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**“Building From The Bottom Up:  
A Conceptual Framework To Expand The Function Of Nonprofits”**

**BY**

**BRIAN SZKLARCZUK**

**A Thesis  
Presented to the Faculty of Graduate Studies  
in Candidacy for the Degree of**

**MASTER OF PUBLIC ADMINISTRATION**

**Departments of Political Studies/Science  
University of Manitoba/ University of Winnipeg  
Winnipeg, Manitoba**

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**Building From the Bottom Up: A Conceptual Framework to Expand the Function of  
Nonprofits**

**BY**

**Brian Szklarczuk**

**A Thesis/Practicum submitted to the Faculty of Graduate Studies of The University  
of Manitoba in partial fulfillment of the requirements of the degree  
of**

**MASTER OF PUBLIC ADMINISTRATION**

**BRIAN SZKLARCZUK©1999**

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## **Abstract**

**This thesis will examine ways in which nonprofit organizations can better utilize their resources in order to improve their ability to provide service to the community.**

**This thesis will develop a conceptual model integrating classic and contemporary ideas from public administration, management and economics. The importance and potential expansion of the concept of the entrepreneur has been overlooked in available contemporary literature. The literature has applied the concept of the entrepreneur narrowly, simply as a managerial function. This thesis will suggest ways in which broadening the concept of entrepreneur can improve service provision in the nonprofit's uncertain political, economic and social environment.**

**The conceptual model begins by re-evaluating Joseph Schumpeter's entrepreneurship theory and placing it into the context of the contemporary nonprofit organization. Schumpeter's concepts will be re-evaluated in the nonprofit setting and used in conjunction with contemporary work to illustrate ways in which nonprofits can expand their entrepreneurial talent. A central focus on increasing volunteer participation in entrepreneurial functions will form the basis for a series of recommendations.**

## **Acknowledgments**

During the research and writing of this work, there were many who provided much needed support and encouragement. Each deserves special recognition.

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## **Chapter I. Introduction**

**This thesis will suggest ways in which nonprofits can equip themselves for improved mission achievement given the increasingly constricted financial and ideological environment among governments and the private sector. Classical theory from Schumpeter's concept of the circular flow and the entrepreneur will form the basis for a contemporary approach to viewing the capabilities of nonprofits in a new paradigm. The conceptual model presented in this thesis will focus on expanding the role of volunteer participation in nonprofits to include entrepreneurial functions. The concept of the entrepreneur used in this thesis is a synthesis of ideas drawn from Schumpeter's vision of the entrepreneur combined with new insights into the contemporary environment of nonprofit organizations. This understanding of the entrepreneur must not be misinterpreted by the popular notion of the entrepreneur as simply a successful, usually male, business person.**

**In the rapidly changing policy arena, nonprofit organizations must find new ways of achieving mission if they are to succeed in this often hostile environment. New ways of thinking are needed to adapt to this changing environment. Most nonprofits continue to be modeled after a conventional business organization. Over the last century, the fundamental structures of formal nonprofits have changed very little. Unfortunately, there has been little constructive research or writing about how nonprofits may change their organizational structure to accommodate new concepts and operational cultures.**

## **The effects of neo-liberalism, globalization and corporate ideology on nonprofits**

Neo-liberal policy developments in the last decade have reduced nonprofit funding from both government and the private sector. Globalization and corporate ideology have constrained their ability to meet mission. Several factors are responsible for this. Increased global competition among corporations has placed pressure on governments to reduce spending, and lower taxes, in order to encourage private investment. Policy instruments have been removed from government, as capitulation to international competition has undermined national regulations, crown corporations and market controls. The international mobility of capital has limited monetary controls and reduced governments' ability to mediate between social and commercial interests. In response to this pressure, government has sought ways to lower expenses, one of which is to reduce funding to nonprofit organizations.

The prevalence of economic and commercial ideology and propaganda in public discourse has had a negative effect on community and individual perceptions of nonprofit organizations. The shift to a less interventionist government in the late 1980's is a result of this attitude. In public discourse there is a general agreement that the free market is the best way to organize and distribute resources.

These factors coincide with a growing social deficit, which has increased the need for services which can only be provided by nonprofits. Unfortunately, the prevailing attitude is such that it is unlikely that nonprofit funding will improve in the near future.

The necessity for finding new resources and innovative approaches to mission achievement is obvious, but the challenges are formidable. The conceptual framework provided in this thesis seeks ways in which this might be accomplished. Nonprofits must find ways to reduce their resource dependence on government and the private sector. The increasing involvement of volunteers at all organizational levels is one approach to this problem. Promoting entrepreneurship among all staff provides a foundation for the continuous innovation necessary to achieve mission in a constantly changing environment.

### **Orientation of the thesis**

Chapter two will introduce approaches used to define non profit organizations. Other definitions fundamental to the thesis include the concept of the entrepreneur, mission and innovation among others. These will be defined contextually throughout the thesis. The definitions of nonprofit include the ‘legal-structural’, ‘cross national’, ‘negative’ and ‘popular vocabulary’ definitions. Another definition will also be identified, Drucker’s definition of nonprofits as ‘human change agents’. These definitions provide a variety of perspectives that shape our understanding about the function and purpose of nonprofit organizations in society.

In chapter three contemporary literature which identifies the prominent issues and key components of nonprofit study will be reviewed. The literature review will address contributions from economics, management and public administration. Various topics

will be addressed including the concept of altruism and the role of the nonprofit entrepreneur. Contemporary literature focusing on issues facing nonprofits in the Canadian policy environment will also be addressed.

The themes emerging from the literature review will then be critically assessed. The role of the entrepreneur and the need for a nonprofit conceptual framework will be emphasized. A means of broadening the existing discussion will be presented as a conceptual model which fully integrates the concept of the nonprofit entrepreneur. Joseph Schumpeter's 'circular flow' and 'Entrepreneurship Theory' will be briefly introduced.

Chapter four provides an analysis of Schumpeter's Entrepreneurship Theory. Schumpeter's placement of the entrepreneur at the center of all economic activity and his circular flow model will be explained. The concept of production, economic and non-economic subjects, innovations, bankers, capital, credit and interest will be discussed in the context of the circular flow. Following this, an explanation will suggest ways in which Schumpeter's model can be used to describe various aspects of nonprofit organizations.

In chapter five a conceptual model which applies Schumpeter's business cycle and entrepreneurship theory to the contemporary nonprofit environment will be developed. A conceptual framework will be established based on the concept of the circular flow applied to the nonprofit setting.

Key aspects of the Schumpeterian model that can be used to enhance nonprofit organizations such as the expansion of the function and understanding of the

entrepreneur will be identified. The benefits of expanding the function of the entrepreneur to include many persons in nonprofit organizations, including volunteers, will be assessed. Recommendations for expanding entrepreneurial roles in nonprofit organization will be outlined.

Chapter six will summarize the findings regarding the circular flow and volunteer entrepreneur brought forth in the thesis. This chapter will discuss the relevance and practicality of these concepts to all nonprofits, regardless of economic, political or social context. The concept of the circular flow can be used as a tool to assess the impact of service delivery and volunteer participation. This assessment may illustrate the need for an increased role of volunteers. This requires a shift in management style away from control of resources, to a management style which coordinates the activities of persons within the nonprofit. The chapter will outline the areas that require greater research. A broad, global based analysis is needed to verify the concept of the circular flow and to compare the tempo at which mission is achieved in formal and informal nonprofits in developed countries and developing countries as well. This undertaking can serve to link the financial and human resources of nonprofits in a global network to raise awareness and serve the global mission in a fuller manner.

## **Chapter II. Defining the nonprofit**

This chapter will introduce the approaches used to define nonprofit organizations. The characteristics of the ‘legal-structural’, ‘cross national’, ‘negative’ and ‘popular vocabulary’ definitions will be identified. Each definition will be compared and evaluated. While these definitions are useful for describing the structural content of nonprofits, they provide limited insight into the broad purpose and role that nonprofits play. The following discussion of Drucker’s definition of nonprofits as ‘human change agents’ should raise important questions about the function and purpose of nonprofit organizations in society. Other terms such as mission, entrepreneur and innovation, and volunteer will be explained contextually throughout the thesis.

### **Legal Structural Definitions**

The legal structural definition is essentially regulatory. Tax regulations are used to distinguish nonprofit organizations from other types of organizations. This approach has its origins in the taxation regulations of the United States Internal Revenue Service Federal Tax Code and the Revenue Canada Income Tax Act. These regulatory regimes have been put in place to help identify organizations as nonprofits. Organizations which meet established criteria obtain certain privileges.

Organizations considered to be non profit, in the United States, fall under tax codes 501 (c) and 501 (c) (4) which states that organizations are able to gain tax



exemptions “... which are educational, scientific, religious, charitable organizations, private foundations, corporations and community organizations, civic and social welfare organizations.”<sup>1</sup> The United States Federal Taxation code identifies areas of service that are socially progressive. These include arts and culture, community development, social services, religion, education and research and health care.<sup>2</sup>

In Canada, the legal structural definition identifies the characteristics of nonprofit organizations as those which are dedicated to “the relief of poverty, and the advancement of religion, education, and other purposes beneficial to the community as a whole.”<sup>3</sup>

The Canadian and United States legal structural regimes primarily identify and characterize nonprofits by their inability to distribute earnings. You will note the opposite characterizes private ‘for-profit’ corporations. This interpretation is illustrated in Hansmann’s work, where non profits are characterized as organizations “barred from distributing its earnings with members, officials, directors and trustees.”<sup>4</sup> Lames and Rose-Ackermans provide a similar example, with nonprofit organizations characterized

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<sup>1</sup> David L.Gies, Steven J. Ott, Jay M. Shafritz, eds. *The nonprofit Organization: Essential Readings* (California: Brooks/Cole Publishing Company, 1990) , 41.

<sup>2</sup> Ibid.

<sup>3</sup> John Shields and B.Mitchell Evans, “*Shrinking the State: Globalization and Public Administration “Reform”* (Halifax: Fernwood Publishing, 1998) , 90.

<sup>4</sup> Harry B.Hansmann, “The Role of Nonprofit Enterprise” *The Yale Law Journal*, (April 1980) ,838; quoted in James T Bennett and James T. DiLorenzo, *Unfair Competition: The Profits of Nonprofits* (New York: Hamilton Press, 1989) , 11. and James C. Crimmins and Marky Keil, *Enterprise in the NonProfit Sector* (Washington, D.C: Partners for Liveable Places, 1983 ) , 15.

as “ private organizations that are prohibited from distributing a monetary residual.”<sup>5</sup>

There are several ways to describe the differences between the legal structural definitions in Canada and the United States. Quarter’s formality-informality continuum is one approach. <sup>6</sup> This continuum suggests an effective means of conceptualizing the difference between the formal registered and other nonprofits. Canadian nonprofits essentially operate within a formal three tiered system. The most formally limited tier, the registered charity, possesses charitable status with Revenue Canada. Registered Charities have greater limitations on resource allocation. The second category of nonprofits are incorporated within a province or territory, but do not possess charitable status. These organizations are not able to offer the same monetary incentive to potential donors, however, they are not restricted by the regulations imposed on registered charities. The third tier is the least formally limited of the three. It consists of many unregistered organizations that carry out activities within the character of nonprofits. The size and scope of this third category is the least understood.

In the U.S. nonprofit sector, there is a similar pattern of formal limitation; however, the three tiers which characterize the Canadian experience are compressed into two. Organizations which qualify under the regulations of the Internal Revenue Code are granted charitable status and regulated in a similar manner as Canadian registered

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<sup>5</sup> James Estelle and Susan Rose-Ackerman, *The Nonprofit Enterprise in Market Economies*, vol.9, *Fundamentals of Pure and Applied Economics* (London: Harwood Academic Publishers, 1986) , 4.

<sup>6</sup> Jack Quarter, *Canada’s Social Economy: Co-operatives, Non-profits, and Other Community Enterprises*. (Toronto: James Lorimer & Company, 1992) , 41-62.

charities. The other nonprofits operate at two levels, either within the mainstream economy by participating in activities similar to registered charities or outside the formal, mainstream nonprofit sector, in ad hoc informal arrangements.

The legal structural regulations within the nonprofit sectors in Canada and the United States are similar. The tax regulations in both Canada and the United States do not specifically define a charity or what is charitable. This lack of specificity in definition results in a degree of ambiguity.<sup>7</sup> In Canada, for example, the term 'other purposes beneficial to the community as a whole', leaves one to ask many questions. Who defines whether or not the nonprofit is beneficial to the community? Do interpretations shift with time? These are all questions which are not often asked and for which there are few answers.

Nonprofits in Canada and the United States have the ability to offer tax receipts. It is argued that this practice creates demands that would not otherwise exist. These demands are not mirrored in any of the market tax structures. More importantly, organizations and participants in both countries have the ability and freedom to apply for nonprofit status. If organizations are not accorded charitable status, their ability to act within the character of nonprofits will not be reasonably compromised by the state. Individuals and organizations who participate in nonprofit type activities will not be coerced or pressured by the state, if their activities are inside the scope of the formal legal structural definition. The provisions of liberal democratic freedoms allow

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<sup>7</sup> Douglas Campbell, *The voluntary non profit sector: An Alternative*. Discussion Paper No. 93-13, Government and Competitiveness ( School of Policy Studies: Queen's University, 1993).

individuals the right to act in an altruistic manner.

The legal-structural is limited as an approach. It is essentially an “artificial construction resulting from the political process of federal taxation.”<sup>8</sup> The next section of this paper will discuss more general cross national definitions. This discussion will generally highlight the different notions of nonprofits.

### **Cross National Definitions**

Developing operational definitions that are consistent across national boundaries is one of the greatest challenges facing international nonprofit analysis. Salomon refers to the problem within the current international study of nonprofits as ‘suffering from a conceptual confusion’, with national definitions that refer to different concepts and institutions.<sup>9</sup> The difficulties of developing functional cross national definitions becomes apparent when considering British, North American, European, Latin American and Japanese non profit sectors.

In France, for example, the term ‘economie sociaux’, or social economy, is used. This term refers to institutions which in theory, work towards a common goal of social

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<sup>8</sup> James T.Bennett and Thomas J. DiLorenzo, *Unfair Competition: The Profits of Nonprofits* (New York: Hamilton Press, 1989) , 13.

<sup>9</sup> Lester M.Salomon and Helmut K.Anheier, *The Emerging Nonprofit Sector: An Overview*. Johns Hopkins Nonprofit Sector Series 1 (Manchester: Manchester University Press, 1996) , 3.

transformation.<sup>10</sup> In reality, critics such as Quarter suggests this is not the case. He suggests the nonprofit sector does not have equal standing with the market and the state. Rather, the latter two institutions dominate the nonprofit sector. The nonprofit organizations within this 'third institution', do not share a common goal of social transformation, but rather, focus on providing services. The focus on services is a short term goal, as the service providers are reliant on the resources available to them. Social transformation in comparison, not only includes service provision but also advocacy and active citizenship.

The term which describes the Latin American/African situation, Non Governmental Organization (NGO's), suggests an organization operating at arms length from government. However, outside of the Latin American/African context NGO is used to describe religious orders, churches, nonprofits groups and others.<sup>11</sup> Because the term is applied broadly, it is difficult to establish its meaningful parameters.

Comparatively, the Japanese 'koeki hojin' has the most unique arrangement. Organizations which seek nonprofit status must demonstrate a substantial asset base, resulting in a nonprofit sector consisting of large corporations with substantial assets. Unlike some countries which have a nonprofit sector comprised of small, medium and

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<sup>10</sup> The critique provided by Quarter (1992) examines the North American social economy in particular, however, his discussion of the term is appropriate for the discussion of the *economie sociale* in France.

<sup>11</sup> Jeanne Wolfe and William Jay, "The Revolving Door: Third Sector Organizations and the Homelessness," in *Housing the Homeless and Poor: new Partnerships among the Private, Public, and Third Sectors* eds. George Fallis and Alex Murray (Toronto: University of Toronto Press., 1990).

large organizations, the Japanese have a sector which is small in number. The Japanese approach is unique because nonprofits in other areas, such as North America, have to demonstrate a relation to a socially desirable activity. The Japanese, appear to be overly reliant on financial assets, rather than societal benefits.

Salomon provides one solution to deal with this cross national dilemma. He suggests that a workable cross national definition should group organizations which “....are formally constituted, separate from government, nonprofit seeking, self governing, and voluntary to some degree.”<sup>12</sup> Even with this clarification, it is still very difficult to compare nonprofits cross nationally. Nonprofits are difficult to define in the context of what they are, hence they have traditionally been defined by what they are not, negative definitions. A discussion of negative definitions will follow.

### **Negative Definitions**

Since nonprofits have traditionally been defined by what they are not, it is important to discuss the concept of the ‘negative definition’. First, it should be stressed that other institutions, namely the market and state, are described by what they are, and rarely described by what they are not. Secondly, although negative definitions may seem to simplify the complex business of classifying nonprofits, in fact they complicate the task.

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<sup>12</sup> Lester M. Salomon and Helmut K. Anheier, *The Emerging Nonprofit sector: An Overview*. Johns Hopkins Nonprofit Sector Series 1 (Manchester: Manchester University Press, 1996), xvii.

Traditionally, the market has been defined as an institution comprised of actors with varying degrees of monetary power. The level of power and influence of these market actors is used as a measurement tool. However, when attempts are made to define the nonprofit sector, the positive definitions based on activities which accurately reflect the market and state are transformed into negative definitions. One example of this approach is provided by Anthony and Young who define a nonprofit as “an organization whose goal is something other than earning a profit for its owners....”<sup>13</sup>

The negative definition is a popular means of describing nonprofits. But as critics, such as Drucker illustrate, the negative definition is very misleading. For Drucker, “it only makes a difference for the tax collector that a hospital, for example, is nonprofit or for profit.”<sup>14</sup> Further to this, he adds, it is difficult if not impossible, to define something by what it is not. The popular usage of the term nonprofit provides another way to define the nonprofit. A discussion of the ‘definitions derived from popular usage’ will follow.

### **Definitions derived from popular usage**

Many of the works in the body of nonprofit literature provide a reference to popular understandings of nonprofits which are found in numerous sources, namely

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<sup>13</sup> Robert N. Anthony and David W. Young, “Characteristics of Nonprofit Organizations” in *The Nonprofit Organization: Essential Readings* eds. David L. Gies J. Steven Ott and Jay M. Shafritz (California: Brooks/Cole Publishing Company, 1990) , 216.

<sup>14</sup> Peter F. Drucker. *The New Realities* (New York: Harper & Row, 1989) , 198.

dictionaries. These definitions support an argument for, or against the existence of the term non profit. However, this approach is used inconsistently. There is a great deal of discontinuity and disagreement among contributors.

Anthony and Young, after a careful analysis of numerous dictionaries and reference sources, are unable to find a listing for the term 'not for profit'.<sup>15</sup> They recognize that the interpretation of the terms not for profit and nonprofit vary within the United States. However, in the existing literature, these terms are used interchangeably to describe the same type of organizations. There are numerous examples that demonstrate a lack of agreement of the term nonprofit within our vocabulary.<sup>16</sup>

### **Conclusion: Drucker's 'human change agent'**

There are a number of ways to define or conceptualize the nonprofit. Although they provide insight into our understanding, each of the definitions has inadequacies and limitations. Most importantly, they do not address the main purpose and function of nonprofit organizations. A better definition is provided by Drucker, who defines these organizations as "human change agents."<sup>17</sup> This definition looks at organizations, not

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<sup>15</sup> The sources include Black's Law Dictionary, Kohler's Dictionary for Accountants, Websters Dictionary, Funk and Wagnalls, and the American Heritage Dictionary. Robert N. Anthony and David W. Young, "Characteristics of Nonprofit Organizations" in *The Nonprofit Organization: Essential Readings* eds. David L.Gies J.Steven Ott and Jay M. Shafritz (California: Brooks/Cole Publishing Company, 1990) , 216-235.

<sup>16</sup> McLaughlin (1986) pre dates the work of Anthony and Young (1988).

<sup>17</sup> Peter F. Drucker, *The New Realities* (New York: Harper & Row, 1989) , 198.



in terms of their structural content, but rather, their purpose. It focuses on the human impact these organizations have on individuals and on society in general. Unlike other definitions, Drucker's reinforces the ideals on which nonprofits are based, and focuses on the actions of these organizations. His definition poses the question, What is the purpose for the existence of these organizations? The answer, "to change the human condition", refocuses our understanding so we can begin to see the outcomes and results of nonprofits as a primary characteristic of them.

Although Drucker's definition is comprehensive, it poses difficulties when distinguishing which entities fit into a nonprofit model from those which do not. For example, there is a social entity that meets the criteria of Drucker's definition, yet is rarely referred to as a nonprofit. This social entity is a human change agent, existing somewhere between the market and the state. There are legal regulations which govern them, and they have regional differences. The one unique feature which separates this entity from most nonprofits is that it is defined by what it is, rather than by what it is not.

The entity in question is a family; an institution not commonly associated with a contemporary definition of a nonprofit organization. The 'family' fits Drucker's interpretation, but raises doubts about the utility of this approach. This example illustrates how the concept of human change agents can be applied to many different aspects of society, many of which are not considered nonprofit organizations.

### **Chapter III. Literature Review**

This chapter consists of two parts. The first part is a review of contemporary literature that provides the reader with a discussion of the key components of nonprofit study as well as the prominent issues. These issues are addressed from a variety of different perspectives including economics, management and public administration. In the second part of this chapter, I will identify and critically assess the themes emerging from this literature.

#### **Part One: A Review of Contemporary Literature**

The review of contemporary literature will begin with the concept of altruism. Following thereafter is a discussion of the entrepreneur in relation to nonprofit organizations. A discussion of economic and historical perspectives will follow. Selected management theory will be discussed, focusing on Drucker's contributions. The later sections of the literature review will examine contributions from public administration. This body of literature provides a contemporary account of nonprofit relationships with government and the market. These works also illustrate the role that nonprofits play within the broader policy framework of the Canadian state.

In the article, *What is Altruism*, Wolfe looks at concept of altruism as it relates to

nonprofits.<sup>18</sup> Altruism is a term used to describe how and why people act to help others.

He stresses that no single theory will explain human behavior, but rather, theory must be flexible enough to recognize the complexity of its objectives. Explanation is best achieved through the development of a pluralistic model that allows social scientists to use many different tools, techniques and methods to further their understanding of how people act.

In his introduction, Wolfe identifies a lack of cohesiveness within the study of altruism. Literature on altruism has come from many different fields of inquiry, resulting in confusion about its source and meaning.

### **Altruism**

The author assesses three approaches used by social scientists to explain altruism. The first, behavioral altruism comes from the field of psychology. Altruism is understood as a 'genetic switch', and as a product of pre or unconscious behavior. Wolfe notes that psychologists are moving away from this type of explanation for individual behavior, yet this approach dominates social science analysis. Wolfe suggests that social scientists should move beyond this approach in order to broaden their analytical perspective.

Motivational altruism is the second approach. It approaches the study of altruism

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<sup>18</sup> Alan Wolfe, "What is Altruism" in *Private Action and the Public Good* eds. Walter W. Powell, and Elisabeth S. Clemens (New Haven: Yale University Press, 1998) , 36-46.

from an individualistic standpoint, reducing all actions to emotional appeal. Here, a clear distinction separates the private and public realms, however, as Wolfe notes, this clear distinction does not always exist.

The third approach, environmental altruism, uses the natural or ecological environment to explain altruism. As Wolfe notes, this approach is a polar opposite of behavioral altruism's 'genetic switch'. This approach concentrates on culture and social institutions. Altruism is viewed as a variable which is activated at certain times. However, as Wolfe notes, this approach relies on a narrow set of assumptions.

Another perspective on altruism is found in Ackerman's *Altruism, Ideological Entrepreneurs and the Nonprofit Firm*.<sup>19</sup> In this work, Ackerman presents a theoretical explanation for the existence of charitable giving and nonprofit firms in mixed economies.

### Utility Functions

In explaining why people give to charitable organizations, Ackerman emphasizes the importance of an economic concept, utility functions. Just as there are countless individual utility functions, there are various reasons why people give money to charities. Ackerman briefly discusses some of them. She suggests 'the act of giving itself' is one reason. People value their own acts of charity and get a 'warm glow' from

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<sup>19</sup> Susan Rose-Ackerman, "Altruism, ideological entrepreneurs and the non-profit firm," *Voluntas* 8, no.2 (1997) : 121-134.

their marginal contribution. Inter generational values are another explanation for charitable giving.

Subsequently, the author looks at why people give to nonprofits and not to for-profit organizations. In private firms, gifts can be used for profit seeking ventures. In the nonprofit firm, this activity is illegal and donations must be used for non-residual purposes. This gives people confidence that donations to nonprofits will be used for their intended purpose.

### **Entrepreneur and Entrepreneurship Theory**

Ackerman seeks to answer why nonprofits exist in mixed economies. She believes the answer to this is found in the ideological commitment of the nonprofit entrepreneur, the ideologue. Ackerman's discussion of the ideologue begins a new section in this literature review which focuses on how the entrepreneur and entrepreneurship theory relate to nonprofit organizations.

Ackerman defines the ideologue as a person who has "...strong beliefs about the proper way to provide a particular service. He or she espouses an educational philosophy, holds religious beliefs that imply certain forms of service delivery, or subscribes to a particular aesthetic or psychological theory."<sup>20</sup>

Organizations run by an ideologue have two advantages in a competitive, mixed economy. They are quality control and product differentiation. Quality control is the

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<sup>20</sup> Ibid., 125-126.

quality of product produced by the organization and made available to the consumer. A firm run by an ideologue will hire individuals with similar views. By doing this, the ideologue is able to ensure that the end result will meet certain quality standards.

Nonprofit firms also have the benefit of product differentiation. Because of their nonprofit status, consumers tend to have more confidence in the entrepreneur, believing they provide a better service than a for-profit firm. Ackerman compares nonprofit and for-profit nursing homes, day cares and hospitals to support this assertion. The results suggest that nonprofits have a higher overall customer satisfaction rating. However, Ackerman notes that this increased service often comes at a higher cost to the nonprofit firm, whereas the for-profit firm has the advantage of producing less expensive services.

The ideological character of nonprofit firms enables them to attract money and customers. The entrepreneur plays a paramount role, as their beliefs, vision and commitment to a goal “can in some cases be a guarantee of high quality to ordinary consumers.”<sup>21</sup> This ideological component aids in attracting money and customers, two vital factors to an organization’s purpose and existence.

As Ackerman’s work suggests, the entrepreneur plays an important role in nonprofit organizations. To better understand what this concept is and how it relates to nonprofits, Badelt’s work, *Entrepreneurial theories of the non-profit sector*, provides useful insight.<sup>22</sup> Christopher Badelt prepares a synopsis of entrepreneurship theory in

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<sup>21</sup> Ibid., 130.

<sup>22</sup> Christopher Badelt, “Entrepreneurship theories of the non-profit sector,” *Voluntas* 8, no.2 (1997) : 162-178.

relation to the non profit sector. Badelt begins by reviewing some of the principles and features of entrepreneurship theory, then applies them to nonprofits. His analysis examines entrepreneurship theory as a supply side behavior, concentrating on what motivates entrepreneurs and managers in nonprofit firms. This is accomplished by examining the differences in production efficiency with government and private institutions.

His analysis begins with a review of the basic principles of Schumpeter's work. In Schumpeter's classic work, *The Theory of Economic Development*, the entrepreneur is the person whose function is to carry out new combinations in the production process and possesses a specific attitude towards change. Badelt emphasizes that the entrepreneur is not necessarily the owner of an enterprise, or an independent businessmen, both of which are often referred to as entrepreneurs. Badelt goes on to identify the key elements of this conceptual framework. However, Schumpeter's theory will be critically examined in later chapters, thus, only the main findings of Badelt's analysis will be discussed below.

Badelt's analysis contends that entrepreneur actions may not be sufficient to explain activities in a firm because many production activities are outside the control of the entrepreneur. For example, an organization may be confined by limited resources which the entrepreneur does not have control over. In his discussion of the four factors of production, land, labor, capital and entrepreneurial talent, Badelt identifies one aspect that is utilized by nonprofits more than any other institution, volunteer labor. For Badelt, volunteer labor is part of the production process. It is manipulated in conjunction with

land and capital by the entrepreneur, who is the paid staff member. The entrepreneur arranges the production factors in such a way that best responds to changing demands. This is an important point that will be discussed in greater detail later in this thesis.

Badelt views entrepreneur theory not as a means to explain behavior, but as an instrument to understand and change the perception of nonprofit organizations. Badelt stresses that entrepreneur theory has the ability to change the image, the understanding, and the assumptions of non profits. By using this theoretical approach, the knowledge base of nonprofits can be expanded and the perception of the nonprofit sector can be enhanced. This is well stated by Badelt, who suggests that “Entrepreneur theory is an instrument to increase the self-consciousness of non profit organizations. The term ‘entrepreneur’ has a positive connotation; when non-profit managers are drawn as ‘entrepreneurs’, they are no longer second-class managers”.<sup>23</sup> This issue will be examined in a more substantial manner later in conjunction with a discussion of the role of the volunteer.

In Badelt’s work, he makes reference to Young’s *If Not for Profit, for What?* one of the first to develop a nonprofit entrepreneurship framework.<sup>24</sup> Young’s framework of entrepreneurship seeks to explain the behavior of entrepreneurs in nonprofit firms. In these firms, the entrepreneur is given substantial discretionary movement by the nonprofit organization. In Young’s analysis, the voluntary sectors existence and growth is

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<sup>23</sup> Ibid., 173-174.

<sup>24</sup> Dennis Young, *If Not for Profit, for What?* ( Lexington: D.C. Heath and Company, 1982).



partially explained by the actions of nonprofit entrepreneurs. Entrepreneurial behavior is attributed to a combination of different motivations that may include idealism, emotional attachment and intellectual purpose. In addition, Young stresses that entrepreneurial behavior does not fully explain the performance and behavior of nonprofit organizations. Other external factors such as social policy also play a substantial role in determining performance and behavior.

One of the most important ideas presented by Young is that "the nonprofit has a residual character and is able to accommodate a range of entrepreneurial motivations that may clash with the more well-defined accountability and survival rules of the commercial and governmental sectors of the economy."<sup>25</sup> Ideological differences also have a significant influence on the perception of nonprofit entrepreneurs.

Another useful economic perspective is provided by Wiesbrod. His work has been a significant influence in shaping nonprofit theory and discourse. His article, *Toward a Theory of The Voluntary Non-profit Sector in a Three-Sector Economy*, is a cornerstone in the economic nonprofit literature.<sup>26</sup> In brief, his market government theory suggests that nonprofits develop only after the government and the market have failed to provide services. Government provides services at the level of the median voter, with the nonprofit organization responding to the demand left unfulfilled by government.<sup>27</sup> One

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<sup>25</sup> Ibid., 163.

<sup>26</sup> Bruce M. Kigma, "Public good theories of the non-profit sector: Weisbrod revised," *Voluntas* 8, no. 2 (1997) : 135-148.

<sup>27</sup> As Kigma notes, this theory has gained wide acceptance and recognition within the economic literature, with over 100 citations in various economic journals.

of Weisbrod's most recent works, his 1998 contribution is titled *Institution Form and Organizational Behavior*.<sup>28</sup>

Weisbrod looks at the issue of organizational efficiency. It is an attempt to determine whether for profit or nonprofit firms are able to attain goals more effectively. Weisbrod notes that literature on this subject is weak because similarities and differences between nonprofit and private firms are often assessed in a simplistic, over generalized manner. His analysis aims to broaden this discussion, by assessing and testing the assumptions used to describe behavior in both types of firms.

The analysis begins by defining institutional form, which consists of the "goals or objective function and the set of constraints it (the firm) faces for achieving its goals."<sup>29</sup> Subsequently, Weisbrod identifies and discusses the constraints that nonprofits face. One of them is the nondistributional constraint. This constraint describes the limitations nonprofit firms face because they cannot distribute earnings to its shareholders or owners. The consequence of this constraint is that managers do not perform as efficiently in nonprofits as they do in for-profit firms, because they lack the motivation and incentives associated with self interest. Weisbrod cautions the importance of this constraint has been exaggerated. He notes that non profit and private firms behave differently because their objectives differ. Without this constraint there would still be differences, resulting from the legal-structural provisions of nonprofit

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<sup>28</sup> Burton A. Weisbrod, "Institutional Form and Organizational Behavior" in *Private Action and the Public Good* eds. Walter W. Powell, and Elisabeth S. Clemens (New Haven: Yale University Press, 1998) , 69-84.

<sup>29</sup> Ibid., 74.

status. In economic terms, these would be considered to be part of production factors used by the firm. For example, the formal nonprofit firm has lower mail rates and reduced property taxes, both of which affect their use of production factors. As a result, nonprofits substitute factors of production for those with lower input prices, for example, substituting labor for land or capital.

Weisbrod illustrates that other differences have also been overlooked as a result of the focus on the nondistributional constraint. Supply prices are one example. The supply price of labor may be lower for nonprofits who are able to use volunteer labor. As well, the nonprofit may face greater demand for its services, explained in part, by customers' preferences and perceptions of the nonprofit and the environment in which it supplies service.

Weisbrod provides an economic explanation for the differences between private and nonprofit firms. Private firms referred to as the 'profit maximizer', concentrate solely on maximizing self interest. Behavior and decisions made by private, for-profit firms are oriented around the primary objective of profit maximization and managerial income. Nonprofits, which Weisbrod labels as the 'bonoficer', have dual goals, profit maximization and the provision of socially desirable goods and services. This second goal sets it apart from the for-profit as its social mission sets it apart in the economic environment. Weisbrod is careful to point out that not all non profits are bonoficers, with some organizations being structured as nonprofits, yet oriented towards the single goal of profit maximization.

Bonoficers engage in activities that have external social benefits and lower

external costs. The activities and products or services they supply have greater added value for the demander, yet are priced at a level close to their productions costs. This suggests that nonprofits have a greater focus on outcomes, rather than concentrating on empire building or wealth building.

To see the difference in bonificer and profit maximizer behavior, Weisbrod identifies four measures and tests them in for-profit and nonprofit care homes. The four measures are efficiency, labor input utilization, customer satisfaction and distribution of output.

The results of the first measure, efficiency, are inconclusive. Weisbrod cautions that a comparison of production costs between two institutional forms may involve very different inputs. Thus, comparing efficiency is a difficult task.

Results of the second measure, labor input utilization rate, suggest that nonprofits have a different rate than for-profits. Nonprofits use more professional oriented staff, such as nurses. Generally speaking, this type of labor is oriented towards service provision. Since level of service is an outcome, we can say that nonprofits use more 'outcome based' labor.

Important distinctions between the for-profit and nonprofit occurred in the third measure, customer satisfaction ratings. Users of the nonprofit care home gave a higher consumer satisfaction rating, but as Weisbrod suggests the difference is not "quantitatively enormous."<sup>30</sup>

In the fourth measure, distribution of output, Weisbrod measures the 'price cost

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<sup>30</sup> Ibid., 80.

margin', the difference between the cost of the service and the price charged to the demander of the service. The evidence suggests that nonprofits have lower price cost differences, implying they sell their products at or near the production costs of that service. One difference between for-profits and nonprofits is the use of non price rationing mechanisms. The use of this mechanism enables the nonprofit firm to manipulate demand to match the supply of a good or service. Examples of this are waiting lists. Church run nonprofits have the longest waiting lists, other nonprofits have shorter waiting lists and the for-profit care homes have the shortest waiting lists, if they have them at all.

Through his analysis Weisbrod identifies two useful recommendations for future research. First, he stresses that competition reduces behavioral differences between nonprofit and for-profits. Actions of each are more pronounced in monopolistic competition. Secondly, Weisbrod states that one must be careful to control for many variables as this reduces the probability of an effect being a result of unforeseen variables.

In his second recommendation, Weisbrod incorporates the discussion of the entrepreneur. He suggests that research in this field should concentrate on trying to answer what determines the supply of nonprofit entrepreneurs given the many different goals that exist. These goals include altruistic aspirations, public service, and charitable goals. Once the organizational goals of non profits are better understood, he states, only then can private firm assumptions be brought into the nonprofit context. This second recommendation has great importance for this thesis and will be revisited.

### Third Sector

This literature review will move from economics to a review of the historical role of nonprofits, the third sector, in the United States. Two articles by Peter Dobkin Hall will be reviewed.

In the article, *The Managerial Revolution, the institutional infrastructure, and the problem of human capital*, Hall criticizes an argument presented by Chandler that asserts for-profit managers have been the key to the growth and success of the American economy.<sup>31</sup> Chandler argued that for-profit managers have been responsible for the success of the American economy. In support of this assertion, Chandler points to the for-profit creation of the multi unit business enterprise, the facilitation of technological innovation, the increase in production speeds and the expansion of markets.

In response, Hall argues the American economic success can only be properly understood and explained through the existence of three institutions, the for-profit, nonprofit and government. Hall argues the American business experience cannot account for the success of democratic capitalism alone. Rather, one must consider the interrelationship between the nonprofit, the state and the market, to explain the success of democratic capitalism. The third sector, Hall argues, has played a pivotal role in the political process, in addition to providing public needs and taking the place of government when required. Hall stresses that comparative analysis of this type must not

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<sup>31</sup> Peter Dobkin Hall, "The Managerial revolution, the institutional infrastructure, and the problem of human capital," *Voluntas* 7, no. 1 (1996) : 3-16.

only consider market actors but also acknowledge the role of the third sector.

A later article by Hall, *A Historic Overview of the Private Nonprofit Sector*, provides detailed insight into the involvement of nonprofit organizations in American history from the 18<sup>th</sup> century to the present.<sup>32</sup> In his analysis, Hall illustrates the dominant themes in American nonprofit history and identifies specific instances in which nonprofits have been interpreted inaccurately.

Hall's historical analysis begins with two contentions about the history of the nonprofit sector. The first maintains that nonprofits are products of capitalism and democracy, the second suggests that throughout the American experience, the state and private sector have played an integral role in shaping the third sector, as it is known today.

The body of his analysis begins by assessing the pre 1780 period of American society and its involvement with voluntary organizations. In this period, the nonprofit had not yet been formally defined, yet quasi voluntary organizations did exist. However, the underlying motives for the existence of these organizations were very different from today. Hall states the 'family' as the most common form of a nonprofit institution in this period. The 'family' acted as a public institution, with responsibilities for education, economic production and social welfare. In his analysis of this period, Hall stresses that these voluntary organizations, superficially resemble contemporary nonprofits. However, the responsibilities of the family were imposed through coercive means.

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<sup>32</sup> Peter Dobkin Hall, "Historical Perspectives on Nonprofit Organizations" in *The Jossey-Bass Handbook of Nonprofit Leadership and Management* ed. Robert D. Herman (San Francisco: Jossey-Bass Publishers, 1994) , 3- 43.

The American revolution is described as a watershed in the history of American voluntary organizations. Hall suggests that the emergence of new ideas of organization and ideology provided the “political, economic and legal conditions favorable to the development of voluntary associations and private philanthropy.”<sup>33</sup> The dislocations of war encouraged altruistic behavior because of the increased need for charity. However, Hall cautions, many were skeptical and fearful of these new organizations. Pervasiveness, scepticism and fear is a recurring theme throughout his historical analysis.

The period between 1865 and 1920 is referred to as “The Non Profit Sector and the Search For Order.” Three important developments come out of the this period. They are the growth of the political party, the writings of Tocqueville and the introduction of legal structure to nonprofit organizations.

Political parties were quasi-voluntary organization, based on limited suffrage. The political party provided a means for those who became disenchanted with politics and the dominant ideology of the day to have a “...counter force to the electorate power of the democratic majority.”<sup>34</sup>

de Tocqueville's, *Democracy in America* is central to the study of nonprofit, or voluntary organizations. This literature review, may in fact, under represent the important contribution that de Tocqueville has made. However, it is difficult to illustrate de Tocqueville's contemporary relevance because many works discuss de Tocqueville superficially by providing the “obligatory citation to de Tocqueville in their encomiums

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<sup>33</sup> Ibid., 6.

<sup>34</sup>Ibid., 9.



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In his seminal work, de Tocqueville described American society, illustrating many of its unique features, one being the existence of voluntary organizations. Through his travels, de Tocqueville acknowledged the growing inequality within America and suggested that the 'American' voluntary sector could provide the means for achieving amelioration.

Hall suggests that de Tocqueville over exaggerated the importance of voluntary organizations in American society. He points out that while they were important to political, economic and social life in the north eastern United States, this was not the case for the rest of the west and southern United States. In these areas, the public institution was preferred over voluntary organization. There was suspicion surrounding this new type of organization. Hall points out that voluntary organizations were one mode of collective action, but not the only mechanism used to influence public life during this period. The contribution of de Tocqueville and the critique presented by Hall is an important part of the comparative analysis to follow in later chapters.

During this period, the legal structure of nonprofits began to take shape. Legislation was developed that identified tax exempt organizations which included educational, charitable, benevolent and religious institutions. The latter part of this period gave rise to charitable organizations and eventually to the nonprofit foundation, both of which were funded largely by the private sector. The privileged sector responded

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<sup>35</sup> Thomas Silk, "The Legal Framework of the Nonprofit Sector in the United States" in *The Jossey-Bass Handbook of Nonprofit Leadership and Management* ed. Robert D. Herman (San Francisco: Jossey-Bass Publishers, 1994) , 62.

to the rising levels of inequality that de Tocqueville described. Control of the voluntary sector was situated within the minority of wealthy industrialists and as Hall describes, “a paradigm for the resolution of the nation’s social and economic problems began to take shape.”<sup>36</sup>

Previous literature suggests the welfare state led to the expansion of charitable organizations. However, Hall’s analysis shows that the private sector, led by a few wealthy industrialists started the nonprofit sector, in the early part of the 20<sup>th</sup> century. This was at least thirty years before the expansion of the welfare state.

In Hall’s analysis of the post World War II period in American politics, he identifies a tenuous relationship between government and the third sector. As Hall notes, suspicion surrounding the power of the charitable sector continued to grow, resulting in the formation of various special government committees. These committees were established to investigate the growing power and financial status of nonprofit charities and foundations. The committees’ inquiry did not result in substantial evidence or significant legislative changes.

While the nonprofit sector was developed by the private sector, its major financial supporter in post World War II America was government. In the Reagan and Bush administrations, a prevalent view was held, that the private sector was the prime funder of charitable nonprofits. But Hall’s analysis demonstrates this was not the case. The nonprofit sector continued to be primarily funded by the welfare state and not private

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<sup>36</sup> Peter Dobkin Hall, “Historical Perspectives on Nonprofit Organizations” in *The Jossey-Bass Handbook of Nonprofit Leadership and Management* ed. Robert D. Herman (San Francisco: Jossey-Bass Publishers, 1994) , 17.

business. The dominance of the prevailing attitudes in the Bush and Reagan administrations resulted in a massive reduction in funding to these groups. As a result, Hall notes, the capabilities of nonprofits at large were crippled.

### **Management Theory**

The management theory section of this review will concentrate on the works of Peter Drucker. Although Drucker is often criticized as being a popular writer, even referred to as the ‘guru’s guru’, this characterization is not entirely accurate. Drucker’s impact on management theory and many other fields is substantial. His work has been cited over 2000 times since 1973, with over half of these citations occurring within the last 9 years according to the Social Science Citation Index.

Drucker’s work is much more important than popular commentary suggests. His training in the classical Austrian school of economics, combined with his experience in banking and finance, and his studies in psychology, sociology, organizational theory and classical literature prepared him to be an important synthetic and original contributor. It has enabled him to bring together many fields of discourse in an innovative way which bridges theory and practice. Drucker addresses many of the issues discussed in this thesis as well as other literature in this review. He uses the concept of amelioration to identify the importance of the nonprofit in bridging the increasing levels of social inequality. The relationship between nonprofits and the broader government policy framework is also assessed. The concept of leadership in relation to nonprofits and entrepreneurship theory

is explored. The similarity between altruism and mission becomes evident in his analysis. He also provides insight and suggestions relating to future challenges faced by nonprofit organizations.

In his first two works *The End of Economic Man* and *The Future of Industrial Man*, Drucker first questions what future organizations and society would look like. What types of organizations will exist? What roles will they play? The answer is first explored very broadly, starting with the political system that controls, shapes and regulates society and the organizations within it. He looks at two alternative political models of organizing society, namely capitalism and fascism. His analysis concludes that what society requires is “continuity and the need for innovation and change.”<sup>37</sup> He is in the opinion that this is best achieved through capitalism.

Drucker speculates what the future organization and society will look like under capitalism. He suggests that large businesses will provide the organizational framework for society by providing for economic, emotional and spiritual needs. As the reader will note from the following discussion, these questions were reassessed by Drucker many times, with his answers changing with each iteration.

In *Landmarks of Tomorrow: A Report on the “Post-Modern” World*, Drucker identified four landmarks that shaped society, work and organizations in late 1950's America.<sup>38</sup> These landmarks included a shift in world view from an industrial to an

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<sup>37</sup> As cited in Jack Beatty, *The World According to Peter Drucker* ( New York: Free Press, 1998) , 38.

<sup>38</sup> Peter F. Drucker, *Landmarks of Tomorrow* (New York: Harper and Brothers Publishers, 1957).

information based society, and a new 'perception of order' based upon the concept of innovation and change. The 'education explosion.' Education was another landmark "rapidly becoming a condition for national survival."<sup>39</sup>

The most important factors for the purpose of this literature review is Drucker's analysis of the formation of new organizations that are "transforming work that was previously confined to individual effort. It does not replace the individual by the organization, it makes the individual effective in teamwork."<sup>40</sup> These new organizations included nonprofits as well as for-profits. Drucker was interested in exploring the relationship between work, economic prosperity and social good. His analysis suggests that social good could be attained through the requisite organizational agent, the nonprofit sector.

This resonates in his later 1993 work, *Post Capitalist Society*. Here Drucker articulates the realities of society including the role of government and third sector. His post capitalist society lacks a developed notion of strong citizenship, which has been destroyed by the 'megastate'. He sees the nonprofit sector as the only mechanism capable of revitalizing community bonds.

Drucker's disenchantment with the modern welfare state is evident in this work. He suggests that government should shift from "being a doer and manager in the social sphere... to confine itself to being the policy maker."<sup>41</sup> In place of government, the

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<sup>39</sup> Ibid., 114.

<sup>40</sup> Ibid., 68.

<sup>41</sup> Peter F. Drucker, *Post-Capitalist Society* ( New York: Harper & Row, 1993) , 169.

nonprofit should become the doer, conditional upon them achieving results that legitimize their new role. However, Drucker cautions, exercise of this power is dependent on the political will to change the status quo.

The question of social responsibility of business is also discussed in *Post Capitalist Society*. Drucker dismisses the suggestion that the sole reason for the existence of business is to make profits. Although profit is an underlying motive, business has social responsibilities.

*Managing In A Time Of Great Change* is a collection of essays in which many of these same themes are treated.<sup>42</sup> In this piece, Drucker uses examples of past or current events to illustrate new ways of thinking about the challenges of management.

Drucker outlines the shift from an industrial to a 'knowledge society'. A knowledge society, Drucker suggests, requires a strong government, business, market and third sector. In this knowledge society, the third sector plays a predominant role, thereby ensuring a balance between individual interest and common good.

He explains, in a knowledge based economy, that opportunities for success are greater than in an industrial society. However, with greater opportunities comes increased competition and greater risks of failure. According to Drucker, the nonprofit sector should take care of social tasks in a knowledge society. The modern welfare state has been ineffective, and business has proven unwilling to champion the cause of social progress. In response to his early prediction that large business would provide this social

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<sup>42</sup> Peter F. Drucker, *Managing in a Time of Great Change* (New York: Truman Talley Books/ Plume, 1995).

bond, Drucker admits his goals for business in *Future of Industrial Man* had not been achievable. The answer for Drucker now "... lies outside the employing institution", referring to the third sector. The goal of the third sector is "to create human health....", achieved in part by a membership based relationship and a two way bond linking the organization with the individual in a voluntary manner.<sup>43</sup>

A minor, yet important assertion is made by Drucker in *The New Realities*. He suggests that "the third sector can only flourish on American soil."<sup>44</sup> This is due in part, to the traditions and pluralism of American organizations. Throughout his work, it is apparent that the third sector Drucker speaks of, is based on the American experience.

In *Managing the NonProfit Sector*, Drucker shifts focus to provide tools for managers in the current nonprofit environment.<sup>45</sup> In the introduction to this work, Drucker compares the nonprofit sector to the market and the state by simply comparing the 'product' of each institution. The market supplies a product and sells it. The government, Drucker suggests, produces effective policy. The nonprofit, however, produces something very different, a 'changed human being.' Given the uniqueness of this product, he says, the current range of business tools available to nonprofit managers have failed to address needs regarding 'mission', 'results based performance', 'strategy', 'innovation' and 'volunteer management'. His work seeks to fill this void by providing

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<sup>43</sup> Ibid., 256.

<sup>44</sup> Peter F. Drucker, *The New Realities* ( New York: HarperCollins, 1989) , 205

<sup>45</sup> Peter F. Drucker, *Managing The Non-Profit Organization: Principles and Practices* (New York: HarperCollins, 1990 ).

tools for managers in the nonprofit environment.

In the first part of the work, Drucker outlines the basic 'principles' of non-profit management, beginning with the concept of the organizational mission statement. The mission defines the institution, or organization. Effective mission statements are operational and focus on strengths and available opportunities of the organization. They take into account existing activities and seek ways to improve them. For Drucker, mission is a fluid concept, requiring flexibility to respond to changes in the external environment. An organization with flexibility is able to practice 'organizational abandonment'. This process entails a shift in the direction, mission or day to day programs of an organization. Simply put, "managers of non-profits also have to build in review, revision, and organized abandonment. The mission is forever and may be divinely ordained; the goals are temporary."<sup>46</sup>

Drucker understands leadership not as a hierarchal concept, but as an 'action oriented behavior'. In a nonprofit organization, all participants are leaders, regardless of their status as paid or unpaid members. His analysis does not suggest that leadership and innovation are traits or characteristics only belonging to senior organizational members. Rather, senior members are responsible for utilizing the abilities and skills of the organizational members. Drucker's explanation suggests that "we are creating tomorrow's society of citizens through the non-profit service institution. And in that society, everybody is a leader, everybody is responsible, everybody acts....Everyone

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<sup>46</sup> Ibid., 5.



raises the vision, the competence, and the performance of his or her organization.”<sup>47</sup>

This theme was briefly discussed in a work published in *Harvard Business Review* one year earlier in, *What Business Can Learn From Nonprofits*.<sup>48</sup>

In *Managing the Nonprofit*, Drucker makes a clear distinction between the roles and responsibilities of senior organizational members and those within the lower levels, including volunteers. Managers and Board of Directors are the senior members, responsible for developing mission and providing leadership for the organization. They determine strategy and set objectives. Volunteers, on the other hand, provide tactical support and are responsible for lower level activities within the organization. This clear delineation between management and labor was first made in his for-profit management works.<sup>49</sup> However, in an article predating *Managing the Nonprofit* by one year, Drucker argues for the inclusion of volunteers in more significant roles in nonprofit organizations in order to “put their knowledge to work.”<sup>50</sup>

Another issue raised by Drucker is the ‘lack of bottom line’ within nonprofit organizations. He suggests that nonprofit organizations need to utilize qualitative and quantitative tools in order to accurately gauge performance. Financial resources are

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<sup>47</sup> Ibid., 49.

<sup>48</sup> Peter F. Drucker, “What Business Can Learn From Nonprofits,” *Harvard Business Review* (July/August 1989) : 88-93.

<sup>49</sup> John Micklethwait and Adrian Wooldridge, *The Witch Doctors: Making Sense Of The Management Gurus* (New York: Times Books, 1996), 71.

<sup>50</sup> Peter F. Drucker, “What Business Can Learn From Nonprofits,” *Harvard Business Review* (July/August 1989) : 88-93.

integral to the nonprofit, but Drucker cautions “an institution that becomes a prisoner of money raising is in serious trouble and in a serious identity crisis.”<sup>51</sup> He acknowledges that financial concerns are often paramount to a nonprofit organization, yet cautions that an established mission and strategy is also vital to success.

### **Public Administration**

This part of the literature review will examine works at the forefront of public administration literature. The articles look at various issues including the impact of neo-liberalism on nonprofits in Canada, the climate of nonprofit competition with ‘for-profit’ organizations, and provide a rationale for the use of nonprofits to provide social services. This section ends with a recent examination of the information needs of nonprofit organizations. This issue has received little attention, yet is vital to the current discussion of nonprofits.

In *Shrinking the State*, Shields and Evans, assess the impact of neo-liberalism on Canadian governance.<sup>52</sup> They argue that the domination of neo-liberalism has transformed many aspects of public policy and reshaped public administrative discourse. The nonprofit sector has been eroded as a result of the impact of neo-liberalism.

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<sup>51</sup> Peter F. Drucker, *Managing The Non-Profit Organization: Principles and Practices* (New York: HarperCollins, 1990 ), 56.

<sup>52</sup> John Shields and B. Mitchell Evans, *Shrinking the State: Globalization and Public Administration “Reform”* (Halifax: Fernwood Publishing, 1998).

Shields and Evans begin to demonstrate this erosion by providing a descriptive overview of the third sector in Canada. The scope of the third sector includes 74, 027 registered charities in Canada and 5% of the Canadian labor force is employed by nonprofit organizations. There are also difficulties in defining and studying the Canadian third sector. It is a subject with “no commonly accepted nomenclature.”<sup>53</sup>

Shields and Evans challenge the left and right historical interpretations of the nonprofit sector. Their critique of the political rights neo-liberal assumptions suggests that the expansion of the welfare state and increases in taxation levels have resulted in a decline in voluntary giving. The empirical data presented by Shields and Evans provides a “clear counter argument to neo-liberal economic assumptions.”<sup>54</sup>

The authors go on to describe the effects of neo-liberalism on fiscal policy. They cite the ‘marketization’ and ‘commercialization’ of the nonprofit sector as the negative result of neo-liberalism. Marketization has forced nonprofits to engage in commercial activities and compete with for-profit organizations and government. Governments imposed requirements have forced nonprofits to shoulder a greater administrative burden in order to implement and measure performance. Neo-liberal assumptions are directly affecting the important democratic structures within nonprofit organizations. Ultimately, they note, the client base of nonprofits are most adversely affected.

The second section of the work discusses the implications of neo-liberalism on the ‘realignment’ of the third sector. This realignment is dominated by Alternative

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<sup>53</sup> Ibid., 89.

<sup>54</sup> Ibid., 93.

Service Delivery arrangements and partnerships linking various levels of government with nonprofit organizations. These arrangements are characterized by an unequal partnership, with the state playing a dominant role. The intention of the state in these new arrangements, is to 'off load' responsibilities to the nonprofit sector. The authors conclude that the current era, dominated by alternative service delivery and partnerships results in an environment in which "social service provision comes to be leaner and more residual in nature, a hollow shell of its former self." <sup>55</sup>

Following the theme of commercialization in the previous work, Gilbert's *Welfare for profit: Moral, Empirical and Theoretical Perspectives* will be reviewed.<sup>56</sup> This article, dating back to 1984 illustrates how the discussion over the role of the market and the nonprofit sector has existed for some time. In this work, Gilbert analyzes the arguments against the use of for-profit organizations as service providers in the American welfare state. The author takes the position that "social welfare program objectives are better served by public and private non profit agencies than by profit-making organizations." <sup>57</sup>

Gilbert first points to the major changes in the American welfare state that have occurred since 1960. One change is the shift from cash benefits to in kind benefits. These in kind benefits are allocated to individuals which meet a basic means test, through what

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<sup>55</sup> Ibid., 113.

<sup>56</sup> Neil Gilbert, "Welfare for Profit: Moral, Empirical and Theoretical Perspectives," *Journal of Social Policy* 13, no.1 (1984) : 63-74.

<sup>57</sup> Ibid., 65.

Gilbert calls the ‘social market’. There have also been shifts in responsibility for financing and service delivery. The introduction of pay for service arrangements and the expansion of public funds to purchase services provided by public agencies are examples of this shift. One of the most prominent shifts has government purchasing services from a combination of sources blurring between the for-profit and nonprofit sector.

Gilbert’s analysis contends that non profits are better suited to ‘serve the social welfare needs of the communities than for-profits for a number of reasons. Gilbert’s first reasons are the differences between the board of directors of a for-profit and nonprofit firm. The non profit board is comprised of members of the community who are dedicated to the social goals of the organization. On the other hand, a for-profit board is comprised of a membership that is bound by a fiduciary responsibility to “protect the financial interests of the ownership groups...”<sup>58</sup>

The two institutions also have different accountability structures. For profit firms are held accountable to the consumer public, not through their governing bodies but through the market. Nonprofits, on the other hand, have a unique relationship with their consumers and with the service purchaser. Non profits are more accountable to the purchaser, than the consumer. The primary purchaser is often government. The consumer rarely pays for the service, and therefore can rarely exercise purchasing power. One of the strengths of Gilbert’s work is that it presents a balanced argument, suggesting that accountability in nonprofit organizations is hard to enforce.

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<sup>58</sup> Ibid., 68.

Gilbert finds differences between for-profit and nonprofits in the 'motives and ideological disposition of these enterprises'. The for-profit, Gilbert notes, is characterized by its capitalist motives, such as a 'caveat emptor' while the nonprofit is characterized by a charitable ethos. In the nonprofit, consumers rarely purchase services, rather, goods and services are provided for individuals who are in a 'vulnerable life situation'. Gilbert suggests that this difference is somewhat exaggerated, as the social market and market economy can exist side by side.

The questions and arguments presented by Gilbert have also been discussed in public administration literature in Canada. In "*Shifting the burden: how much can government download to the non-profit sector?*", Hall and Reed look at the issue of downloading to assess whether nonprofit organizations have the internal capabilities to deliver an increasing amount of services in an era of downloading.<sup>59</sup> Their article begins by providing an overview of the political climate of downloading which is dominated by financial retrenchment as federal and provincial governments withdraw from direct social service delivery. This withdrawal has taken two forms, the termination of government programs and the reduction of government provided services. The authors contend that downloading has been the only viable option, given the pressures to control and reduce spending. As governments have reduced their activities, the third sector has become the cost effective substitute to maintain basic services.

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<sup>59</sup> Michael H. Hall and Paul B. Reed, "Shifting the burden: how much can government download to the non-profit sector?," *Canadian Public Administration* 41 no 1 (Spring 1998 ) 1-20.

However, Hall and Reed suggest that few nonprofit organizations have the internal capabilities to meet this demand. They point out two limitations that reduce the nonprofits effectiveness, 'human resource capabilities' and the 'value set'. Hall and Reed suggest that nonprofits suffer from a lack of professional expertise, relying on volunteer labor, and little paid expertise. They suggest the heavy load of responsibilities imposed on nonprofits by various levels of government is far too great. Nonprofits have a history of providing specialized services within a certain organizational value set that is not in line with the demands of government. This value set, and the goals nonprofits seek to attain, often conflict with government policy.

The point that Hall and Reed emphasize is that nonprofits have inherent limitations and cannot fulfill the role imposed on them by downloading without the support of government action. This is illustrated using Salomon's theory of government-non-profit relations. While Hall and Reed provide an adequate overview of the basic components of Salomon's work, Salomon's 1987 work, *Partners in Public Service: The Scope and Theory of Government-Nonprofit Relations* provides a more comprehensive explanation.<sup>60</sup>

Salomon seeks to develop a theoretical explanation for government-nonprofit relations in the American context. Before presenting his theory, Salomon provides a critique of the Weisbrod's market failure theory and Hansmann's contract failure theory, both of which see the voluntary sector as a 'second best' solution to the provision of

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<sup>60</sup> Lester M. Salomon, "Partners in Public Service: The Scope and Theory of Government-Nonprofit Relations" in *The Nonprofit Sector: A Research Handbook*, ed. Walter W. Powell (New Haven: Yale University Press, 1987), 99-117

socially desirable collective goods.

Salomon's government-non profit relations theory seeks to turn these negative frameworks, "on their heads", by providing a rationale for the existence of the voluntary sector as a preferred mechanism for the provision of collective goods. The role of government, in relation to the voluntary sector, is to provide support. This is determined and justified by four factors: Philanthropic Insufficiency, Philanthropic Particularism, Philanthropic Paternalism and Philanthropic Amateurism.<sup>61</sup>

Philanthropic insufficiency is the inability of the voluntary sector to generate adequate resources to respond to the needs of the community. Market fluctuations and the free rider problem both account for this inability. Philanthropic particularism is the "tendency of voluntary organizations and their benefactors to focus on particular subgroups of the population."<sup>62</sup> Philanthropic Paternalism is a product of the power of a nonprofit organization. Being situated within the hands of a small number of individuals serving a community. This group, usually take the form of the Board of Directors, which has control of the general direction of the nonprofit's response to community needs. Philanthropic Amateurism is a result of the organizational history attracting individuals with 'moral suasion and religious instruction' rather than job professional skills.

Hall and Reed uses this theoretical framework to illustrate the effects of downloading on small and large nonprofit organizations. The number of small nonprofit organizations, providing advocacy, educational and counseling services has been

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<sup>61</sup> Ibid., 111.

<sup>62</sup> Ibid.



reduced. This reduction is a direct result of reduced government funding and 'donor fatigue'. Large non profits have also been affected because they have shifted operations to meet the demands of the government of the day. Currently, the demand is on service provision, funded through short term contractual arrangements.

Reed and Hall conclude that a balance needs to be established between program management and social cohesiveness. The latter is achieved through advocacy based organizations. They also stress the need to "build conceptual framework which can 'capture the non profit more fully' as well as government-nonprofit relations. They suggest the success rate and the cost effectiveness of downloading could be determined empirically.

A key concept in public administration literature is 'effectiveness'. To understand how this term is conceptualized within nonprofit thinking, *Multiple Constituencies and the the Social Construction of Nonprofit Organizational Effectiveness* will be reviewed.<sup>63</sup> In this work, Herman and Renz attempt to identify what organizational effectiveness is, how it can be described and how it is determined by various organizational stakeholders.

Herman and Renz begin their analysis by questioning the use of mission, as a determinant of organizational effectiveness, an approach popularized by Drucker. The authors suggest that this approach is only useful when comparing organizations that have similar characteristics.

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<sup>63</sup> Robert D. Herman and David O. Renz, "Multiple Constituencies and the Social Construction of Nonprofit Organization Effectiveness," *Nonprofit and Voluntary Sector Quarterly* 26, no. 2 (June 1997) : 185-206.

In their brief review of the organizational effectiveness literature, the authors note that the study is very broad, with “as many models of effectiveness as there are organizations”. Despite the breadth of the interpretations, they narrow their study to two conceptual approaches, multiple constituency and social constructionism. The former suggests that organizations are made up of multiple stakeholders with different criteria for determining effectiveness. Because of these multiple stakeholders the nonprofit charity has to be sensitive to these multiple goals. Social constructionism suggests that organizational effectiveness is determined by the opinions of those involved in an organization. It is a “general ontological perspective”, as Herman and Renz describe it, which suggests that reality is comprised of the actions, beliefs and knowledge of individuals. In this view, organizational effectiveness is not a static phenomenon, rather it is determined by “stakeholders judgements formed in an ongoing process of sense making and implicit negotiation”<sup>64</sup>

Using the assumption that organizations are collections of individuals and effectiveness is a social construction, Herman and Renz gather information from both internal and external stakeholders to determine the similarities and differences in their evaluative criteria for ‘effectiveness’. In their description of their research design and sampling population, Herman and Renz identify the types of nonprofit charities targeted. These include nonprofit developmental disability and health and welfare provision organizations. The results of their analysis confirm what the contemporary literature suggests, that bottom line outcomes are not the only measures of nonprofit

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<sup>64</sup> Ibid., 188.

organizational effectiveness perceived by practitioners. Alternative indicators of effectiveness are used by practitioner. 'Correct procedure' and 'doing things right' are simple examples of alternative indicators.

Herman and Renz do not include external stakeholders in their analysis because they tend to have a different set of evaluation criteria and hence different outcomes.

The implications of Herman and Renz's analysis for managers and individuals within organizations are twofold. First, their work demonstrates that stakeholders have different views on effectiveness criteria. Nonprofit managers must be sensitive to this and respond by tailoring effectiveness data to the various stakeholders. The second key finding suggests that because effectiveness is a social construction, it needs to remain flexible. By maintaining flexibility the Board of Directors can respond to the changing needs of the external environment.

The subject of effectiveness cannot be discussed without also looking at the topic of accountability. To illustrate the interplay of these subjects in the literature Carroll's, *Administrative devolution and accountability: the case of the nonprofit housing program*, will be reviewed.<sup>65</sup> Although this work examines the case of nonprofit housing, the findings are consistent with and relevant to a range of implications for the ideas brought forth in this thesis.

Carroll's analysis begins with a discussion of the four predominant accountability systems. The most familiar system is bureaucratic accountability, characterized by its

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<sup>65</sup> Barbara Wake Carroll, "Administrative devolution and accountability: the case of the non-profit housing program," *Canadian Public Administration* 32, no. 3 ( Fall 1989): 345-366.

'rule bound' type of control. As Carroll notes, the features of this system include standardization of processes and outcomes as well as a hierarchal arrangement. The second type of accountability system is professional accountability. Professional judgement and expert decision making replace the traditional bureaucratic hierarchal arrangement. The third system, institutional accountability, is based on a relationship between an organization and its external constituents. The fourth system is legal accountability, governed by a fiduciary relationship between a regulator and regulatee. Carroll notes that all systems are used by government. However, some are better suited for pre or post audit situations.

Subsequently, Carroll asks, which system works when programs are delivered outside the traditional scope of government? To answer this, Carroll first presents a review of the various definitions of nonprofits. All nonprofits have accountability systems in place, regardless of their formal or informal status. However, when nonprofits and government are brought together to deliver services, the internal accountability systems that characterize each are ineffective at maintaining control and service quality. One of the problems that Carroll identifies is the conflict between the government sponsored program goals and the goals of the nonprofit organization. The author suggests that alternative forms of control need to be developed to reduce this conflict and ensure that nonprofits deliver services in the way that is intended by the government funding the project. These alternative mechanisms include incentives for compliance and the development of internal professional standards for members of the nonprofit organization.

In conclusion, Carroll suggests that “the ultimate power and decision making rests with a volunteer board which is expected to have the expertise to unravel and control the action of their paid staff - at no benefit to themselves.”<sup>66</sup> The board, she suggests, becomes captive of their paid staff and that the only accountability mechanism in place is a “financial report and a reliance on volunteers to ensure internal controls are maintained and to conform to the spirit of the project.”<sup>67</sup>

### **For-profit entry into social service delivery**

At this point, the literature will examine an article from the field of management that has applicability to the themes and issues raised by the observers of public administration. This literature provides a descriptive overview of the climate, in the environment of nonprofits, the competition they face and the changes being imposed on them. This next article looks at the issue of ‘for-profit’ entry into social service delivery.

In *The New Landscapes*, Ryan provides a synopsis of the changes that are shaping the environment of nonprofits.<sup>68</sup> Traditional views which placed for profits outside the scope of social services have been fragmented and an ideological shift towards marketization has become dominant. The nonprofit monopoly has been challenged by

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<sup>66</sup> Ibid., 362.

<sup>67</sup> Ibid.

<sup>68</sup> William P. Ryan, “The New Landscape For Nonprofits,” *Harvard Business Review* (January-February 1999) : 127-136.

this new marketplace. There is no longer a clear distinction between for-profit and nonprofit sectors.

In Ryan's analysis, outsourcing is a large component of the shift from 'rowing to steering', a conceptual framework critically described by Osborne and Gaebler.<sup>69</sup>

However, the author is skeptical that outsourcing has achieved success because it has been adopted without adequate empirical reasons. Decisions concerning outsourcing are often "more emotional than rational". Ryan also notes the impact of that the private sector has had on public sector culture. The culture of nonprofits has been greatly influenced and shaped by private sector concepts and ideas. These changes have had a significant impact on nonprofits, placing them in a difficult situation. They must adapt to an environment in which there is a new reward system, and set of performance measures.

The new social service environment, what Ryan calls a 'new zeitgeist', puts for-profits at a distinct advantage. They are typically larger, with a greater infrastructure, larger staff, and with a greater investment in technology. Through stock offerings, they are able to accumulate capital quickly. Meanwhile, nonprofits rely on grants which do not give them the ability to build reserves. For-profits have short term profit motives, and can move to areas that are more profitable. Nonprofits, on the other hand, have a long term commitment to community development.

In this 'new zeitgeist', the level of responsiveness also separates for-profits and

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<sup>69</sup> See David Osborne and Ted Gaebler. *Reinventing Government: Reform of Reinvention?* (Montreal: Institute for research in Public Policy, 1993).

nonprofits. For profits respond to two clients, the contractor and the user. On the other hand, nonprofits face a greater challenge, responding not only to government and service users, but also to society.

Ryan examines the responses of the nonprofit sector in this environment of increased competition for social service contracts. The for-profits have become project managers, the nonprofits are used as sub-contractors. Some nonprofits have responded by creating sub firms that are for-profit entities within the nonprofit umbrella.

Ryan expresses the view that nonprofits have some attributes which continues to separate them from for profits. They are able to deliver a contract as well as fulfill a mission which includes reinvestment into the community.

When Ryan discusses what he calls the 'new zeitgeist', he describes the new relationship between nonprofits and government. One of the components of this relationship is the use of information. Information plays an important part in nonprofit organizations by providing support for decision making and data for measuring performance.

In *The Voluntary Sector in the 'Information Society': a Study in Division and Uncertainty*, Deacon and Goulding look specifically at how information is used by nonprofits.<sup>70</sup> They attempt to "provide a broad descriptive map of the perceived information needs, sources and uses of voluntary groups..."<sup>71</sup> While their work identifies

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<sup>70</sup> David Deacon and Peter Goulding, "The Voluntary Sector in 'the Information Society': a Study in Division and Uncertainty," *Voluntas* 2, no 2 : 69-88.

<sup>71</sup> Ibid., 70.

problems facing nonprofit organizations responsible for the delivery of library services, the findings can be extended to the broader study of nonprofit featured in this thesis.

Information is a critical element within voluntary organizations. It enables nonprofit organizations to understand and work within the institutions around them. Information enables them to understand legal changes, funding structures, funding applications, and assists nonprofits in identifying the needs of the community.

Their analysis defines information as “any factual knowledge acquired through experience or study which might be of value to a group in its work.”<sup>72</sup> They identify four types of information. The first, national information, includes legislation as well as political trends. The second, local information, includes correspondence with local government and other groups. The third is practical information related to funding and management issues. The fourth is issue based information, which includes social and political issues.

Their findings suggest that the information needs of nonprofits vary more than other types of organizations. They have different characteristics and require different information. For example, they suggest that there is a ‘growing divide’ between formal nonprofits and completely voluntary organizations. The formal organization, which utilizes professional, paid staff recognizes the importance of information. Informal voluntary organizations do not typically recognize the importance of information.

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<sup>72</sup> Ibid., 75.



## **Part Two: Literature Review Critique**

The literature review has identified many of the key elements in the study of nonprofit organizations. Many contributors have suggested ways in which nonprofits can improve their role in society, yet none have developed a cohesive conceptual framework which might give us a blue print for the future. The goal of this thesis is to bring together ideas from the existing literature and develop a conceptual framework which can be used to improve the position and functioning of nonprofit organizations.

The public administration literature illustrates the challenges facing the nonprofit sector today. The general findings suggests that neo-liberalism has dominated the policy community, bringing about changes that have reshaped the nonprofit sector. These changes include 'marketization', 'commercialization' and 'downloading', all of which stem from the dominant ideological ethos of neo-liberalism as exemplified in the contemporary administrative state. This literature describes these effects on nonprofits, but fails to identify solutions to the problems threatening nonprofits. Evans and Shields describe the environment in which the relationship between the government and the nonprofit has been dramatically altered. In previous eras, funding was available for all types of nonprofits. These included education nonprofits , advocacy based nonprofits and nonprofits that delivered essential social services. However, in the current era, many nonprofits, especially the education and advocacy based organizations, are experiencing a massive reduction in government support. The current policy direction is leaving these types of organizations underfunded and without resources to achieve their organizational

mission. Evans and Shields in depth description of the neo-liberal policy on nonprofits is important for understanding the current environment. However, they do not provide suggestions that can be used to improve their position.

Similarly, Hall and Reed examine the issue of 'downloading'. They assess whether nonprofits can fill the void left by government reduction in direct provision of social services. The author's analysis suggest that nonprofits do not have the managerial infrastructure needed to fill the void. They also point out the need for a conceptual framework for understanding nonprofits from a broader perspective. However, their analysis does not provide any solutions or suggestions for nonprofit management to develop the needed infrastructure. Nor does their work forward any ideas about the nature of this conceptual framework and what it should include.

Another problem facing the development of a conceptual framework is the lack of a Canadian perspective on the history and theory of nonprofit organizations. The most influential contributors to the theory of nonprofits base their work on the American experience. They include Salomon, Tocqueville and many others. The Canadian contributors have established their findings based on many of the ideas first presented in American works. However, the Canadian experience is not a derivative of the American experience.

The literature from management, economics and public administration all suggest that the entrepreneur is important to understand the nonprofit. However, the entrepreneur is often conceptualized in its hierarchical sense. This is alluded to in Hall's historical analysis.

In the late 19<sup>th</sup> and early 20<sup>th</sup> century, a small number of individuals amassed great fortunes from industrial and commercial enterprises. Wealthy industrialists such as Carnegie and Ford were labeled ‘entrepreneurs’, a term that suggested keen business and marketing skills. As their empires grew, public sentiment sometimes shifted against them. Government and labour became critical of their wealth and impact on society. To mediate the negative effects taking shape in the form of labor unrest and government inquiry, these individuals used their wealth and power for the betterment of American society. They formed voluntary organizations in their name, ‘foundations’ as they are known today. These organizations addressed social issues facing American society, defused public criticism, kept economic empires safe from government and fulfilled altruistic motives. Through these organizations, industrialists claimed ownership of social issues and controlled the direction of charitable and government reform. At the time, government was unable or unwilling to provide adequate social services. The power of private foundations clearly outperformed the government’s meager resources. The foundations identified which issues would be addressed, ranging from the arts to poverty and allocated funds with their goals in mind.

Foundations had a great degree of centralized financial control and decision making. They were organized as a classic hierarchical organization. Both of these characteristics continue to shape organizations today. The legacy of the early foundations continues not only in structure, but also in the assumptions and beliefs promoted by their founders. The concept of the entrepreneur has evolved in relation to these factors.

Many of the current nonprofits, especially the formal charities and semi-formal

nonprofits feature hierarchical structures and a high concentration of entrepreneurial control. Both of these features are carried over from the early foundations. In the contemporary nonprofit, the entrepreneur is not the financier, but rather the paid manager or the volunteer Board of Directors. Throughout the literature no contributors conceptualize non-Board of Director volunteers as entrepreneurs. In the economic literature, volunteers at large are seen as providing a labour function.

In Drucker's management literature, a clear distinction between the entrepreneur and volunteers is established. The entrepreneur, or leader, is responsible for setting strategy for the organization. The volunteer, on the other hand, provides low level 'tactical' support for the achievement of the organizational strategy.

It is evident from the literature review that the entrepreneur is the prime mover of the nonprofit organization. However, the literature does not fully explain their role in relation to the broader political and social forces that are shaping the nonprofit sector. As well, the literature does not provide any recommendations for any of the existing shortcomings facing the nonprofit sector today.

This thesis seeks to provide these recommendations and bring forth the key issues surrounding the entrepreneur. To understand the concept of the entrepreneur in relation to these broader ideas, it is necessary to look at Schumpeter's entrepreneurship theory as it was originally put forth. By looking at Schumpeter's work we can extend his ideas to the nonprofit organization. In particular, this thesis will suggest that Schumpeter's work can be expanded to include not only the volunteer board member and the nonprofit manager, but other volunteer organizational members as well. By

expanding the concept of the entrepreneur to include more organizational participants, the capabilities of the nonprofit organization as a whole can be increased. This may provide the nonprofit with a greater ability to cope more effectively with the economic, social and ideological environment which continue to shape it.

#### **Chapter IV. Schumpeter's entrepreneur as innovator**

The first part of this section of the thesis will look at Schumpeter's *Theory of Economic Development*. This theoretical framework is based on a continuously evolving process of economic development, taking place in the 'circular flow'. The circular flow is comprised of a series of interactions between entrepreneurs who develop innovative production processes and the financiers who fund the implementation of these production processes. As a result of the innovations of individual producers, the economy evolves and the process continues. This section of the thesis will explain the concept of the entrepreneur in relation to this circular flow as put forth by Schumpeter.

Later, this model will be modified to explain events in the nonprofit setting. Some of Schumpeter's work can be used in this setting to explain the use of volunteers as entrepreneurs. I will show that this conceptual model, based upon the Schumpeterian model, provides a more thorough understanding of the entrepreneur within the nonprofit organization. It will be argued that broadening one's interpretation of the entrepreneur within the nonprofit may enhance the capabilities of these organizations. As well, this model provides a useful blue print for the future direction of nonprofit organizations.

In Schumpeter's 'circular flow' model of economic development the entrepreneur is the key to all economic activity. The entrepreneur is the prime change agent. Through his 'innovations', capitalism continually evolves, creating economic progress. While the concept of the entrepreneur is not new, Schumpeter's interpretation is different than other contributors. The works of Adam Smith, Marx and Heydens place

little emphasis on the entrepreneur. This chapter will concentrate on this theory which is featured in *Business Cycles and The Theory of Economic Development*, published in 1939 and 1934 respectively.

We should begin by understanding the aim of Schumpeter's work. His work was designed to bring some 'common sense' to the study of the circular flow and economic theory in general. Schumpeter sought to describe the activities within the economic process through the use of theory. For Schumpeter, "theory provided the tools for approaching facts and practical problems."<sup>73</sup>

His theory begins by analyzing the fundamental constituents of capitalist society. Schumpeter identifies two classes of persons in capitalist society. The first class, 'economic subjects', are central to economic development. Schumpeter describes them as subjects, with limited individual control over the economy. However, they initiate change then seek to educate the consumers, change their consumption wants and demands.<sup>74</sup> These changes are 'dynamic'. The other members of society comprise the second class. They are not considered 'economic subjects'. However, they are dependant on the actions and behavior of economic subjects. The choices, actions and decisions of 'economic subjects' affect not only themselves but others in society. The economic subjects act as producers in an environment which is uncertain and has inherent risks. All economic activity is conducted with one goal in mind, to 'satisfy wants'. In

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<sup>73</sup> Joseph A. Schumpeter, *The Theory of Economic Development: An Inquiry into Profits, Capital, Credit, Interest, and the Business Cycle* (Cambridge: Harvard University Press, 1934), x.

<sup>74</sup> Ibid., 65.

contemporary economics this is referred to as utility maximization.

In Schumpeter's model, production takes place within a capitalist economy. Schumpeter describes capitalism as the 'commercially organized state, one in which private property, division of labor, and free competition prevail.'<sup>75</sup> For Schumpeter, capitalism is also "that form of private property economy in which innovations are carried out by means of borrowed money, which in general... implies credit creation."<sup>76</sup> Production is solely designed to further the 'commercial and industrial flow' within the capitalist economy.

In the development of his theory, Schumpeter stresses that events in the economic sphere are not isolated. There are broader political and social forces that influence economic activity and economic development. This is best described in the following quote, "economic development is not explained economically but is dragged along by the changes in the surrounding world."<sup>77</sup> These changes have entangled the individual within capitalist society in a complex net of social and economic connections.

Economic development is also influenced by the past. Earlier periods have been 'forever altered' by certain types of economic, political and social changes. The change that Schumpeter describes is spontaneous and discontinuous. It is brought about by

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<sup>75</sup> Ibid., 5.

<sup>76</sup> Joseph A. Schumpeter, *Business Cycles: A Theoretical, Historical, and Statistical Analysis of the Capitalist Process*, vol 1 (London: McGraw-Hill Book Company, 1939) , 223.

<sup>77</sup> Joseph A. Schumpeter, *The Theory of Economic Development: An Inquiry into Profits, Capital, Credit, Interest, and the Business Cycle* (Cambridge: Harvard University Press, 1934) , 63.



entrepreneurs who are the “...bearer of the mechanism of change.”<sup>78</sup> Schumpeter refers to the process in which this change occurs as a circular flow. He compares it to “the circulation of the blood in an animal organism.”<sup>79</sup>

Within this circular flow, the entrepreneur is necessary for the facilitation of change. The entrepreneur rearranges existing production processes, Schumpeter calls this an ‘innovation’. To implement the innovation, the entrepreneur requires financing, ‘credit’. The entrepreneur must demonstrate his merit to the ‘banker’ to receive necessary credit. In return for credit, the firm pays interest to the banker. Without credit, the entrepreneur cannot purchase production inputs to create an innovation. When an innovation is successful, it results in entrepreneurial profit. These innovations result in changes that affect capitalist society. These changes forever alter an existing state of affairs. This is the circular flow, a process that is continually evolving. Given the basic assumptions of Schumpeter’s work, we can now look closely at the inner workings of the circular flow.

### **Schumpeter’s circular flow**

The circular flow is a flow of resources and talent from workers to firms and government. In exchange for their labour, workers acquire purchasing power. In the circular flow, two types of production take place. The first is the creation of ‘useful

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<sup>78</sup> Ibid., 61.

<sup>79</sup> Ibid., 71.

things', or objects that are consumed. This requires certain 'production forces' which are land and labour, capital and entrepreneurial talent. In the second form of production, 'innovation', these factors are arranged differently than the first. Here, the factors are used to create a 'new combination'. When this new combination is developed, it creates an innovation. While nonprofits do not produce in the same manner as Schumpeter's commercial and industrial environment, the concept of the circular flow provides one means of explaining the activities within the nonprofit. This will be illustrated in the next chapter.

There are five alternative methods or types of new combinations that can take place.<sup>80</sup> The first method involves the introduction of a new good "that is one with which the consumers are not yet familiar."<sup>81</sup> The second results in the "introduction of a new method of production, that is one not yet tested by experience in the branch of manufacture concerned, which need by no means be founded upon a discovery scientifically new, and can also exist in a new way of handling a commodity commercially."<sup>82</sup> The third method of innovation involves "opening of a new market, that is a market into which the particular branch of manufacture of the country in question has not previously entered, whether or not this market has existed before."<sup>83</sup> The fourth includes the "conquest of a new source of supply of raw materials or half-

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<sup>80</sup> Ibid., 66.

<sup>81</sup> Ibid.

<sup>82</sup> Ibid.

<sup>83</sup> Ibid.

manufactured goods, again irrespective of whether this source already exists or whether it has first to be created.”<sup>84</sup> The fifth type of innovation involves “the carrying out of the new organizations of any industry, like the creation of a monopoly position... or the breaking up of a monopoly position.”<sup>85</sup>

The person who introduces this new combination is the entrepreneur.<sup>86</sup> For Schumpeter, the entrepreneur is not only the business man or person with ownership of a firm. He sees the entrepreneur very broadly, including,

“all those who actually fulfill the function by which we define the concept, even if they are, as is becoming the rule, “dependant” employees of a company, like managers, members of boards of directors, and so forth, or even if their actual power to perform the entrepreneurial function has any other foundations, such as the control of a majority of shares. As it is the carrying out of the new combinations that constitutes the entrepreneur, it is not necessary that he should be permanently connected with an individual firm..”<sup>87</sup>

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<sup>84</sup> Ibid.

<sup>85</sup> Ibid.

<sup>86</sup> Joseph A. Schumpeter, *The Theory of Economic Development: An Inquiry into Profits, Capital, Credit, Interest, and the Business Cycle* (Cambridge: Harvard University Press, 1934) , 74.

<sup>87</sup> Ibid., 75.

The person who is an entrepreneur also performs other kinds of activities in the firm. Schumpeter suggests that the level of complexity, specialization and hierarchy in capitalist organizations did not allow for one to be an entrepreneur at all times.<sup>88</sup>

Entrepreneurs develop a 'new combination' in one area of a firm. However, it is unlikely they will develop new combinations in other areas of a firm. Schumpeter emphasizes that no one is always creating combinations.

In the contemporary literature, there is an unstated assumption which implies the entrepreneur is a permanent vocation. The entrepreneur is depicted as the nonprofit manager or the volunteer board of director. However, Schumpeter's analysis suggests the entrepreneur is "not a profession and as a rule not a lasting condition."<sup>89</sup> There are two points that Schumpeter emphasizes in regard to the entrepreneur. The first point is buried within one of his footnotes, where he states the entrepreneur is not the risk bearer.<sup>90</sup>

Personal characteristics such as status do not determine who is an entrepreneur. This is a vital element to his work as he does not define the entrepreneur by his class or status. He sees everyone as a potential entrepreneur. Schumpeter explains that "entrepreneurs are like hotels which are indeed always full of people, but people who are forever changing. They consist of persons which are recruited from below to a much greater extent than many of us are willing to admit."<sup>91</sup>

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<sup>88</sup> Ibid., 77.

<sup>89</sup> Ibid., 77.

<sup>90</sup> Ibid., 75.

<sup>91</sup> Ibid., 156.

However, to become an entrepreneur, one must possess certain abilities or skills.

In this part of Schumpeter's analysis, some confusion arises over the term leader and entrepreneur. He uses these terms simultaneously, suggesting that one individual may play both roles. It appears this is determined by the context in which this innovation takes place as well as the size of the organization. In small firms, the owner may play the role of entrepreneur and leader. However, this is not always the case, especially in large firms.

The entrepreneur has to be able to develop a new combination for a problem that falls outside the 'boundaries of routine'. He is called upon to recommend a 'best possible solution' to a complex problem. In less complex situations, managers are needed, not entrepreneurs. Schumpeter makes a clear distinction between the entrepreneur and the manager. The entrepreneur creates a new combination, while the manager is needed to implement new combinations in a profitable manner. The manager is also responsible for overseeing the operations of a firm.

In complex situations, leaders create certain conditions which are necessary for innovation. They possess intuitive skills and confidence, described as an 'effort of will'. Entrepreneurs that step outside the 'barriers of routine' have little information or data from which to develop new combinations. To compensate, the leader uses his intuition, rather than guessing or relying on strategic assessments and estimations. This requires confidence to take actions when information may not be available. An example of a military strategist is used to emphasize this point. The leader must possess the 'effort of will' to deal with issues and barriers that may ultimately arise. These barriers may

include political, legal and social tensions.

Some person may attempt to resist innovation which inevitably affects other producers and laborers. Innovation “may impose temporary sacrifices, privation or increased efforts upon the members of the community.”<sup>92</sup> Schumpeter suggests that innovation displaces some of the producers and suppliers in the circular flow. When an innovation is introduced, other producers and labor are unable to earn entrepreneurial profit or wages. Without wage earnings or entrepreneurial profit, they are not able to purchase consumption goods. These persons become displaced by the capitalist circular flow. Schumpeter was concerned about the broader effects of innovation. He suggests the community should assist those displaced by the capitalist economy.

To carry out an innovation, an entrepreneur rearranges factors of production. When the entrepreneur is unable to modify the use of factors of production, innovation will not occur. The innovation will occur elsewhere, and the firm in question may cease to exist because they did not innovate. The concept of innovation is continuously emphasized by Schumpeter as necessary for the continual survival of organizations in the circular flow. Thus, the entrepreneur and his ability to innovate is dependent on the person who finances the means of production. For Schumpeter, this is the ‘banker’. Entrepreneurs cannot implement innovation without ‘bankers’. This analysis suggests the entrepreneur contributes to the short term viability of the firm, but does not necessarily contribute to the long term success of a firm. Firms require support from the

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<sup>92</sup> Joseph A. Schumpeter, *The Theory of Economic Development: An Inquiry into Profits, Capital, Credit, Interest, and the Business Cycle* (Cambridge: Harvard University Press, 1934), 69.

banker, if they are to survive. The long term viability of a firm will ultimately be determined by the banker's willingness to support innovation.

In Schumpeter's model, the leader, or entrepreneur, leads the firm into new channels of production. However, this person is reliant on the bankers' capital to implement a new combination. Schumpeter lays out the process of obtaining capital. He emphasizes that "No one other than the entrepreneur needs credit."<sup>93</sup> The entrepreneur seeking credit approaches the banker. This credit provides the entrepreneur purchasing power for the acquisition of capital. The banker rates the entrepreneur's past achievements which determines 'trust worthiness'. If the entrepreneur is able to establish a level of trust worthiness with the banker he is granted credit, "Betriebskredit".<sup>94</sup> This is working capital, the only form of credit given by the bank. According to Schumpeter's theory, all credit is aimed at innovation to further the circular flow of economic development. Bankers only provide it to those who demonstrate an ability to 'innovate'. Many of these aspects of Schumpeter's work also apply to nonprofits, which require resources to create innovations. This will be further explained in the chapter to follow.

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<sup>93</sup> Joseph A. Schumpeter, *The Theory of Economic Development: An Inquiry into Profits, Capital, Credit, Interest, and the Business Cycle* (Cambridge: Harvard University Press, 1934). 102).

<sup>94</sup> Ibid., 103.

### **The role of capital and interest**

There are two other factors involved in this transaction, capital and interest.

Capital is referred to as the ‘independent agent’ of economic development. It is “nothing but the lever by which the entrepreneur subjects to his control the concrete goods which he needs, nothing but a means of diverting the factors of production to new uses, of dictating a new direction to production.”<sup>95</sup> As the theory suggests, capital is vital to the process which allows for innovation.

The other factor is the concept of interest. Interest is described as the “ephor of the capitalist system.”<sup>96</sup> It acts as a ‘brake on development’ which controls the fluctuation within the economic sphere. As we have seen, these effects are felt by many persons, including economic subjects and the community at large. Schumpeter was conscious of the impacts of capitalist development. However, he was unable to provide answers or solutions to the broader problems associated with innovation. Although innovation was central to economic development, there are negative consequences that arise from development. For example, the number of economic subjects are reduced. This creates a two class society, with persons separated by their ability to purchase goods. Schumpeter did not try to solve issues such as this. His analysis recognizes there are human costs associated with capitalism. An example would be the loss of purchasing power when individuals are displaced by innovation. For Schumpeter, purchasing power

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<sup>95</sup> Ibid., 116.

<sup>96</sup> Ibid., 211.



equated to individual freedom and independence. Schumpeter recognizes there were no easy answers to these issues which had become ingrained in the fabric of capitalist society. Rather, Schumpeter used credit as an instrument to limit future economic expansion. By limiting future expansion, innovation and the negative consequences of it could be controlled.

### **Entrepreneurial motivation**

In Schumpeter's circular flow, entrepreneurial talent, land/labour and capital are all necessary. Yet the circular flow cannot be generated without entrepreneurs. Schumpeter was intrigued by the elements which motivated entrepreneurs. He recognized that financial rewards provided the purchasing power necessary to participate in a capitalist economy. He called this type of motivator, the 'dream', which is very similar to the contemporary concept of 'vision'. Schumpeter also recognized other motivating factors which he characterizes as the "will to conquer" and the "joy of creating."<sup>97</sup> Entrepreneurship and its motivating factors are paramount concerns to both the Schumpeterian analysis of commercial and industrial production as well as the nonprofit. In the next chapter, the concept of the entrepreneur and motivation will be further explained in the context of the nonprofit.

With the first type of motivator, persons are influenced by the possibility to achieve a level of social distinction that comes with being an entrepreneur. This social

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<sup>97</sup> Ibid., 93.

distinction comes with the introduction of a new combination. If a combination is successful, the entrepreneur receives entrepreneurial profit. This entrepreneurial profit is first defined as 'surplus over costs' and includes an "appropriate wage for labor performed by the entrepreneur, an appropriate rent for any land which may chance belong to him, and finally a premium for risk."<sup>98</sup> As his wage rises, he is able to move upwards along the social, political, economic spectrum. Prior to the innovation, the person may have been an employee, but afterwards is elevated in status and pay. As such, his dependence on others within the circular flow decreases. Essentially, this type of entrepreneur is motivated by 'satisfaction of wants'.

The second motivator is the "will to conquer...not for the sake, not of the fruits of success, but of success itself."<sup>99</sup> As he notes, the motivational characteristics of these entrepreneurs are different than the first. Success is much more important than financial rewards. The person motivated in this manner, is an entrepreneur who undergoes "hedonistic adaption", moving beyond the initial needs.

The third motivator is the "joy of creating, of getting things done or simply exercising one's energy and ingenuity."<sup>100</sup> This person plays a vital role in the process of industrial development. He creates the necessary conditions for investment, based on successful innovation. Schumpeter suggests that those motivated by the 'joy of creating

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<sup>98</sup> Ibid., 128.

<sup>99</sup> Joseph A. Schumpeter, *The Theory of Economic Development: An Inquiry into Profits, Capital, Credit, Interest, and the Business Cycle* (Cambridge: Harvard University Press, 1934), 93.

<sup>100</sup> Ibid.

and the will to conquer' may in fact have their needs met outside of the capitalist economy. It is here where a vital point is brought forth. Schumpeter states that "Nevertheless, it is true that the second and third groups of entrepreneurial motives may in principle be taken care of by other social arrangements not involving private gain from economic innovation."<sup>101</sup> This can be interpreted to suggest that private gain is not a satisfactory outcome for those which may not be concerned with satisfaction of wants.

Schumpeter leaves us with an unanswered question. He briefly touches on the subject of entrepreneurs outside of the industrial context, but does not weave this into his theoretical framework. He asks, "What other stimuli could be provided, and how they could be made to work as well as the "capitalist" ones do, are questions which are beyond our theme."<sup>102</sup>

We know from his earlier work in *Business Cycles* that entrepreneurs are not limited to the realm of capitalist industrial and commercial life. Leadership and entrepreneurs exist in other forms, "even in a primitive tribe or in a socialist community."<sup>103</sup> To understand why they exist requires us to consider aspects other than entrepreneurial profit and credit creation. They exist not only for these reasons, but to fulfill the motives that Schumpeter identified. In this next section, I will explain how this framework will be modified to examine the role of the entrepreneur in nonprofit

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<sup>101</sup> Ibid., 94.

<sup>102</sup> Ibid., 94.

<sup>103</sup> Joseph A. Schumpeter, *Business Cycles: A Theoretical, Historical, and Statistical Analysis of the Capitalist Process*, vol 1 (London: McGraw-Hill Book Company, 1939) , 223.

organizations. I will also discuss the difficulties associated with this.

### **Modifying Schumpeter's framework**

Schumpeter's circular flow acts as a conceptual map that explains many aspects, including the role of the entrepreneur, innovation, capital, credit and interest. However, it focuses solely on 'industrial and commercial life'. In Schumpeter's time, little, if any attention was paid to the nonprofit sector in terms of economic discourse. Schumpeter's model, nevertheless provides a useful way of understanding the role of entrepreneurs in any type of organization. The entrepreneur is the facilitator of change and the implementor of new combinations of innovation. This is especially evident in nonprofit organizations where the entrepreneur provides the ingredient to fulfill an organizational mission. Nonprofit contributors have recognized the importance of the entrepreneur in explaining many aspects of these organizations and Schumpeter's work is frequently referenced. However these works only examine a few components of Schumpeter's model. Most contributors do not challenge the assumptions upon which Schumpeter's model is based. They often apply his theories directly from the for-profit to the nonprofit without consideration of the difference between the two.

Badelt, for example, identifies the importance of the volunteer component of Schumpeter's 'labour' category. Yet he sees volunteer labour as a 'production process'. This notion of work as a component of 'production' is misapplied in the nonprofit context. Badelt makes little distinction between factory workers, for instance, and

nonprofit volunteers. This for-profit paradigm upholds classical economic hierarchies which should not be applied in the nonprofit environment. Volunteers are not easily exchangeable factors of production to be manipulated by paid staff.

Ackerman's concept of the ideologue recognizes the importance of the entrepreneur to the nonprofit, but again, she applies the concept of the entrepreneur directly from the original for-profit context. The ideologue is presented as a high level manager with inventive ideas for change. This maintains organizational hierarchies, as volunteers and others are not considered potential entrepreneurs.

The two examples of Badelt and Ackerman suggest the necessity for investigating Schumpeter's concept of the circular flow in the nonprofit context. An in depth analysis of the nonprofit circular flow may provide practitioners with a greater understanding of the different environment, activity and mission of the nonprofit. Through this vehicle, nonprofits may expand their conceptual tool box, and realize the potential role for volunteers as entrepreneurs. In the next chapter I will identify and discuss aspects of the Schumpeterian model that can be modified for the nonprofit setting, beginning with the circular flow.

## **Chapter V. Using Schumpeter in the age of the contemporary nonprofit**

### **The nonprofit circular flow**

One of the key concepts in the previous chapter, the circular flow, is relevant to today's nonprofit environment. The circular flow and its focus on the entrepreneur and mission provide the basis for a conceptual framework which shows how nonprofits can expand their existing abilities.

The functioning of all nonprofits may be described as a circular flow. The relationship between internal and external influences on the nonprofit are explained by this model. The interactions between internal and external aspects are explained in a way that accounts for constant change. The circular flow is a dynamic concept which highlights the potential for change in organizational behavior. An understanding of the complexities and interconnections in the circular flow enables practitioners to assess the broader implications of their actions and behaviors. By taking a holistic approach to planning, strategy and policy implementation, one can realistically assess the effectiveness of their organization. External factors including economic conditions, government policy, political influences, prevailing ideology, and global trends are taken into account. Of particular importance to the nonprofit environment are social conditions, including cultural, community issues and employment conditions. Through an assessment of an organizations' place in the circular flow one can identify opportunities and limitations of their situation. Most importantly, the circular flow shows

how internal resources can be manipulated to have a positive influence on the external environment.

One predominant issue that must be taken into account when looking at the nonprofit environment is its resource dependency. Unlike for-profit entities, which sell products or services to accumulate wealth and capital, nonprofits must rely on external resources to maintain self-sufficiency. Their financial reliance on government grants, corporate philanthropy and private donations places them in a tenuous position. Their financial resources are outside of their direct control. As a condition of this dependency, nonprofits must seek alternative ways to achieve their goals. Because their goals are different from profit seeking entities, finances are not the nonprofits' dominant concern. Alternatively, nonprofits must focus on their human resources, the part of the internal flow which they can control and which achieves their mission to change the human condition.

The internal activities of nonprofit organizations are accomplished by the human resources, consisting of both paid and unpaid staff. Members from both are able to make decisions, establish policy and deliver services. All of these actions are directed at the primary goal of changing the human condition. Both paid and unpaid staff are motivated by altruistic intentions and are equally committed to the mission of the nonprofit. Paid staff are motivated to some degree by monetary gain, however their commitment to the ideals of the nonprofit is not compromised. An indicator of this commitment is that paid staff in nonprofits often have shorter terms of employment and are paid less than their counterparts in the for-profit and government sectors. Regardless of their position as paid

or unpaid staff, what is most important to consider is how a person impacts the internal workings of the nonprofit. Individual choices, decisions, actions and behavior all have an impact on the circular flow. Although contributions by individuals vary greatly, it is the net effect of combined effort that can increase the tempo of the circular flow.

The concept of tempo as it relates to the circular flow requires further explanation. Tempo is a measurement of the impact that the nonprofit has on the community that it serves. It reflects the actualization of change in the human condition. The tempo of the circular flow is difficult to quantify. It measures a number of factors that determine the success of mission put into action. These include how service is offered, quantity, its success at changing lives, and its influence in the community. The tempo reflects the individual contributions made by both paid and unpaid staff in the nonprofit. Tempo is an abstract concept, one which reflects the non-linear contributions of nonprofits to society and which needs to be approached from an intuitive holistic perspective.

The entrepreneur is the primary vehicle for increasing the tempo of the circular flow. The entrepreneur is the change agent in the nonprofit organization. By using the internal resources of the nonprofit, the entrepreneur can find new ideas and methods which have a positive effect on its external influence. Entrepreneurs provide the nonprofit with new perspectives or alternative methods for rearranging resources, to meet mission in a better way. In utilizing new sources, the entrepreneur can increase the tempo of the circular flow.

When new methods or perspectives are enacted in the nonprofit an innovation



occurs. Innovation is the entrepreneurial idea put into operation. This contributes to the mission of the organization. The group that is affected the most are the end users in the community which the nonprofit serves. An example of such an innovation is a nonprofit where an entrepreneur has shifted the coordination of its activities and marketing from popular media and word of mouth to a more progressive internet communications method. Board meetings, volunteer recruitment, information services, service delivery and the day to day operations are focused on internet communication. This has several advantages, among them are cost savings. Costs are reduced when communication and service delivery are removed from their physical environment. Less money is required for capital investment and property. Recruitment is invigorated by increasing communication with its volunteer base. This facilitates the potential for finding volunteers to replace paid administrative positions. Responsiveness to its client base is improved through greater communication with both clients and staff. This increases the tempo at which the nonprofit is able to serve the community. The value of individual effort and contribution can be more easily recognized and reinforced through this medium. A response to this is greater commitment of volunteers to the mission, as they become more active participants.

Innovation, as the above example illustrates, is key to the nonprofit's effectiveness at serving the community. The improvements to the lives of the end users brought about by innovation reflect the increasing rate at which the nonprofit cycles through its circular flow. Innovation is a key concept that illustrates the dynamic nature of the circular flow. As the product of the entrepreneur, innovation is the critical point

where a concept or idea meets the external environment and creates change. This point of convergence between the internal and external aspects provides a focus for discussing the complexities involved in the circular flow.

The internal functioning of a nonprofit organization follows a three stage cycle. Before describing each stage, it must be noted that this cycle is non-linear. In most organizations all three stages are operationalized simultaneously, in various different projects and initiatives. The nonprofit entrepreneur can organize ideas and activities in all three stages. The cyclical stages of internal development are resource recruitment, resource application and project or mission assessment.

Resource recruitment is the first stage. Both financial and human resources need to be identified and pursued. A realistic assessment of short term capabilities is required. Organizations must assess the available financial and human resources to determine whether a project is achievable.

Resource application involves managing service delivery and the day to day operations of the organization.

Project or mission assessment is the third stage. In this final stage in the internal cycle nonprofits must evaluate their performance. Four factors must be considered. It must be determined whether human and financial resources were used in the best way possible. Secondly, volunteer and paid staff satisfaction needs to be assessed. This is important for maintaining a motivated resource base. Thirdly, the satisfaction of financial funders must be assessed. Did donors, whether corporate, government or others receive value for their contributions? Quantitative and qualitative analysis can be used to

assess this value. Close communication with funders would also facilitate an assessment of their overall satisfaction, and of their likelihood of continuing their support. The fourth factor is an assessment of overall mission. Here the nonprofit must assess overall impact of their operations on their client base. Is mission being achieved?

In general, project and mission assessment lead back to the resource gathering stage, and the cycle begins again. Results of project assessment are used to rearrange objectives for the next cycle of development, and hopefully, of innovation. No single period or project can ever fully achieve the mission of an organization, and therefore continuous cycling and progression is required to meet the demands of changing external conditions, as well as the changing needs of their targeted client base. It must be stressed that the internal development of an organization is not as linear as this model suggests. All three stages, resource recruitment, application and assessment occur simultaneously within an organization. Individuals within an organization may be working with different aspects of the three stages at the same time. For instance, in a large formal nonprofit with a hierarchical structure, there are some staff who are responsible for narrowly defined areas of the cycle. The marketing staff may be predominantly concerned with resource recruitment. Volunteer coordinators work more with human resource application, but also recruitment and assessment. Program directors cross all categories, from financial recruitment, to service delivery and assessment. The complexity and interconnections between different components and time frames illustrates the multitude of variables which make up the internal circular flow of a nonprofit organization.

No less complex are the components of the external flow. All of the activities of

the internal flow occur in the context of forces being constantly applied by the social, economic and political environment. These factors comprise the external component of the circular flow. The mission of nonprofits are often defined by their response to conditions, often negative, created by the external environment. When a nonprofit creates a change, they counteract the potential negative impact of external environment. Following is a description of the many of the ways in which the external circular flow affects nonprofits.

Economic conditions can have both a negative and positive effect on a nonprofit. For instance a recession might create greater unemployment. This in turn puts new pressures on many nonprofits which must adapt and innovate to meet the new demands placed upon them by the community that needs its service. In response, a nonprofit might seek ways to increase the tempo of its internal cycle. This illustrates some of the dynamics between internal and external flows. A particular external condition may create the conditions for an innovative change in the way a nonprofit operates.

Alternatively, prosperous economic conditions may be beneficial to the nonprofit. They may face a lower demand for their services, when there is greater wealth in the community. This economic growth may result in increased government spending on nonprofits as well as in the private sector. Prosperous corporations will need greater tax shelters. This will give them the incentive to donate to nonprofit organizations.

Another quasi-economic influence is corporate ideology. This, for the most part, has had a negative impact on nonprofit organizations. Corporate ideology influences peoples perceptions about nonprofits. Economic terminology has become the norm in

public discourse. Notions of efficiency, production, and consumption have been defined by advertising and marketing propaganda. As discussed in the definitions section of this thesis, even the definition as 'nonprofit' is defined by what it lacks in comparison to the corporation. This has far reaching impact on the perception of nonprofits in public discourse. Nonprofits and government services are perceived to be less efficient and not as good at providing goods and services compared with the private sector. The influence of corporate ideology on the structure of formal nonprofits is very strong. Nonprofits have been forced to mimic structures and processes dominant in the corporate sector without due consideration to the very different goals and service they provide. Bottom line considerations in resource and program assessment have often become paramount to service delivery. Corporate ideology is synonymous with government as well. Government assessment of nonprofits and their resource allocation use for profit standards in determining the value of an organization.

Government policy is another layer of complexity in the external circular flow. In many ways, government policy is relatively stable, but its cumulative effects over time can be drastic. The general neo-liberal policy direction has had insidious effects on nonprofits. Advocacy and education groups have been hit hardest by changes in the political spectrum. Their reliance on government funding to survive has placed them in a very difficult position, as policy changes have decreased funding to these organizations. Many of these organizations do not have recourse to other sources of funding, because their organizations are not usually attractive to corporate donors. For example, women's abuse advocacy groups, and women's shelters do not provide high profile services which

might promote corporate image. A tobacco corporation, for example is more likely to fund an arts or sports organization because of their image, and greater advertising potential.

The trend toward privatization of government and nonprofit services is another effect of the neo-liberal policy arena. Recent cut backs in Manitoba to Child and Family Services and the privatization of Home Care are examples of this trend.

On the other hand, government policy can affect nonprofits in positive ways. Community pressure on a particular social issue may cause government to increase funding to some nonprofits and to fund new programs. Aids Hospices, aboriginal healing centers, fitness and recreation programs, including provincial and national sports bodies, are examples of government funding of community oriented programs.

The community represents the external social force of the nonprofits circular flow. The community shapes the direction of the nonprofits mission. The nonprofit serves a mission which is representative of the needs of this community. Individuals or groups within the community have specific needs which are not addressed by either the market or by government. These needs vary a great deal. They may range from the needs of homeless persons for food, clothing and shelter, to the needs of art connoisseurs. Both of these examples correspond with a specific mission, “to feed the homeless” or “to establish an art gallery.” A group, or individuals with this request relies on an existing nonprofit to serve its needs. If there are no existing group, a new nonprofit is established or the need is left unfulfilled.

The internal and external circular flows of nonprofit organizations have been

illustrated in this section. The continuous cycling of external and internal flows, as mentioned, is complex and non-linear. All aspects of the three internal stages of resource recruitment, application and assessment evolve along side the multitude of external economic, political ,government and community influences. Constant entrepreneurial talent and innovation are required for the nonprofit to succeed in this volatile environment. The next section will explore ways in which the concept of the entrepreneur can be better utilized to improve the ways in which nonprofits can affect the circular flow and achieve their mission.

### **The nonprofit entrepreneur**

Popular and business definitions of the entrepreneur are inadequate in the nonprofit context. The concept of the entrepreneur needs to be revised to include a broader range of persons who may contribute to mission by developing new innovations. This new paradigm incorporates ideas from Schumpeter's original entrepreneurship theory and applies them to the nonprofit context in the current economic, social and political arena. A new definition of the nonprofit entrepreneur will be forwarded which suggests a broad expansion of the popular understanding of who can be an entrepreneur and what roles they can play in nonprofit organizations.

The entrepreneur is not a permanent position in an organization, with a particular set of responsibilities. This view is a misconception engendered by popular and business terminology that equates the entrepreneur with the business manager. Anyone in an

organization has the potential to be an entrepreneur, from paid managers to volunteer staff at the front lines of service delivery. The entrepreneur is defined by his or her act of innovation. This can occur at all organizational levels if there is a mechanism in place to allow entrepreneurial talent to come forward. No matter how large and formal or small and informal the organization the potential for talent is the same. Not everyone can or will come forward with new ideas, but it is essential that organizational culture encourage this development.

In the current policy arena nonprofits, both large and small, seldom actively encourage innovation outside of paid managers and the board of directors. This hierarchical structure often discourages others in different positions within an organization to come forward with innovation. The more senior paid positions are perceived to have the answers to innovation. Unfortunately, the opposite is often true. Participants on the front line, especially volunteers, are better positioned to understand the needs of service delivery and the effectiveness of mission in operation. This organizational culture may intimidate potential contributors, especially volunteers. Often, volunteers are not given the opportunity to communicate their ideas to coordinators and managers, making it difficult and frustrating to create change.

There are many reasons why nonprofits must look beyond senior staff for entrepreneurial talent. Senior level staff may not have the opportunity to recognize situations in which innovation might occur. The higher one's position in an organization, the more general one's tasks become. Movement up the organizational ladder goes from a tactical 'bricks and mortar' role to a conceptual and strategic role. Instead of building



the house, higher management conceptualizes “how to build the house”. This step away from building site distances higher level staff from the construction of mission. This function of upper management is necessary and desirable, but in terms of opportunity for innovation, it is overrated.

Innovation is about specifics, not generalities. This positions individuals that work in specific areas better than those in management for potential innovation. This includes all kinds of support staff, and volunteers. How are they positioned better? They know the issues intimately and have first hand experience with them. In the case of volunteers, mission is the driving reason for their participation in the nonprofit. As they are without remuneration, their motivation is solely based on helping others and personal satisfaction. Working directly on the frontlines, these individuals see the direct impact of the external environment and how it affects the circular flow in a way that managers cannot. The nonprofit entrepreneur works at this point of convergence between activity and result, at the juncture of internal and external circular flows. It is here where innovation is most likely to occur. Paid staff and volunteers with such direct experience often have an intuitive ability to recognize the limitations and shortfalls of service delivery, and possess a knowledge of what will work to improve the situation.

So far, this thesis has discussed the concept of the entrepreneur as a kind of philosophy; as a way of perceiving the potential for innovation. What, exactly, constitutes an innovation has not been defined. The discussion about the tasks of the entrepreneur has been deliberately vague for several reasons. There are no hard and fast rules for defining the activity of the entrepreneur. However, there needs to be a practical

basis, and a tangible definition of the entrepreneur, otherwise it becomes just another management buzzword that is not taken very seriously. The entrepreneur defines herself by innovation. Here, Schumpeter's notion of activities which are inside and outside the boundaries of routine becomes important. Whereas, the manager, or so-called 'entrepreneur', may lead an organization with the savvy of having prospected every second page of every single edition of the *Harvard Business Review*, he nonetheless may not achieve anything outside the boundaries of his MBA. This example is a bit facetious, but it makes an important point. Innovation occurs outside the boundaries of expectation.

A precise definition of the activities of the entrepreneur would defeat the notion itself. Innovation cannot be pigeon-holed by a five step program or some other convenient categorical device. Some generalities, however, can be identified. Innovation is contextual. What may be an innovation for one organization may be routine in another. This depends on the size, position, development and sophistication of particular organizations. For example, an internet discussion group might be very innovative for a small informal nonprofit that previously relied on quarterly meetings to communicate. However, for a large formal organization, a website is hardly innovative. The point here, is that it is impossible to judge what constitutes an innovation and what does not, from an external perspective. Innovation is what works in achieving the mission of an organization. This mission may be as simple as fund raising for a community club, or as sophisticated as providing meaningful work for the disabled. An assessment of innovation would be very different between these groups, and could only be made by the members themselves and the community they serve. No matter how simplistic the

innovation appears to others, it may nonetheless constitute entrepreneurial success, if it succeeds at mission.

There are many issues to consider when thinking about who the concept of the entrepreneur is likely to apply to, particularly among large, formal nonprofits. Some entrepreneurs may arise from permanent or temporary staff, paid or unpaid. Others may come from outside the organization itself. Even if a person has only a peripheral contact with the nonprofit, he might have new ideas to bring forward which reflect his experience and insight into the community served by the nonprofit. This entrepreneur may only attend meetings once a month, nonetheless, his ideas should not be dismissed. Talent should not be measured by the amount of time a person spends in an organization.

Persons outside the formal boundaries of a nonprofit may have greater insight into the needs of the clients served by the nonprofit. Community trends and influences may only surface from an outsiders perspective. They might see a particular need in the community that is not met by the nonprofit, and might offer suggestions about expanding the role of the nonprofit. Such persons might also have a keen awareness of private competition in service provision, and might be able to inform the nonprofit of current trends.

Following is a closer examination of the sources of entrepreneurial talent within different levels of nonprofit organizations. This includes both formal and informal nonprofits with varying degrees of sophistication. Some may be entirely volunteer based, others come together on an ad hoc basis for a short period of time or for a specific cause or goal. We begin with an analysis of paid and then unpaid staff in formal nonprofit

organizations. Strategic and operational management will be discussed first, followed by support staff. Finally, the traditional role of volunteers will be assessed at both the board of directors level and the frontlines of service delivery.

Strategic management represents the upper level of nonprofit management. Most staff are permanent, well paid senior employees. Often they are the spokespeople of the organization, and have a higher degree of power and influence than other staff at the operational and support levels. They are responsible for steering the course of the nonprofit, and thus they view the organization from a very broad perspective. They are skilled at handling the multiple tasks required for strategic planning. However, the emphasis on administrative work places them in a position which makes it difficult to create innovation. In the larger formal nonprofits, they are rarely involved with individual service delivery, and may have only a marginal knowledge of the activities of operational staff. Strategic management is an important function in the nonprofit, but contrary to popular belief, it is not the best source for innovative ideas.

Operational management deals with specific areas of nonprofit management. This includes program specialists including volunteer co-ordinators, program administrators, fundraisers and information technologists. These positions are usually either permanent or longer term contract work, often dependent on specific programs and funding constraints. They have specific expertise in their field and are more likely than strategic management to create innovation. They take direction from senior management and administer or implement programs. Essentially, operational management usually plays the role of the 'gate keeper' of innovation. If they do not themselves recognize sources of

innovation, they nonetheless take charge of implementing the innovations recognized by others.

Unpaid volunteer staff make up the final component of our analysis of nonprofit staff. There are two areas of volunteer participation: the board of directors level and the front line 'labour' level. At first sight this seems like a peculiar arrangement. In formal nonprofits there are volunteers at the very top, with paid staff in the middle and volunteers again on the front lines. This begs the question, why are there so many paid staff in the middle? This unusual state of affairs has its roots in the historic origins of the modern nonprofit. The nineteenth century foundation exemplified this pattern. Wealthy industrialist donated their time and money to implement nonprofit organizations. In this way, the industrialists performed a similar role as the volunteer board of directors in contemporary nonprofits. The wealthy philanthropist staffed the foundation with paid employees, usually men. On the other side of the organization, volunteers, usually women, conducted service delivery. These women were often the wives of business managers and other social elite. The masculine notion of the entrepreneur has its roots in this state of affairs. The traditional role of volunteers has also been circumscribed by this historical antecedent.

The volunteer board of directors in nonprofit organizations often consists of two types of community representation. Predominant are economic figures, fitting the popular definition of 'business entrepreneurs'. These figureheads are usually representatives of the business elite who are expected to bring sound financial management and political savvy to the organization. Secondary representation comes

from community leaders who have special insight into the particular mission of the nonprofit.

The business people represented on the board contribute to the popular notion of the entrepreneur. Their role as business leaders, as 'entrepreneurs', is often applied to their work with nonprofit organizations without a second thought. This contributes to the notion that entrepreneurship is simply capitalist business management. Unfortunately, many nonprofits follow this ideology by concentrating on recruiting high profile business representatives for their board of directors. There are serious problems with this scenario, because these business representatives typically are not entrepreneurs in the Shumpeterian context. They are usually very conservative people, who have had success by aggressively competing in the marketplace with great capital at their disposal. Most have not developed new combinations in the economy, but have simply managed existing operations with great success. As the for-profit arena of product and service delivery is of a very different nature than the nonprofit environment, the business person may have difficulty understanding the different goals of the organization. More often than not, for-profit managers in the nonprofit context do not understand the sources of innovation. They seldom recognize the point of convergence between service provision and mission. Having been accustomed to managing from the top down only, they are unlikely to understand the sources of nonprofit innovation. It is difficult to leave corporate ideology at the doorstep of the boardroom to change one's perspective.

Some business board of directors have particular talents and skills which can be utilized to the benefit of the nonprofit. Fund-raising and marketing skills, for instance.

With these talents, business board of directors are able to use their skill to advance the circular flow, and promote entrepreneurship. Unfortunately, popular discourse on the subject recommends that Board of Directors should not be directly involved with the day to day operations of an organization. They suggest Board of Directors play a role in the overall direction of the nonprofit, but not on the specifics. Such recommendations are based on for-profit ways of thinking, but this is out of place in the nonprofit context. Nonprofit Board of Directors have a different function. They are not there to make a profit. They are there to create change in the human condition. This requires a different kind of entrepreneurial talent.

Community leaders and community representation on the board of directors is a secondary component. These individuals are excellent sources for entrepreneurial talent. Nonprofits should emphasize their participation on the Board of Directors. Community leaders are able to respond to innovation because they are aware of the issues and external influences on the nonprofit.

Volunteers on the other end of the organization often play a labour function in the nonprofit. When volunteers are used strictly as labour, their depth of experience is very limited. However, when given the opportunity to work multiple tasks, insight can be gained which can contribute to a volunteer's ability to recognize situations where entrepreneurial talent can surface. Unfortunately, many nonprofits abuse the labour function and do not realize its potential. Paid managers tend to view volunteer labour with a very limited perspective. They become accustomed to certain processes of organizing and delegating tasks to volunteers. This limits their perspective of what

volunteers can do. This results in a situation where menial tasks are delegated to volunteers, and the potential for innovation is reduced, regardless of how much encouragement and appreciation the volunteer is given.

Management of volunteers in the traditional way of organizing and delegating routine and compartmentalized tasks fails to utilize the most fertile potential source for entrepreneurial talent. Nonprofit organizations need to expand the role of the volunteer, to include all aspects of operations, strategy, resource recruitment and labour. A new paradigm is needed which uses the volunteer as the focal point of the nonprofit organization. Volunteers should be allowed to take on as much responsibility as they want, depending on their interests and abilities. There is a misconception that volunteers do not contribute as much to nonprofits as paid professionals. This perception is false. Volunteers, by the very fact of their voluntary participation, have proven their loyalty to the cause. To expand the role of the volunteer a change in this perception needs to take place. The nonprofit culture needs to see volunteers as potential professionals, rather than pawns of program implementation. Volunteers should be allowed a higher level of responsibility within formal nonprofits, even if this infringes on the security of paid staff. Ultimately, from a conservative, mission oriented point of view, it is preferable to have volunteers in place of paid staff wherever possible. This opens up resources for direct activity aimed at achieving mission. For example, a provincial sports body which replaced a paid administrator with volunteer labour could re-allocate the former money reserved for the salary to direct program enhancement.

The change to viewing volunteers as professionals and entrepreneurs does not



entail the wholesale abandonment of the traditional view of volunteers as labour. It must be admitted that many volunteers want nothing other than to play their small incremental role in service delivery. This role is an important component of nonprofit functioning that must not be underestimated, nor taken for granted. What this thesis suggests is that we must think of volunteers in a much broader context. Nonprofits must realize that volunteers are as capable as paid staff at any position or level of an organization.

The advantages of utilizing volunteers at all organizational levels include enhanced entrepreneurial talent. Volunteers experienced in multiple roles both inside and outside the organization may be in a better position to create a new 'combination', as Schumpeter calls them. The greater numbers of volunteers, combined with their diverse and varying life and work experiences, constitute a greater potential pool of entrepreneurial talent in comparison to paid staff. Paid staff often perform their work 'within the boundaries of routine'. They are working to earn their living and for personal satisfaction. Their particular position, with its job description and certain responsibilities, circumscribes their experience and their ability to seek new ways of working and thinking. Most paid staff are to some extent dependent on the income they receive from the nonprofit. This dependency fosters a conservative attitude. A paid professional, for example, is unlikely to find an inspiring new way of working which contradicts her job description and particular role within an organization. Paid staff are unlikely to bite the bureaucracy that feeds them.

Another entrepreneurial advantage of volunteers is their front line experience. Volunteers often become members of a particular nonprofit organization because of a

life experience. An obvious example would be a care giver who volunteers for an Alzheimer's organization because of a family experience with the disease. An emotional, intuitive connection to the mission of a nonprofit can result from such an experience. The tremendous commitment and resolve of hands on, front line volunteers can transform into innovative program policy and strategic development, but only if organizational culture promotes this. Their keen perception of the external social, and community environment, places them at the point of convergence between internal and external circular flows. This is the moment of service delivery. A meals on wheels volunteer reflections of an elderly clients life experiences and the various social and economic injustices suffered, as well as the community support, create an amalgam of intuitive and practical experience which informs her perception. Perhaps her commitment and respect will generate an innovation. An example of this might be a new program which delivers nostalgia, as well as an ethnic meal to the elderly.

Any volunteer who has demonstrated entrepreneurial talent should be considered to take on operational levels of the nonprofit. The particular status, or length of time the volunteer has been with the organization are not important. Anyone, in the right circumstances and at the right time may create innovation. Ambition and creativity should not be penalized or suppressed due to organizational structure. Perhaps succession of management in a nonprofit could be decided by placing innovative volunteers in staff positions, as they become vacant, or when the nonprofit is seriously hit by a reduction in funding. Why not replace resource dependence with entrepreneurial independence?

### **The new model: A conceptual paradigm**

The objective of this new model of volunteer entrepreneurship is not create a 'how to' manual for nonprofit organizations. This would be impossible given the great variation in size, level of formality and mission of nonprofits. Rather, the goal is to open up a new way of thinking about the potential for volunteer contributions to nonprofits. It is not the place of this thesis to suggest ways in which this could, or should be implemented. In this era of formulaic prescriptions of management theory, with its glut of acronyms, an antidote is needed.

Writers in public administration literature, Brudney, for example, have only approached volunteer management from a labour, or resource function model.<sup>104</sup> This does little to enlighten our perspective. Volunteers should not be treated in the same way that labour is used in the for profit context. The nonprofit volunteer is fundamentally different, as this thesis suggests.

Individual organizations must themselves search for ways to promote the volunteer as entrepreneur. This thesis seeks to allow nonprofits a window in which they can appreciate the volunteer, and take the concept of the entrepreneur seriously. There can be no universally applicable theory on how to accomplish this, as every situation is different. The concepts and ideas presented in this paper constitute a toolbox out of which organizations can begin to build mechanisms to promote the voluntary

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<sup>104</sup> Jeffrey Brudney, "Designing and Managing Volunteer Programs" in *The Jossey-Bass Handbook of Nonprofit Leadership and Management* ed. Robert D. Hermann (San Francisco: Jossey-Bass Publishers, 1994), 279-302.

entrepreneur.

The concept of the volunteer entrepreneur is a holistic approach to nonprofit organization which integrates systems thinking, i.e. the circular flow, with conceptual tools forged to help the nonprofit achieve its mission. The broadly defined Schumpeterian entrepreneur, integrates all levels of nonprofit organizations and places them on a level playing field where hierarchies of structure and process become less important than talent and innovation.

## **Chapter VI. Conclusion**

What follows is a chapter by chapter summary of important arguments and findings. The chapter on definitions identifies the ways in which nonprofits have been characterized. Nonprofits' tax exempt status and legal-structural definitions contribute to our perception of the place of nonprofits in society, particularly of their acceptance by government and the community. Such definitions highlight the hierarchical formality of large nonprofits and provide an international reference point for comparative analysis. Legal-structural definitions, however, do not account very well for informal nonprofits. Drucker's 'human change agent' definition provides a mission oriented definition which enables the reader to think differently about the function and purpose of nonprofits. Analysis of the negative definition of 'non' profits provides insight into the frequent misapplication of for-profit structures and ideology in the nonprofit sector.

The literature review and critique illustrates the lack of an encompassing body of theory and analysis specific to nonprofit studies. Problems facing nonprofits are often studied in depth, but ideas for solutions, and ways to move forward are rare. Writers on altruism were narrow in focus, providing an individualist, liberal focus on the needs and desires of individuals who choose to donate their time or money to nonprofits. No author successfully presents a social or community approach for explaining altruism. Attempts at this were, at best, examples provided by individual watersheds in social history, not of broader social/historical trends. The section on contemporary writers on entrepreneurship theory suggests the importance of the concept to nonprofit studies. However, the scope of

the entrepreneur is limited to a management function. The popular understanding of the entrepreneur as a successful, inventive businessperson is upheld in much of this literature. In this scenario the difference between the for-profit and nonprofit entrepreneur is merely a prefix. The historical analysis by Hall is important for the understanding the origins of the nonprofit's close link with business. Corporate philanthropy and the development of foundations contributed to the structural similarities of formal nonprofits. Hall's analysis illustrates how little structural change has occurred within formal nonprofits since their inception. Gender roles, hierarchies and power relationships can be explored in this historical context. The management literature on nonprofits remains deeply rooted in the capitalist context. Few contributors push the boundaries of existing for-profit management theory. Drucker provides a different approach, which reconceptualizes many components of traditional management theory. His holistic approach is refreshing, although it is still conventional in its for-profit sentiment. Drucker's mission focus for nonprofit managers is a useful concept, but is limited by Drucker's acceptance of traditional roles and hierarchies in nonprofit organizations. The public administration literature provides very important insight into the contemporary political and economic conditions in which nonprofits exist. Problems are defined and analyzed, but no tangible solutions are sought. This is the main failing of this literature. Issues are raised, but no suggestions are put forth about how problems may be overcome. Resource dependency, neo-liberal policy change, downloading, accountability, effectiveness and information technology comprised much of this literature.

The chapter on Schumpeter presents a full analysis of the main currents of his work. Schumpeter's theory of the circular flow and the entrepreneur provides a common sense approach to theory. The focus is on people, not production and on seeking internal solutions rather than external. The two components of the circular flow, the internal and external are fundamental concepts for understanding the whole functioning of an organization. Schumpeter's theory of the entrepreneur is vital in that it recognizes the fluidity of the concept between levels and structures within an organization. This critical component of his theory seems to have been overlooked.

The chapter entitled, Using Schumpeter in the age of the contemporary nonprofit, presents the beginning of a new conceptual model aimed at broadening the perspective and functioning of nonprofit organizations. The section on the nonprofit circular flow uses Schumpeter's ideas to explore the possibilities for self-awareness among nonprofits. It provides an alternative viewpoint from which nonprofits can re-assess the interactions between internal and external components of their specific environment. This is the first stage in assessing the potential for entrepreneur talent at all levels of an organization. Human ability and motivation is the primary focus of the internal nonprofit circular flow. This is quite different from the 'production function' of most business enterprises. Innovation can increase the tempo at which the internal flow moves. The external circular flow is illustrated in the context of its own complexity. The interrelationships between political, economic, social, community and government are illustrated in a way that encourages practitioners to understand them as a web of reality, and not as separate components. The point of convergence between internal and external circular flows is

made a focal point of an organization's activity. This point of convergence is where tangible change occurs, and where innovation and the potential for entrepreneurial talent is greatest.

The section on the nonprofit entrepreneur suggests that nonprofits must expand their vision of the entrepreneur to include all levels within an organization, especially volunteers. The situational context for the potential for innovation is explored at all organizational levels. Volunteers are identified as the most likely source for innovative talent due to many variables, including proximity to service delivery, proximity to the point of convergence in the circular flow, volume, specific talent and others. Expanding the role of volunteers to include all organizational levels is recommended, and traditional hierarchies are challenged by insight derived from the circular flow and the volunteer entrepreneur.

### **The New Model**

The concept of the circular flow and the nonprofit entrepreneur challenge many of the assumptions upon which nonprofits have relied. The organizational culture of contemporary nonprofits date back to the 19<sup>th</sup> century period and the rise of the Foundation. This formative era carried forward many of the assumptions and beliefs about nonprofits that are still in use today. The close link with for-profit management theory emerged at this time. Foundations were modeled after the enterprises of the wealthy industrialists who created them. Characteristics include a high degree of



centralization, division of labour, and a hierarchical structure. This organizational culture is still prevalent today among formal nonprofits.

In the contemporary nonprofit environment, these traditional structures do not suffice in dealing with the external pressures brought about by downsizing and an often hostile neo-liberal policy agenda. Furthermore, the traditional nonprofit culture is intrinsically limited by its structure, to allow for new and innovative ideas to surface. Little effort has been made to re-shape nonprofits, in order that they may succeed in achieving mission in the dynamic and changing world of which we are all part.

Some nonprofits will not be able to survive with the limited tools available to them in the current policy arena. Mission becomes harder to achieve when nonprofits accede to the ideological perspective of government and private donors.

The traditional paradigm also fails to account for the real diversity among nonprofit organizations, especially less formal varieties. There are lots of different types of organizations, structures, cultures and compositions. Many of which should not be pigeonholed by the formal definitions of nonprofits.

The concept of the circular flow attempts to incorporate all the divergent external and internal influences on nonprofits, regardless of their particular standing as formal or informal, large or small. Applying Schumpeter's idea about the circular flow illustrates the necessity for nonprofit managers to start thinking differently. By taking a holistic approach new avenues of mission achievement and internal organization can be implemented which are outside the boundaries of routine; that is, outside the boundaries of the accepted norms of nonprofit management and operations.

How can a new way of thinking and managing be enacted? Managers of nonprofits need to begin thinking about their role more as co-ordinators rather than as managers. Nonprofit management typically follows the for-profit model. Production, the manipulation of inputs and outputs, and the delegation of duties to others constitute the work of managers. This business model is out of touch with the nonprofit environment. To co-ordinate rather than manage means to have less direct control over the activity of the organization. Co-ordinators remain at an arms length from the activities they oversee. In this position, they may be responsible for promoting a culture in which innovation is fostered among volunteers and other staff members. Delegation of tasks is decided on individual judgement of service providers and operational staff. This empowers staff at all levels of an organization and promotes mission achievement by motivating individuals. Increased autonomy opens barriers to innovation, by invigorating volunteer commitment. Co-ordinators can focus on intrinsic rewards, such as a sense of accomplishment and belonging, rather than external motivators, such as a salary.

A tailored approach to each individual, at all levels of an organization is required. Large organizations need to recognize the value of volunteers not only as labour. For paid management in nonprofit organizations it is too easy to underestimate and undervalue the contribution of volunteers. Their vantage point may be far from the realities of service provision. Co-ordinators must begin to see the volunteer as the fundamental reference point for the organization. A nonprofit should represent the sum of individual missions. The nonprofit is a collective of people gathered to change a particular aspect of the human condition. Volunteers usually constitute the largest

component of its members. As such, the volunteer should be paramount at all organizational levels. At present, co-ordinators must develop ways to allow volunteers to fulfill their own goals. This is the way forward to creating innovation through volunteer entrepreneurship.

How can this be done? One way to begin might be to survey all volunteers about why they volunteer for this particular organization. Find out more about their motivations, values, skills and interests. This information can be utilized to give volunteers an opportunity to use their unique skills in ways which are not part of the day to day operations of the nonprofit. A number of accountants, for example, might wish to volunteer their expertise at a higher organizational level. With this information a co-ordinator might be able to replace a paid position with a number of committed volunteers. Organizations can begin to professionalize their volunteer base by moving innovators up to co-ordinating positions. This might mean replacement, or partial replacement of paid staff by outstanding volunteers. In this way, an open organizational culture can create intrinsic incentives for innovation. Another method for motivating volunteers is to research the value of their commitment. Provide volunteers with information on the tangible results their effort is providing.

The ideas presented above, by no means constitute a how-to model for broadening volunteer participation in nonprofits. As stated previously, each individual organization must develop their own ideas about volunteer participation. The ideas suggested here are merely examples of what is possible, not prescriptions of how to implement change. Every organization is different, and some are not responsive to

change. This is a perfectly acceptable reality for many organizations. In some cases, if you move quickly to re-arrange an organization you risk alienating resources, staff, community and clients alike. Organizational culture, especially among large, formal nonprofits, cannot be changed quickly. Incremental change rather than transformative change is often more successful at changing the direction of such an organization. Any change is dependent on a multitude of factors, many of which are external to the nonprofit and thus cannot be controlled. Government regulation and policy, for instance, might prohibit certain kinds of innovation, especially if the nonprofit is dependent on government for its financial resources.

The concept of the circular flow is a useful tool for any organization to assess the impact of service delivery and volunteer participation. Schumpeter's model, as applied to the nonprofit provides insight into the point of convergence between the internal operations of the nonprofit and the external environment where service provision is achieved. The circular flow can be applied to any organization, from a lemonade stand staffed by a couple of children fund raising for school programs, to a multinational nonprofit such as the Red Cross. The circular flow can be applied internationally, across cultural and political divisions. By comparing the operation of nonprofits across economic, political and cultural norms, the practitioner can gain insight into the nature of altruism, and a new perception of what is possible.

Nonprofits in poor, 'underdeveloped' countries are very different from the rich western nonprofit bureaucracies. Yet, a comparative analysis of the circular flow of each might lead to insights which could benefit both. In very poor areas, Bangladesh for

instance, volunteer entrepreneurship may be very strong. Even though there is little economic prosperity there is a substantial amount of innovation taking place. Perhaps this is because of necessity. A nonprofit may be entirely voluntary, informal and have very little resources, yet their mission may be very immediate, feeding homeless children for example. The dire necessity of the external circular flow is ripe for innovation to occur. Why is this the case? There is less organizational hierarchy, and more willingness to listen to any solution that might come forward. The urgent need pushes the tempo of organizational change.

Western nonprofits tend to be more formal, larger, and possess far greater resources, yet their mission is often less urgent than that of the poor informal nonprofits of the developing world. A systematized, structured hierarchy inhibits organizational change. The somewhat lower urgency of mission, combined with bureaucratic features results in a different perspective on the need for innovation. Even so, innovation is just as desirable in the affluent nonprofit as it is in those that struggle to survive.

A cross-cultural, and socio-economic comparison of nonprofits may be accomplished by using the circular flow as a mechanism. An analysis of the vastly different external circular flows across cultures and nations may provide connections which can bring together new ways of organizing nonprofits. For example, the incremental policy change characteristic of western governments constitutes a very different external influence than the civil unrest, and totalitarian regimes found in other areas of the world. In this way, the concept of the circular flow can be used to find new ways of defining the role of mission, service delivery, volunteers and entrepreneurship.

### **The Next Step**

The conceptual framework presented in this thesis suggests ways in which the concepts of the circular flow, entrepreneurship theory and increased volunteer participation can improve nonprofit organizations. As yet, these are untested ideas. There is a need to validate and substantiate the focus on volunteers and informal nonprofits. Many aspects of nonprofits, both formal and informal need to be studied and assessed. A variety of data can be gathered from nonprofits to substantiate these ideas. We need to find out more about the role of innovation. We need to find out how mission is achieved at all levels of size and formality. Issues which require investigation include the relationship between resource dependency and innovation. What is an appropriate mixture between resources and innovation? Obviously, both are required, but how much is one dependent on the other? Investigating these aspects will allow nonprofits to refine concepts in the circular flow.

Another important area for future research involves finding out more about the types of nonprofits that receive the least attention, the informal nonprofits, especially in developing countries. How is mission achieved with few resources? How is this different from western nonprofits? What role do entrepreneurs play, and how is innovation accomplished? Who are the entrepreneurs? In developing countries a greater number of women than men volunteer for nonprofits. Perhaps studying this can help nonprofits in other contexts to see the entrepreneur as a gender equal concept.

Finding out more about informal nonprofits in developing countries may increase

awareness about global responsibilities of nonprofit mission. Too often nonprofits are mandated only within their national boundaries. Perhaps awareness and co-operation with other cultures and nationalities may result in global partnerships. This could change the way nonprofits operate, and expand the scope of the entrepreneur. Re-allocating resources where need is most urgent may result in better service delivery and a more equitable division of resources between developed western communities and developing communities. This would accelerate the rate at which nonprofits serve mission by linking human and financial resources globally. We see this happening already with the Mennonite Brethren, which coordinates with informal nonprofits in developing countries.

Such partnerships may be a fertile ground for sharing information, strategy and innovation. The wealthy western nonprofits can share information and communication resources, such as internet access, to facilitate a closer interaction across physical limitations of time and space. Individual communication, between volunteers working in very divergent external social, economic, political and community environments could provide new insight and innovation. For example, much can be learned from nonprofit entrepreneurs in developing communities who achieve mission despite a nearly total lack of financial resources. Many insights can be gained from their example, even at the higher management levels of wealthy bureaucratic western nonprofits.

However, before any of this can be accomplished, nonprofit practitioners need to gather data from nonprofits in a global context, and try to assess the potential for connections, partnerships and entrepreneurial innovation.

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