provided some high level indications of change could be learnt from the annual issue of the full National Accounts. The importance of publishing data on the distribution of nonprofits across industries is of particular importance. The failure to do this (because of small samples) is a major problem with the 1999-2000 Satellite account and its 2006-07 successor.

There is likely to be pressure to extend data collection to include far more nonprofit organisations (as was done in New Zealand). This should be resisted. Indeed, for purposes of comparability the ABS should consider only including nonprofit organisations that employ staff, rather than adding an indeterminate of non-employing but economically significant organisations.

Efforts to collect data on outputs or outcomes should also be postponed until adequate data on the inputs the sector is regularly collected. Governments which must provide the resources for the ABS to collect this data may wish to concentrate on a few industries rather than ensure the sector is completely covered. This would be a mistake. Far greater value will be achieved by expanding the sample of employing NPIs than in adding many more small nonprofit organisations to the sample frame or by pursuing outputs that can only be partial and outcomes that are mostly impossible to measure without a massive research.

While it is important for international comparisons to disaggregate the nonprofit sector by the ICNPO (as is partly done at present), it is vital that the sector is also disaggregated by Australian and New Zealand Standard Industry Classification (ANZSIC) as well. Only in this way will the contribution of nonprofits to various industries be assessable. These sort of comparisons between for-profit and nonprofit involvement in different industries are perhaps more important than international comparisons. The aggregation of data into forms suitable for Australian and international comparisons will not be difficult.

The ABS should also ensure that when it conducts industry level surveys of industries where nonprofit organisations are noticeable (eg community services, performing arts, sport, employment and training services) that it stratifies a sufficiently large sample to ensure that data can be reported for nonprofit and for-profit organisations rather than lumping them together as sometimes happens.

The collection and publication of this economic (or input) data should coincide with the collection of data from households on volunteering and sources of financial support, particularly giving by individuals and by business. The ABS has already conducted two surveys of business giving (ABS 1999, 2002) and data on individual giving could be readily collected in the same survey that collects data on volunteering. Data on volunteering and giving should be collected for the same year or almost the same year as is used for the collection of data from nonprofit organisations.

It is not necessary to try and collect data from all nonprofits nor even to enumerate all of these. A focus on nonprofits large enough to employ staff or the slightly larger set of “economically significant nonprofits” is sufficient. The addition of data on volunteering for nonprofit organisations enables an estimate to be made for the whole nonprofit sector.

Output data.

There are several administrative data collections from which output data for certain services provided by nonprofit organisations easily can be gained. These include hospitals, schools, registered child care, aged care provision. To the extent that these can be easily gathered they could be appended to a triennial publication. Their main value is for comparative – to allow the relative contribution of nonprofits to for-profits or government entities to be assessed.

Summary

Overall, the basic framework for providing a useful set of measures for the nonprofit sector are already in place within the ABS. What is needed is the commitment of resources that would enable them to be expanded to the degree outlined above. It is particularly important that this expansion to an adequate level of input data is not distracted by a search for exotic measures at the level of outcomes or impacts.

This is not to argue that such efforts may not be worthwhile, but that they not be at the expense of a comprehensive and regularly updated data set.

It may be that some institutional enhancement is needed to ensure that the ABS is sufficiently resourced to undertake the large sample surveys that are needed. Perhaps a representative advisory group of users is required – not just state and Commonwealth government departments but nonprofit organisations, businesses and academics. Several of these groups may be able to contribute dedicated funds so that the data collection could be funded by more than from the ABS core budget, or a dedicated Commonwealth government commitment.

In addition, while data collections are needed for research, research that uses the data is its main justification and also helps refine the next iteration of data to be collected. The Productivity Commission should examine the value of state and federal governments establishing a research centre, perhaps along the lines of the Australian Housing and Urban Research Institute (AHURI) to encourage this sort of research. Such a research centre could have an institutional relationship with the advisory group proposed above.

Recommendation

The Productivity Commission should explore the need for institutional enhancements that would ensure sufficient funds were available for a comprehensive triennial satellite account of the kind sketched above. Such enhancements might include a small advisory group of representatives of various users, some of whom might also contribute funding to the data collection, along with a linked research group.

PART 4: Another way of thinking about contributions and their measurement

The following paragraphs suggest another way of thinking about the contribution of nonprofit organisations. In addition to identifying contributions that nonprofit organisations make, it also attempts to assess whether these contributions would be generally considered beneficial and most importantly whether they are or could be produced by other institutions or types of organisations.

Both of these qualifications are important as not all nonprofits seek outcomes, or have unintended consequences that most would agree with. Further, many do no more than perform tasks that could and perhaps have been performed by for-profit or government bodies. They are still making a contribution but one that could be substituted, as opposed to a contribution that if not provided by nonprofit association could not be readily duplicated. This distinction is more easily stated than operationalised. In many cases where a nonprofit is providing a service that could be readily provided by a commercial organisation it is also providing other benefits that the for-profit could not, such as the opportunities to participate in the governance of the organisation that a mutual offers (Lyons and Simpson 2009).

One approach to identifying contributions is to think about the ways that NPIs (or many NPIs) contribute to the economy, to society and to the polity or political system.

Economic Contribution

NPIs contribute to the economy:

1. by providing employment,
2. by providing services,
3. by mobilising resources (gifts of money and time) unavailable to other organisational forms,
4. by developing new services or better ways of providing services (innovation).
5. by providing mechanisms for economic coordination and the effective spread of information and skills within the economy.

The first three of these contributions are well recognised. It should be noted that very few (around 38000) NPIs actually employ staff; the great majority rely entirely on volunteer labour. Most NPIs provide some form of service and the services they provide are many. NPIs can be found in most industries, though most commonly in the service industries. Most provide services to their members – that was why they were formed and why new members join. Some provide services to others – this is the conventional mark of a charity as opposed to a mutual. The term service is rather flexible. While delivering a meal to a disabled older person is clearly a service, is

staging an opera? Or teaching a younger generation traditional dances of their parents' ethnic origins? Or conducting a religious ceremony? Some attempts to distinguish between different contributions of NPIs distinguish between service delivery and other broad "objectives" or "roles". Many of the conventional services provided by nonprofit organisations, those supported by governments, could be provided by for-profit or government entities, though certain other benefits may be lost. Other services, especially those associated with interest articulation and representation and religious worship are uniquely provided by nonprofits.

All nonprofit organisations rely on gifts of time from founders and members. The great majority are maintained only by these gifts (volunteering) from some of their members. Many of the 38000 NPIs that employ staff to deliver their mission also mobilise volunteers to add to their output, or to raise funds. They also mobilise gifts money and resources in kind. They are not unique in this: many government entities (schools, hospitals, art galleries and national parks services) also seek gifts of time and money from their users or the wider public. But by far the greater amount of the 700 million hours and around \$10 billion of donated funds and resources are raised by the efforts of the nonprofit sector. The conventional explanation is that when people want to support a cause, they prefer to donate to a nonprofit rather than a for-profit firm (which is they fear may divert the gift to the owner's pocket) or a government department (which is funded by their taxes and may be tempted to divert their donation to other purposes). It is the nonprofit that is more trustworthy. Most of these resources donated to nonprofit organisations are put to public purposes. Without a nonprofit sector, most of these funds would be spent on personal consumption, not a public good.

Nonprofit organisations have been responsible for developing many important innovations in service provision: eg aged person's independent living accommodation, surf lifesaving, telephone and internet counselling – the incentive being the provision of a needed or more appropriate service rather than an increased income. The incentive for innovation by nonprofits is different to that pursued by for-profit entrepreneurs or firms. Conventionally, the latter are motivated to innovate by a desire to make money- but producing some goods more efficiently or a new sort of good that meets a need in new ways and creates a new market. Nonprofit entrepreneurs are focussed on new ways of addressing need. Initially, they are uninterested in markets because those in need are unable to purchase the service (Young 1983). To roll out their innovation they need third party funding. They occupy parts of the economy where for-profit entrepreneurs are unlikely to be found.

The nonprofit form is often chosen by individual producers or for-profit firms who wish to collaborate on a joint venture. Such arrangements hark back to a common solution to what Elinor Ostrom calls common pool problems, such as sharing limited water supplies or avoiding over-fishing – cooperation organised by participants using nonprofit forms are one way of addressing such problems (along with legislation and regulation or the creation of markets by creating and distributing property rights). Nonprofit organisations in the form of business and professional associations also play an important role in the circulation of knowledge and skills within the economy, especially at the level of an industry or profession. They also regulate the behaviour of their members. Often this is mandated by the government, but the legitimacy of the process with those being regulated is a product of the fact that the process is based

on regulation by peers. While some of the tasks performed by business and professional associations, such as information transfer and training can be performed by for-profit or even government organisations, the mutual (or member control) character of these bodies is a strength.

Not all believe such organisations provide an indisputable benefit. Some argue that they interfere with the optimal operation of markets and for that reason at least need regulating.

In considering the provision of services, it should be noted that few services are provided by NPIs alone. The representation of collective interests is one set of services only occasionally provided by for-profit firms; religious worship is inevitably provided by NPIs. For most services, the issue is whether NPIs contribute more, or in a different way to for-profit or government entities – are they more efficient in providing a service, or do so at a better quality for the same price or are they more trustworthy and therefore require less regulation/supervision than a for-profit providers? Do they provide other benefits that other forms cannot replicate? These are both theoretical and empirical questions. To the extent that governments are interested in subsidising the provision of such services, they are now for the most irrelevant for Australia, as governments failed to ask them in the past and now treat for-profits and NPIs alike in most industries.

What of their measurement?

We have readily available data for measuring only the first three of these contributions. They are what is conventionally measured – eg by the ABS in its NPI satellite account, or, (sometimes) in its service industry surveys and voluntary work surveys. The data needs have been discussed above. The final two economic contributions are at this point, not readily operationalised nor measured.

Social Contribution

Nonprofit organisations are embedded in our society. Around 87% of adults belong to at least one nonprofit; most to at least two. A similar percentage claim to support nonprofits with donations. Around 35% claim to volunteer for them (But note that some volunteer and donate to government entities, and even to for-profits).

Nonprofit organisations contribute to society. People form nonprofit organisations to help others or to provide something for themselves. Nonprofit organisations testify to people's capacity voluntarily to work together without direction from government and without the lure of personal enrichment or the necessity of earning a wage. In this way, nonprofit organisations embody and make manifest the virtues of altruism or mutuality and in so doing point to others the possibility and the mechanisms for collective action.

For example:

- By working with the poor and dispossessed and seeking public support for and participation in this work, nonprofit organisations encourage generosity and concern for others in the general population.

- By organising a meeting to mobilise people who might share an interest or an enthusiasm, the capacity for collective action is demonstrated showing others the possibility and the way of acting collectively.

In these ways, the micro-organisational framework that constitutes a community and that Australians take for granted, are maintained – eg hobby clubs, local sports clubs, residents’ associations, playgroups.

Only nonprofit organisations can manifest and encourage the practice of altruism and mutuality.

As well as providing services, nonprofit organisations are the form of organisation most commonly chosen

- to organise opportunities for socialising or fellowship;
- to give expression to (to celebrate) collective identities and
- to worship a God or Gods.

Another advantage claimed for nonprofit organisations is that by bringing together people of different backgrounds and beliefs they help build a tolerant and more cohesive society. They are better placed than for-profits or governments to do this because they are free of an ulterior motive (money making, vote winning).

In addition, nonprofit organisations provide people with an opportunity to learn the skills of organising (running a meeting, keeping minutes and accounts and so on). These can be used in political campaigns (as set out below) but they can also enable a person to organise around a hobby or an enthusiasm or a sport for their children. Such skills are not taught in schools and while they may be acquired in the course of business, they are mostly only learnt via involvement in a nonprofit association. Any free and democratic society needs many people from all walks of life with these skills.

Nonprofit organisations have been the inevitable form of organising behind much of the social changes that have shaped modern western society. Social movements for the most part consist of or are built around, nonprofit organisations. It is from social movements that most important innovations in our social institutions, indeed, most transformatory social changes have arisen. The extraordinary impact of say the 19th century labour movement, the two feminist movements, the civil rights movement and the environment movement, are clear and evident. What is often not acknowledged is that all these movements relied on, were manifested by, thousands of often uncoordinated nonprofit organisations. In part these movements achieved changes in legislation and governance, but they also, most importantly, changed the way people saw the world and related to each other. For some, association with a movement provided an important identity.

In theories of social capital, NPIs are an essential vehicle for the production and reproduction of social capital. In their formation they draw on social capital and thus reproduce it. In most accounts of social capital theory networks are important; especially for the reproduction of bridging and linking social capital. Frequently these networks are nonprofit associations (Passey and Lyons 2006).

As well as being networks, some nonprofit organisations provide space which can be used by other nonprofits or by community members who might be moving to form a new nonprofit. This space is usually a hall but sometimes an open space. In some cases the provision and maintenance of this space is the sole purpose of the nonprofit, as with community hall trusts, but more usually, it is a by-product of their major purpose. Many hobby groups and ethnic associations rely on church halls for meeting, and even storage space; others rely on a local show or racing association for access to an open space for fundraising events. This is not a uniquely nonprofit contribution. Such space is often provided by local government and sometimes by government schools, but theirs is a shrinking rather than a growing presence; without the nonprofit contribution society would be a good deal poorer.

The theory of social exclusion/inclusion, at least in its Australian manifestations does not address the role of organisational forms in building inclusion, though there is a large European literature on social enterprise that locates this particular set of nonprofit associations as a response to social exclusion (mainly, via work insertion) (eg Borzaga and Defourny 2001; Evers and Laville 2004). Australian usage of these concepts appears underdeveloped and welfare focussed. Clearly nonprofit organisations in the social assistance industry contribute to social inclusion in this sense, but this does not seem to be a particular property of the organisational form. Nonprofit organisations in other industries can also contribute to overcoming social exclusion: for example in bringing together excluded groups into learning relationships with mainstream institutions – eg bringing kids from Catholic and Islamic schools together, or the work Surf lifesaving has done in encouraging Lebanese Muslim kids to join surf clubs. It is hard to imagine the last example being successfully pursued by any other than a nonprofit.

Four provisos must be recorded to the above:

1. We have no established measures for these contributions. At a fundamental level, this is because we have no social theory that is as widely accepted as neo-classical economic theory. As a result we have no widely accepted account of the contribution of nonprofit or third sector organisations and therefore no accepted measures of that contribution. Instead, there is competition between structural functionalism, communitarianism, structuration theory, feminist theory, post structuralism, post Marxism and so on, in giving an account of how society works and thus of the contribution of different social institutions to that process. This should not prevent some measures being developed – such as associational membership and so on, but it will mean that some of these inevitably will be contested. It also means that many contributions will be overlooked because they are difficult to measure.

2. It is clear that other organisations and social institutions (eg the family, schools (which might of course be nonprofits)) provide some of the benefits identified as being contributed by nonprofit organisations. Any measure of the contribution of nonprofit organisations to achieving these sought-after outcomes must be able to distinguish effects that are attributable to nonprofits and not other institutions; such distinctions cannot routinely be drawn.

3. Many of the efforts to develop measures of social impact – eg SROI, measure the impact of particular programs, not of the nonprofit. In fact they are independent of

organisational form – ie they can be just as readily used to measure the impact of a program provided by a for-profit or government entity. As well, they have been developed and are only suitable to measure the impact of programs in some social services and employment services – not sport, not the arts, not recreation. Schools have their own set of highly controversial impact measures.

4. It should also be noted that the nonprofit form of organising is also available to those who wish preach intolerance and hatred: in other words that seek social disruption. Measures of the social contribution of NPIs need to net out these effects. This is not easy as some nonprofits champion causes supported by some but strongly opposed by the others. Is their success at mobilising support for a controversial cause a social benefit or not? It is worth recalling that some values we now take for granted, such as indigenous or gay rights were once highly controversial.

What of their measurement?

As already noted, many of these effects can be described but are not easily measured. The measures that we do have are percentage and characteristics of population who are members of associations, occupy leadership roles, or are in other ways active members (ie volunteering for the organisation). Internationally some of these are compared in the World Values Survey (eg Inglehart 1997). There are no widely accepted standards for these measures. Some surveys conducted by university researchers (eg Australian Electoral Survey, the Australian Survey of Social Attitudes, the World Values Survey) collect information on some of these variables. The social capital module in the ABS's 2006 General Social Survey also has some useful data on associational membership that can be cross tabulated with other attitudes behaviours to at least point to correlations between associational membership (or volunteering) and those other attitudes and behaviours. It is a field of research that would repay a concentrated research effort.

Political Contribution

Nonprofit organisations make a major contribution to the effective operation of a democratic political system. Some nonprofit organisations directly participate in the political system, representing to policy makers the views of the many diverse social and economic interests that are present in any complex economy and society and in turn packaging and purveying analysis and interpretation of policies to their members. Business, trade and professional associations are an important set of nonprofits in this context. They and other interest or advocacy groups seek legislative or policy change, or try to resist changes advocated by other interests, including other nonprofits. An important group of nonprofit actors in the political system are political parties. All aspire to have members elected to the legislature where they hope they can exert more influence on the government than they can from outside parliament. Some aspire to form government, on their own or in coalition with other parties.

Most nonprofit organisations do not participate directly in politics, but help underpin or sustain democratic politics by being the “elementary schools of democracy”, in the words of Alexis de Tocqueville describing the United States 170 years ago. They are the places where ordinary people learn some of the basic arts of organising, where they learn how and when to trust strangers, where they gain the confidence to express

their views and to participate in the wider political system. A great deal of US research has been done on this and related issues over the past 40 years (eg Verba and Nie 1972; Verba et al 1995; Warren 2001). Australian research has shown that members of an association are 2.7 times more likely to participate in some form of political action (eg petition signing, boycotting goods, attending meetings etc than people who are not members of an association (Passey and Lyons 2005). More work would be required to demonstrate the direction of the correlation. As well, they are clearly not the only source of learning such political skills.

Sometimes, when people think about these various contributions to the political system, the third sector is referred to as civil society, or, more accurately, as a major component of civil society.

What of their measurement?

When it comes to measurement of the political contribution of nonprofit organisations the ground is a little better tilled than it is for understanding the social contribution of nonprofit organisations. As well as US research referred to, the World Values Survey also touches on such matters, as does comparative work on citizenship and measures of civil society. However, such work is not easily generalisable and does not give rise to comparable measures, except by the comparison of the views of “knowledgeable informants”. The efforts of the global civil society organisation Civicus to develop a civil society index illustrates the possibilities but also the weaknesses of such approaches (Lyons 2009).

There have also been some efforts to tease out the various factors that shape government policies. These mostly are case studies; some try to evaluate the effect of nonprofit advocacy, industry or professional groups in this process. Their findings appear to be heavily influenced by the theoretical approach taken and cannot be reduced to measurable variables.

Once again, it is necessary to note that some nonprofit organisations can also have effects that damage the democratic character of a political system, for example, organising to exclude some voices from being heard. Perhaps, seeking to exclude some interests for example by damaging their legitimacy is part of the vigorous competition of a truly democratic political system. But the use of threats of physical violence is not.

A further proviso should be noted. This discussion has focussed on the various ways different groups of nonprofit organisations contribute to economy, society and a democratic political system. In each case, usually by way of examples, it has been made clear that the remarks apply to particular groups of nonprofits, usually identified by their activity (or industry). But it should also be noted that even within the same field not all nonprofits have the same effects. This has implications for government funding for the provision of certain services. To take a simple example: a large charity may provide a D&A service in a crisp efficient and professional way, in contrast to a self-help organisation made up of ex-addicts. But the latter organisation may produce better outcomes in the longer term. To answer such questions requires a different sort of analysis (eg program evaluation or SROI). Once again this and the following example point to the need to recognise that nonprofits have a variety of

outcomes and impacts that would not be identified by focussing exclusively on their mission or objectives or purpose.

Theda Skocpol (2003) has described how in the US hierarchically organised networks of local democratic associations have been replaced by professional lobbying organisations based in Washington and sustained by professional fundraising campaigns. The latter are effective in their lobbying efforts but fail to provide the grounding in politics that the former provided for many years; with perhaps a consequence fall off in conventional forms of political participation such as voting. The point here is that some nonprofit organisations are better than others at producing some of the contributions attributed to a particular class of nonprofits generally.

PART 5: Thinking about government funding of nonprofit organizations

It is important the Inquiry does not subscribe to the common myth that sometime in the 1990s State and Federal governments moved to outsource lots of services previously provided by public servants to the nonprofit (or nonprofit and for-profit sector). In fact, the only services so outsourced were those previously provided by the CES, and a few child welfare services. The great growth of government payments to nonprofit organisations is the result of massive increases in the demand for services always provided by (or mainly provided by) nonprofits. What changed (and slowly over a decade or two from the mid-1980s) was the language which governments used and the rules which governments set in place to control the services that they subsidised (and occasionally fully funded).

On p13, 2nd paragraph, it is said that as governments have contracted out areas of public service provision, the sector has moved into more traditional public sector roles (for example in employment and training services). This is incorrect in several respects. While it is true that the outsourcing of the CES was very important and enabled a few nonprofits to double in size, most of those nonprofits were already providing employment and training services. More importantly, **the outsourcing of the CES is not an example, but a one-off case.** The many other social assistance services that nonprofits provide with the assistance of government funding were provided by them before government funding was received and certainly before governments invented the formulation that they were purchasing services on behalf of clients. These services were not government services that were outsourced. What changed was that as demand increased so too did government funding and the scope of the services and the size of some of the nonprofit organisations providing those services. What also changed was the way that governments described their funding programs and the rules and procedures that accompanied them. The fiction that these services were once government services is used to justify a whole heap of regulations that would be harder to justify if the history of government funding was known among the people who now run funding programs. A research body like the Productivity Commission should get the story right.

Although the Productivity Commissions terms of reference require it to address the issue of government funding only in the context of “community organisations” it is

arguably important to address the specific focus in the context of all forms of government funding of nonprofit organisations in all fields or industries where it takes place. Ideally governments will soon move to adopt clear and principles for funding private organisations for the provision of facilities and services.

The following section is taken from an unpublished study of government funding of nonprofit organisations, which includes sections (not included here) that reviews previous research and identifies the full range of variables that are involved in any government funding relationship. The section below outlines three models or ideal types of government funding relationship along with their defining characteristics that makes one or other appropriate for a particular government purpose. It suggests that governments seek to identify which model is most appropriate for their purpose and to fashion a minimum set of rules that are appropriate to that type of funding relationship rather than creating a muddle of rules drawn unreflectingly from different models.

Three models of government funding

The long list of variables outlined above makes it clear that each funding program will probably have its own unique mix of these, its own DNA as it were. In order to make a little more sense of the vast range of possibilities, it is helpful to develop a simple typology. A simple set of three “ideal types” widely used in the literature (though not always coherently) is as follows:

- **Grants;**
- **Quasi-market Contracts;**
- **Quasi-vouchers.**

In distinguishing one type from another, it is necessary to identify a single variable that is always present in one (pure) type of transfer and never in either of the other two. The variable should be one that has a powerful influence on the form of relationship between transferor and transferee.

A **grant** is the basic form of transfer. It will be covered by an agreement that the funds granted will be spent on some project or program but there is no expectation that the government making the grant will receive a benefit.

A **quasi-market contract** exists where the government specifies that funds are to be used to provide certain services to certain classes of people. Generally contracts are issued after a competitive tendering process; often the government talks of purchasing certain services. Transfers may be dependent on achieving certain outputs or outcomes. Contracts should be easy to distinguish from grants: in government accounting purchases are treated very differently to grants; in taxation terms, grants are GST free while contracts are subject to the GST. In practice these rules are often not observed.

The third form, the **quasi-voucher**, is distinguished from a grant or quasi market contract by the feature that it is a payment made on behalf of someone receiving the service, to help them pay for the cost of the service. The relationship between the service provider and the government is that of a licensee and licensor. That is the

government licenses providers and determines eligibility of recipients, but the recipients are free to choose from among licensed providers.

Another basic distinction between the three (ideal) types is that each model assumes that the main expertise to lies with a different party in each model. In a **grant**, it is assumed that the grantee (the nonprofit or for-profit organisation) has the expert knowledge of a project or program and initiates the proposal (though the government may have indicated that it was interested in receiving proposals). In a **quasi-market contract**, it is assumed that the government has a high level of expertise in the service to be delivered and that it draws on that to specify the precise type of service required by particular people needing the service. In the **quasi-voucher**, it is assumed that the customer or their carer has sufficient knowledge to recognise that they need a service and to choose the best service provider for them in their particular circumstances. It is also assumed that providers are skilled but also that the government has put in place and maintains an appropriate system for licensing and monitoring providers.

The above has tried to describe ideal types. It is not to deny that at times (mostly) governments will not create hybrids, by mixing characteristics of the different types (eg by overlaying a quasi-market contract on a quasi voucher relationship, or highly specifying a grant). Such arrangements are unnecessarily cumbersome and inefficient.

Under a **grant**, the government funds a nonprofit to assist it to pursue its (ie the nonprofit's) mission. Generally, the government acknowledges that the nonprofit understands the project for which funds are sought and agrees to its account of how funds are to be applied and its specification of outputs or outcomes. The government may seek independent comment on the organisation and its claimed outcomes before funding, but basically acknowledges that it does not have a high degree of knowledge of the services or project to which the funding is to be applied. A grant may have certain conditions attached and may be organised as a contract – that is, in return for funding the recipient agrees to do certain things.

Within the **grants** type there are several sub-models:

Deficit funding. Basically, the government agrees to underwrite the costs of provision of a service, usually after setting the amount that providers can charge users of the service. It was once the basic method for funding nonprofit nursing homes;

Capital grant. Again, this is rarely used now. The government agrees to fund the cost of providing a facility that will be owned by the nonprofit (sometimes with a payback requirement if the facility is sold within a specified time). Interest subsidies in education provide a current example of this type;

R&D grant. The government agrees to fund a nonprofit to develop or trial a new method of service delivery;

Capacity building grant. The government provides a nonprofit or group of nonprofits with limited term funding to build their organisational capacity – eg for staff training or to develop a fundraising program);

Project grant. The government department funds a nonprofit organisation to stage an event or provide a set of services to particular segments of the population for a limited period of time. Usually the objectives and a description of the project are set out in an agreement or a formal contract along with levels of funding and reporting requirements. As there are generally more applications than funds available there decision process is in effect a competitive one.

Operational grant. The government department funds the nonprofit to cover some or all of its costs in delivering certain services. There may be considerable specification of performance to be achieved by the nonprofit and these along with levels and timing of funding and reporting requirements are set out in an agreement which may or may not be described as a contract. Despite high levels of specification of what is to be achieved with the funds transferred, there is no competitive tendering and the specifications will be determined in conversations between government officials and senior staff of the nonprofit organisation. Funding may be described as a grant or as the purchase of a service (even though in national accounting terms these are very different transactions). The funding of Major Performing Arts Organisations appears to be a significant example of this type.

Under the **Quasi-market Contract** type the government funds private organisations to provide certain specified services to specified classes of people, often referred to as providers by government agencies. Governments describe themselves as purchasing services on behalf of certain citizens. The funding is governed by a contract and is awarded after a competitive bidding process. It is these features of government initiation, specification and competition that distinguish a quasi-market contract form of government funding from a grant and from a quasi-voucher. That is, what affects the behaviour of organisations being funded in this way is that they are conscious that while they are being funded to provide (or to assist them provide) a continuous service, what they are to do (or to produce) is specified and that they will have to compete with other entities to obtain that funding and can lose that funding in the next competitive funding round. Generally, governments are unconcerned whether contracted organisations are for-profit or non-profit organisations.

An emerging sub-model of the quasi market contract is the franchise. In this sub-model the funding agency requires that the service is badged as a government service and that the service provider is presented as a franchisee of the government.

Under a **quasi-voucher** type, the government department effectively subsidises specific classes of users, although the provider organisation is the recipient of the funds. It is the method used to fund children's services and nursing homes. It is used where providers charge users a (sometimes specified) fee. Governments generally also require providers to be licensed and in this way impose conditions, governing both physical conditions and staff qualifications designed to ensure a certain level of quality in services provided. Once a provider is licensed, it can accept customers, with or without vouchers until the next licence inspection. In this case the selection of a provider is made by the customer. In most cases (schools are a possible exception), governments are unconcerned whether the provider is a nonprofit or for-profit organisation.

Under what circumstances is each model the most appropriate?

It was suggested above that funding relationships have developed haphazardly within each industry and service field. At no point has a government sought to develop a theory or a philosophy or a framework of nonprofit funding. Below are some notes toward such a framework.

More broadly, it should be acknowledged that these three models/types of government funding of nonprofits (private organisations or third parties) are some of a wider set of what Lester Salamon has called tools of government action (Salamon 1989). In an ideal set of circumstances, a government would choose a particular tool best suited to its purpose. In practice governments are rarely placed in a position where they can choose the most appropriate tool. In the case of our three models, the government has already chosen not to provide a service directly itself. It then remains to choose the best way for expending public funds to achieve the government's purpose.

When grants are most appropriate:

G1. When initiative and knowledge of what is required is acknowledged to lie with the nonprofit, for example:

- When government agrees to assist or enable a nonprofit to purchase land, buildings, plant or equipment.
- When purpose of a government program is to stimulate ideas from the sector (eg for community development), encourage research and development or to assist in organisational capacity building.
- When the government wishes to assist a nonprofit in financial difficulties to continue operating.
- Where the service provided is so specialised that no other alternative organisation could perform it – eg funding a chamber orchestra; a regional art gallery.

G2. When the government funding department also has some knowledge of the service field, but:

- Wishes to develop new program ideas and works with one or several nonprofits to develop these ideas in practice, or
- Wishes to assist one or several specialised nonprofits provide services to a limited number of highly disadvantaged clients with complex needs.

Minimum requirements to be applied by and for government:

Pre-grant - That proposer knows what it is doing (assurance by referees, previous history); that proposed outputs and/or outcomes are specified and can be measured (this might be negotiated by government in advance);

Post-grant - That funds have been spent on project or purpose; report on results achieved or assisted by funding.

Where quasi-vouchers are most appropriate:

- Where services are readily understood by users or their carers;
- Where there are many users of services at least some of whom can and/or do pay the full cost of the service;
- Where there are many existing service providers already distributed in (most) areas of demand/need.

- Where there is already a rudimentary licensing process and understanding among providers and consumers about what constitutes a minimum standard of service good quality.
- Where entitlement to a voucher (of a certain value) can be readily determined (either by an independent (government) body or by provider but readily audited).

Minimum requirements to be applied by and for government:

- Knowledge of cost structures of industry and capacity to pay of potential users (that government wishes to encourage/assist) to help determine value of vouchers;
- Knowledge of minimum features required for a satisfactory provision of service – both physical and staff qualifications. Government may need to consult professional bodies associated with the field.
- Pre-determined reporting requirements to be applied as a condition of continuing licensing. As a bare minimum these should enable the monitoring of service use trends and where appropriate to ensure appropriate level of service is applied. Ideally, service quality should be defined and assured by an appropriate professional body independent of both government and providers. Its focus should be on measuring outcomes, user satisfaction and the close monitoring of adverse incidents. In practice governments may wish to be directly involved in the quality assurance process.

Where quasi-market contracts are most appropriate:

In one sense quasi-market contracts are appropriate when neither grants nor quasi-vouchers are appropriate.

- Where the funding department has high knowledge of the service field and is able to specify reasonable outcomes and processes.
- Where persons needing services are many, but all or most are unable to afford to pay or even contribute to the cost of the service;
- Where neither users of service nor carers are deemed able to judge the appropriate mix or level of service;
- Where many of the persons deemed to need a service are unlikely to seek it of their own accord
- Where the government funding agency has a clear view of the outcomes that it wishes to see obtained and believes it can encourage these by constructing an incentive system of payments.

Minimum requirements to be applied by and for government:

- Ability to clearly specify services required and outcomes sought;
- Evidence-based knowledge of connection between specified services and desired outcomes
- Detailed empirical knowledge of cost structure of providing services (including cost of capital);
- Knowledge of bidders or methods for judging likely ability to deliver services that produce sought outcomes.

Common abuses by governments choosing this method of funding:

- Insist on fixed price tendering and then set prices too low for delivering of program objectives;
- Make most payment dependent on certain outcomes and then fail to provide number of users or change other environmental conditions that make it impossible to achieve that level of outcomes (ie place all risk arising from uncertainty on providers);
- Load conditions on contract that are irrelevant to outcomes (eg that organisations are unable to use any knowledge gained in course of contract to propose better ways of providing care, or that they must employ staff under particular arrangements);
- Load onto contract information requirements that are unnecessary for program monitoring and of little value to either program managers or to managers of service providers;
- Force providers to disguise their identity by using branding on vehicles and premises that refers only to the government department contracting the service (ie use a franchise model);

A note on partnership

Quasi-market contracts are often talked of by government as partnerships. Mostly, they display none of the characteristics of a partnership. Yet the nature of the services is such that a proper partnership relationship would be most appropriate. There is a good deal of empirical literature that indicates that when there is a high degree of uncertainty about relations between inputs and outcomes, and where the specialist practice knowledge is shared by contractor and contracted organisations, then genuine partnerships are needed. Frequent re-tendering and risk avoidance by funder are practices that are anathema to the development of genuine partnerships. A crucial question that should be asked by government auditors is why departments have failed to encourage partnerships with all the benefits and program development efficiencies that they would generate.

The marketing literature on business to business relationships sheds helpful light on when partnerships are more appropriate than a contractual relationship. The literature talks of the difference between contractual and relational governance (of the business to business exchange). It finds that relational governance (called here partnership) is better than contractual governance when there is a high level of uncertainty about outcomes and/or when knowledge assets (as opposed to physical assets) are what are to be deployed (Cannon et al 2000). However, in many cases the two forms complement each other; that is, as relationships between firms become more complex and governance of the relationship becomes more “relational” to reflect this, contracts also become more customised to reflect the unique nature of the particular relationship (Popo and Zenger 2002). Some have suggested that the legal framework developed to enable joint ventures between companies would be the most appropriate model for relationships described here as quasi-market contracts (McGregor-Lowndes and Turnour 2003; McGregor Lowndes 2008).

PART 6: Incidental Remarks

Volunteers

The Issues Paper contains misleading information on volunteers. The error shows the difficulty of obtaining and making sense of data on the nonprofit sector.

The misleading info is in 2nd last para on p7 where it says that the nonprofit sector utilises the services of **2.4 million volunteers**. That figure is drawn from the ABS survey of economically significant nonprofits. Because it was collected from a survey of organisations the real figure would be lower than that as the cited figure is inflated by including people who volunteered for 2 or more organisations and who would be double counted. But more importantly, it excludes many more people who volunteer only for volunteer only nonprofit organisations. These are included in the Satellite Account as the one guide to the contribution of the great majority (ie 95%) of nonprofit organisations. The ABS 2006 Voluntary Work Survey estimates that the number of people volunteering for all kinds of formal organisations was **5.2 million**. That would be the figure most people with an interest in volunteering would have in mind. Again, the true figure would be a little lower than that as the 5.2 million probably includes a few people who volunteer **only** for government organisations or for for-profit organisations. The ABS should be able to estimate that number but a colleague and I found the RADL system so hard to use, that we stopped short at estimating the hours contributed to nonprofits (620 million), government and for profits (another 93 million), rather than the people who contributed those hours. Actually it is hours that is the more important figure as it can be converted to estimates of financial contribution by volunteers to the sector.

Regulation

The Productivity Commission is asked to look at regulatory requirements that fall on “community organisations”. The issue of regulation of nonprofit organisations is best viewed initially at the level of all nonprofit organisations with attention paid to the peculiarities in the regulatory framework for particular groups of nonprofits (such as “community organisations”). The Productivity Commission appears to be prepared to take a wider view, inter alia appending to the Issues paper the recommendations of the recent Senate Economics Committee Report into disclosure regimes for charities and other nonprofit organisations.

The Senate Economics Committee recommended that there be a single national legal structure and regulator for nonprofit organisations. While there is much to be said for a single act and national regulator, there is a suggestion in the Senate Committee Report that this should cover all nonprofit organisations, irrespective of size and extent of interaction with the public. In turn this is likely to lead to a backlash against the proposal from the hundreds of thousands of very small, volunteer only nonprofits. Some of these are currently incorporated but less than happy to be so (Passey and Lyons 2009), others are not incorporated but might fear being asked to do so. In fact a legal model exists in many of the states that comprise the United States that allows small nonprofits to gain the benefits of incorporation without going through the legal process and without the necessity of filing annual reports with the regulator. In the absence of an equivalent to Australian incorporated associations’ legislation these states have adopted model legislation that overrides the way the common law applies to unincorporated associations so as to allow them to hold property, to sue and be sued as an entity and to protect individual members from wrongs done by the

association. This protection is automatic and requires no registration by the association (Hopkins 1992). Such legislative provision would provide protection to members of many small unincorporated associations while allowing many small incorporated associations to allow their incorporation to lapse without losing the basic protections which it bestows. It would reduce an unnecessary regulatory burden on both government and groups of people who have organised as small nonprofit associations.

To the extent that the Productivity Commission defines the “community organisations” in its terms of reference as encompassing small volunteer only organisations that are within and serve their community of place or interest, and seeks to encourage such organisations by lightening the regulatory burden on them without removing important protection to members and committees that currently come with incorporation, it should look carefully at this model.

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