

THE FORMATION, PERFORMANCE, AND STRATEGIC DECISIONS OF NONPROFITS

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## ABSTRACT

This dissertation includes three essays about nonprofit organizations. The first essay investigates how the availability of financial and intellectual capital in the macro-environment influences the formation of nonprofit organizations. The analysis is an extension of Weisbrod's (1975) Heterogeneity Hypothesis and Ben-Ner and van Hoomissen's (1991) "social cohesion" principle. Findings indicate financial capital and intellectual capital are important to the formation of nonprofits, but the strength and direction of their influence varies by industry.

The second essay applies Stakeholder Theory to predict the influence of board members, donors, and beneficiaries on nonprofits' performance. The study incorporates 134 charities from six different industries over a five year period and finds nonprofit performance is driven by the interests of the most salient stakeholders. Furthermore, the analysis indicates nonprofit stakeholders have the ability to control the behaviors of managers; behaviors which are not necessarily aligned with mission statements. No evidence, however, suggests salient stakeholders with shared interests collaborate for mutual benefit.

Stakeholder Theory is also used in the third essay to predict the moderating role stakeholders fulfill in the relationship between environmental uncertainty and nonprofits' strategic decisions. The study incorporates the same database as the second essay and discovers the influence of environmental uncertainty on nonprofits' strategic decisions depends on the ability of salient stakeholders to diversify their interests. The identified effect encourages Stakeholder Theory applications adopt a dual-perspective approach to the concept of salience; such applications need to account for the salience of the stakeholder to the organization and the salience of the organization to the stakeholder.

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## PREFACE

The research presented concerns nonprofit organizations. My interest in nonprofits stems from their economic importance and, more importantly, their deviation from management theories.

Nonprofits constitute a substantial and fast-growing segment of the US economy (see Table 1). The nonprofit form is employed by charities, trade unions, non-governmental organizations (NGOs), and community organizations to advance social interests such as healthcare, education, economic development, natural resources, arts and culture, public safety, and recreation. The outputs of nonprofits (e.g. safety, public health, arts and culture, education, environmental preservation) represent the foundation by which other economic activity occurs. Entrepreneurship, market expansion, knowledge management, innovation and countless other economic activities all depend on the social and economic infrastructure provided by nonprofits (Bose, 2003; Gnyawali & Fogel, 1994; Powell, 1990; Powell, Koput, & Smith-Doerr, 1996). In addition, nonprofits are considerable contributors to economic activity in their own right. Each year from 2000 through 2006, nonprofit institutions serving households (NPISH) have accounted for at least 6% of the GDP and about 15% of total wages (Wing, Pollak, & Blackwood, 2008). The importance of nonprofits is also demonstrated in the increasing amounts of support they receive. From 1996 to 2006, private giving increased more than 200% to \$295B, volunteers increased 26.7% to 61.2M people, and donations from corporate giving programs and foundations increased 69% to \$12.7B (Wing, et al., 2008). Thus, theory-building and empirical research about nonprofits has social importance because it better informs stakeholders – from those who are served by nonprofits to the entities within the same economic ecosystem – about the contexts under which nonprofits thrive and fail.

*Table 1 - US Employer-Based Business Growth (number of firms)*

	1997*	1999**	2007*	2009**	10-year CAGR
All Employer-Based Organizations	6,430,633		10,098,738		4.62%
All Nonprofit Organizations		1,202,573		1,581,111	2.77%
501(c)(3) Public Charities		631,902		1,006,670	4.77%

\*US Economic Census

\*\*IRS Business Master File

My research is also motivated by the distinct theoretical challenges belonging to nonprofits. The first challenge concerns governance and the presumptions of profit maximization and rational man (Mill, 1874). For example, Agency Theory (Coase, 1937; Jensen & Meckling, 1976; Williamson, 1983) asserts principals control agents' inefficient behavior through incentives and monitoring (Finkelstein & Daveni, 1994; Hendry & Kiel, 2004; Hillman & Dalziel, 2003). Direct (equity holdings, stipends) and indirect (access to lucrative social networks) economic benefits motivate principals to take such initiatives (Finkelstein & Daveni, 1994; Sundaramurthy & Lewis, 2003; Zajac & Westphal, 1994). Simultaneously, agents rationalize they can expropriate organizational resources more efficiently and with greater certainty by exploiting informational advantages (Eisenhardt, 1989; Jensen & Meckling, 1976). The studies used to build and confirm these theories are derived from for-profit contexts. However, for nonprofits, where private inurement is prohibited and equity markets are absent, these explanations lose applicability. That is, the prohibition of private inurement for principals (i.e. board members) seemingly eliminates their motivation to control agents (Easley & O'Hara, 1983; Hansmann, 1980; Speckbacher, 2003; Wallis, 2006) and the absence of nonprofit, equity markets limits their ability to align the agents' interests with the organization. How then do nonprofits control the strategic decision process?

The second theoretical nuance of nonprofits relates to their mission statements and, in turn, organizational performance. Recent conceptualizations of for-profits' performance have been broadened to include social responsibility and sustainability (A. B. Carroll, 1979; Cruz & Boeche, 2008; Frederick, 1994, 1998; Janjuha-Jivraj, 2003; MacDonald & Norman, 2007; Margolis & Walsh, 2003; McWilliams & Siegel, 2000, 2001; D. J. Wood, 1991), but the emphasis still remains on correlating such organizational behavior to competitive advantages and, in turn, financial performance (Margolis & Elfenbein, 2008; Margolis & Walsh, 2003). For nonprofits, however, organizational performance has always been multi-dimensional. Whereas mission statements identify nonprofits' social causes (what is provided to whom), the perpetuity of the organization is equally dependent upon its economic resiliency. The relationship between nonprofits' financial and social performance is understood as reciprocal and mutually dependent (Baruch & Ramalho, 2006; Moore, 2000); one pursuit cannot be achieved at the expense of the other. This dynamic suggests the resources, knowledge, alliances, or competencies capable of advancing nonprofits'

dual-headed, performance mandates have properties which may be transferrable to for-profit contexts where problems with cost externalization or unfulfilled social responsibilities are unresolved. That is, better understanding about how nonprofits' pursue multiple performance mandates may offer value to researchers struggling to understand why for-profits engage in activities seemingly unrelated to profit-maximization.

For these reasons, I offer the following research.



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## CHAPTER 1

## NONPROFIT THEORY IS A MISNOMER

## Introduction

The founding principles of US nonprofits derive from the Statute of Charitable Uses passed by the British government in 1601 ("The Statute of Charitable Uses Act (1601)," 43 Elizabeth I) which outlined how private money could be used for the public good and, in turn, bypass government taxation. Although evidence indicates nonprofits were the dominant organizational form in the US during the colonial period (Davis, 1917; Newhouse, 1970), the first analytical descriptions of US nonprofits did not emerge until Alexis de Tocqueville's *Democracy in America* (1840) where he described how individuals with similar interests would form organizations outside of the private and government sector to advance social causes. More robust, academic theories explaining why the nonprofit form is best-suited to address social causes did not emerge until the 1970s and 80s; these explanations include the Trust Hypothesis and the Heterogeneity Hypothesis.

The Trust Hypothesis (Hansmann, 1980) and the Heterogeneity Hypothesis (Weisbrod, 1975) both employ demand-side conditions to explain the formation of nonprofit organizations. The Trust Hypothesis states the nonprofit form is a response to a market failure. Donors demand assurance that their gifts will be allocated towards intended purposes rather than expropriated by managers. Such trust is derived from information concerning nonprofits' reputations, histories, and experiences. For new organizations engaged in the process of acquiring resources, these indicators of competence, morality, and intent are undeveloped. Hence, relative to incumbent rivals, new organizations struggle to attract gifts from donors. The nonprofit form, with its formal regulations concerning private inurement and financial reporting, is an alternative method for acquiring donors' trust. The Heterogeneity Hypothesis, on the other hand, emphasizes the demand for social goods<sup>1</sup> by non-median voters. The demand for social goods by median voters (i.e. centrist constituents) is provided by public entities through tax mandates and

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<sup>1</sup> Social goods are those where individual consumption does not inhibit the benefit available to others; suppliers' cost to serve the individual are not substantially different than the costs to serve many; volume does not drive consumers' costs to consume; and buyers' have difficulty in creating, evaluating, and enforcing contracts governing the social goods' quality, quantity, and availability (Ben-Ner, 1986).

allocations to service programs. The non-median voters, however, demand social goods which by definition are not supported by a general consensus. Hence, public entities will not administrate the necessary programs to produce such social goods. Instead, nonprofits, through tax advantages and development activities, garner and combine the necessary resources to offer social goods demanded by the non-median voter. Both hypotheses are based on demand. The Trust Hypothesis is based on the donors' demands for trust, and the Heterogeneity Hypothesis is based on non-median voters' demands for social goods; neither integrates supply-side factors into their predictions.

Scholars' reliance on demand-side influences is an incomplete construction of reality. As the 2011 State of the Sector Survey (Nonprofit Finance Fund, 2011) reported, 54% of 1,935 responding nonprofits indicated an inability to meet expected demand for service in 2011. This is an increase from the 44% and 49% of respondents who claimed they were unable to meet demand in 2009 and 2010 respectively (Frazier, 2011; Nonprofit Finance Fund, 2011). Respondents to the 2011 survey asserted, as they have in the past, difficulty in acquiring additional resources limits their organizations from fulfilling demand for their services. Thus, supply-side environmental conditions need to be integrated into theory which predicts the formation of nonprofit organizations.

This study intends to fulfill this need. Specifically, it seeks to understand if financial capital and intellectual capital influence the formation of nonprofit organizations beyond the predictions of the Heterogeneity Hypothesis. The inspiration for including these supply-side factors derives from the processes of entrepreneurship - the acquisition and combination of resources by enterprising people for the purpose of exploiting perceived opportunity (Bull & Willard, 1993; Chell, 2007; Clifford, 2004; Cunningham & Lischeron, 1991; Granovetter, 1995; Hitt, Ireland, Camp, & Sexton, 2001; Jacobson, 2003). Financial capital replicates the abundance of resources in the environment while intellectual capital accounts for the prevalence of enterprising individuals. By amending supply-side factors to the Heterogeneity Hypothesis, this research presents a balanced view of nonprofit organizations; nonprofits fulfill social needs *when* necessary resources are available.

In addition to building nonprofit theory, this research has social importance. Social goods (e.g. safety, public health, arts and culture, education, environmental preservation) represent the foundation

by which other economic activity occurs. However, recent declines in tax revenue stemming from economic stagnation have threatened the stability of social goods provided by and funded through government agencies. The nonprofit organizational form offers an alternative method of providing social goods. Through favorable tax treatments, nonprofits have a lower cost structure which improves the economic viability of the social goods they produce. Yet taxing authorities routinely scrutinize nonprofits to justify their tax advantages - every nonprofit represents a forfeited taxing opportunity to fund alternative social goods produced by the public sector. Hence, theory and empirical research which confirms the contexts suited to nonprofit formation provides social value.

#### Nonprofit Theory

Theories explaining the need for the nonprofit organizational form are based on market failure and demand by non-median voters (Salamon, 1987). The former is associated with the Trust Hypothesis and the latter with the Heterogeneity Hypothesis (Kingma, 2003; Ortmann & Schlesinger, 2003).

The market failure explanation is credited to Hansmann (1980) who stated nonprofit forms are suited for transactions where buyers (i.e. those providing revenue to the organization) have difficulty assessing product quality and price, forming clear exchange contracts, determining contract fulfillment, and remedying contract disputes. Social goods, where consumption is not excluded or reduced by the consumption of others (Krashinsky, 1997), are especially prone to such market failures (Easley & O'Hara, 1983; Kingma, 2003). For example, donors to a nonprofit charged with providing health care to the impoverished are unlikely to observe the diagnostic and treatment service performed and, as a result, are limited in their abilities to appraise the nonprofit's effectiveness or efficiency. Thus, nonprofit managers have opportunity to be dishonest. That is, they could exploit their information advantage over resource suppliers (e.g. donors, government agencies) by increasing compensation, perquisites, or organizational surpluses at the expense of mission-related causes. The nonprofit form, however, intends to create trust. Private inurement and compensation restrictions provide assurance to resource suppliers that nonprofit managers lack opportunity and motivation to expropriate organizational resources. Conversely, for-profit organizations do not have such restrictions and, as a result, have fewer alternatives to earn trust from potential resource suppliers.

However, as Krashinsky (1986) discussed, market failure does not distinguish the need for nonprofits. All firms exist to reduce the transaction costs associated with market failure (Coase, 1937). For-profits too can leverage information asymmetries and sacrifice product quality for the sake of organizational profits. Competitive forces pressure for-profits to limit such exploitation. Krashinsky stated the anecdotal examples used by Hansmann to support his theory indicate the true advantage of nonprofits is when buyers are distinct from consumers (e.g. healthcare, daycare, and education) or opportunities are available for “free-riders” - those who consume without paying. In the first case, buyers who do not consume have difficulty monitoring product quality and comparing alternative offerings. Buyers will prefer the nonprofit form because private inurement restrictions suggest nonprofit managers have no motivation to sacrifice quality. The for-profit form would require buyers to assume the additional cost of monitoring product quality and delivery. In the second case, the cost of free-riders (i.e. the value of non-reimbursed goods or services) needs to be covered by alternative sources such as donors, government agencies, or fee-for-service clients. Again, the private inurement and compensation restrictions of nonprofits assure these individuals and entities that their supplemental contributions to cover the cost of free-riders will not be allocated towards profit margins or managers’ private interests. For-profit organizations that lack mandates regarding private inurement and compensation cannot provide similar promises and, as a result, are less effective in attracting supplemental revenue to recover the costs of free-riders.

Yet trust could be provided through means other than the nonprofit form. As Krashinsky (1986) noted, numerous methods are available to control deviant behavior: regulations, professional associations, insurance policies, and the legal system all offer mechanisms of deterrence and justice. Thus, the fact that nonprofits exist despite alternative means of providing trust to resource suppliers suggest nonprofit theory needs to integrate supplemental factors. The Heterogeneity Hypothesis fills this need.

The Heterogeneity Hypothesis<sup>2</sup> is credited to Weisbrod (1975) and emphasizes the demand for social goods by the non-median voter. The theory asserts nonprofits fulfill demand not served by the output of for-profit organizations or government agencies (Langton, 1987). For-profits meet the demand

<sup>2</sup> Also termed the “output hypothesis” by Weisbrod.



for economically viable private goods while government agencies employ tax mandates to make otherwise non-profitable social goods available. However, the range of goods provided by the government will only be those supported by the median voter. Social goods demanded by non-median voters will not be provided by government agencies because they lack political support. Hence, Weisbrod concluded the presence and abundance of nonprofits depends on the heterogeneity of demand for social goods. If the demand for social goods is relatively homogenous, then the median voter accurately represents all demand for social goods and government agencies have the support necessary to satisfy said demand. In such circumstances, the need for nonprofits is reduced. However, as the demand for social goods becomes increasingly heterogeneous, a greater proportion of demand is not represented by the median voter and, in turn, not served by government agencies. In these environments nonprofits emerge to fulfill the unmet demand for social goods.

Numerous studies used demographic traits to represent the heterogeneity of demand for social goods and supported Weisbrod's Heterogeneity Hypothesis. Gross (1995) grouped respondents according to multiple demographic traits (e.g. religion, ethnicity, family, income, and education) and associated some groupings with distinct preferences for public education. James (1993) found heterogeneity of income and culture across countries increases the proportion of nonprofits providing education. Feigenbaum (1980) found income, education, and age diversity affects government entities' and individuals' philanthropic activity which, is presumed, increases the size of the nonprofit sector and later Chang and Tuckman (1996) linked racial diversity to nonprofits' output mix: the proportion of mission-related to non-mission-related outputs. An important extension of the Heterogeneity Hypothesis is provided by Ben-Ner and van Hoomissen (1991) who asserted a necessary amount of "social cohesion" by non-median voters is necessary to generate nonprofits. That is, the heterogeneity of demand for social goods creates a need for nonprofits, but a threshold amount of consensus amongst non-median voters is necessary to support the formation of a nonprofit.

#### Theoretical Framework

This research builds from Ben-Ner and van Hoomissen's (1991) finding and asserts their model of nonprofit formation is positively influenced by the availability of financial and intellectual capital in the

community. The inclusion of financial and intellectual capital is based on the process of entrepreneurship. Entrepreneurship is defined as *enterprising people* gathering *resources* to exploit perceived *opportunity* (Bull & Willard, 1993; Chell, 2007; Clifford, 2004; Cunningham & Lischeron, 1991; Granovetter, 1995; Jacobson, 2003; Morris, Kurato, & Schindehutte, 2001). In the context of nonprofits, the trust and heterogeneity hypotheses suggest *opportunity* is the demand for social goods which emerges from buyers' inability to monitor product quality and non-median voters' needs. However, fulfilling the demand for social goods is limited by the availability of resources and enterprising people. This study's inclusion of financial capital intends to capture the *resource* constraint while its inclusion of intellectual capital intends to capture the presence of *enterprising people* who recognize and exploit opportunities (Peña, 2002; Ramos-Rodríguez, Medina-Garrido, Lorenzo-Gómez, & Ruiz-Navarro, 2010). Thus, whereas Ben-Ner and Hoomissen found a convergence of non-median voters was needed to start a nonprofit, this application contends nonprofit formation is also dependent on the availability of financial and intellectual capital.

The model presented here specifically applies to "donative entrepreneurial" (Hansmann, 1980) nonprofits where the organization is reliant on donations, subject to the non-distribution constraint, focused on the provision of services rather than grant-making (e.g. foundations or donor-advised funds), and not managed by consumers, members, or patrons. Donative nonprofits distribute services to beneficiaries and rely on donors to a critical degree for revenues. Hence, nonprofit buyers (i.e. donors) are frequently distinct from nonprofit consumers (i.e. beneficiaries). Donative nonprofits, in effect, redistribute resources. Individuals, social groups, insurers, and business entities with resources make contributions and payments to produce a social good. The enterprising people who start donative nonprofits have successfully identified the social good in demand, located those with the necessary resources, and executed a plan to create sufficient willingness-to-pay by those with the resources.

The amendment of supply-side factors to nonprofit theory produces the five relationships (including two hypotheses) depicted in Figure 1. The demand side relationships capture the Heterogeneity Hypothesis (Weisbrod, 1975), social cohesion dynamics (Ben-Ner & van Hoomissen, 1991), and “crowding out” (Andreoni & Payne, 2001, 2011). The supply side relationships contain predictions for the influence on financial and intellectual capital on nonprofit formation.

The relationship between demand heterogeneity and nonprofit formation replicates the

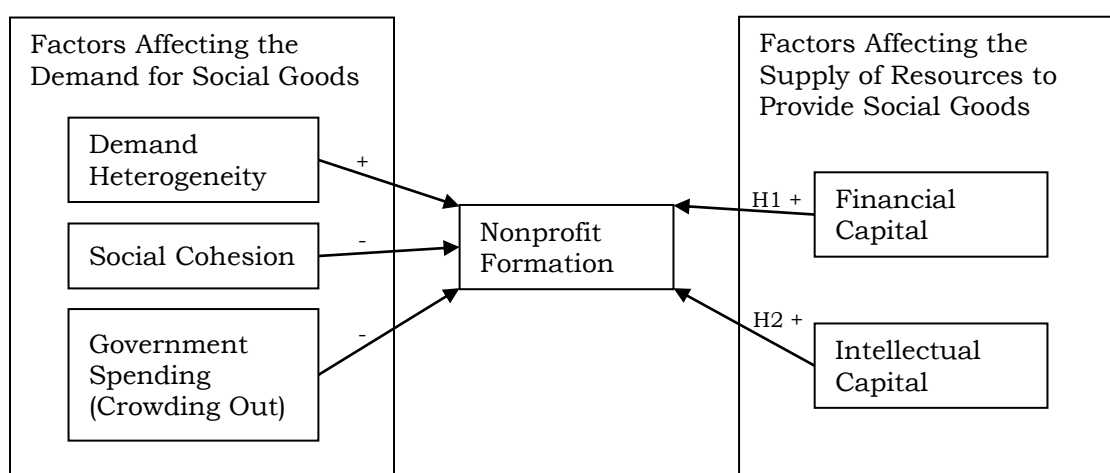


Figure 1 – Nonprofit Formation

Heterogeneity Hypothesis while the inclusion of “social cohesion” captures a nuance of the heterogeneity purported by Ben-Ner and van Hoomissen (1991). They argued that at high levels of demand heterogeneity, the demand for social goods is too diverse for the needed services to be recognized or delivered through economically viable means. At low levels of demand heterogeneity, the demand for social goods is shared by the median voter and government agencies have the necessary support to implement tax mandates and program allocations. However, at moderate levels of demand heterogeneity, the demand for social goods has enough uniformity to make service provision economical but not enough to be supported by the median voter and, in turn, provided by the public sector. Hence, moderate levels of demand heterogeneity will have the strongest influence on nonprofit formation.

Government spending is another factor influencing the demand for social goods and, in turn, nonprofit formation. Again, the Heterogeneity Hypothesis asserts nonprofits emerge and exist to fulfill unmet demand for social goods not provided by the public sector. Greater government spending increases the amount of social goods provided by the public sector which creates a corresponding decrease in the amount of unmet demand for social goods. As unmet demand declines, fewer nonprofits should form. Thus, government spending has a “crowding out” effect on nonprofits. Andreoni and Payne (2001, 2011) offer a supplemental interpretation of “crowding out.” They suggested government spending causes potential donors to reduce or redirect gifts away from grant-receiving nonprofits since, as donors perceive, the financial need of such nonprofits has been remediated by the grant. In sum, then, government spending reduces the likelihood of nonprofits by reducing the amount of unmet demand for social goods and discouraging private donors from supporting nonprofit organizations.

The first hypothesis presented tests the influence of financial capital as a supply-side determinant of nonprofit formation. Financial capital is a critical component of forming an organization (Austin, Stevenson, & Wei-Skillern, 2006; Gavin, 2004; Lee, Lee, & Pennings, 2001; Meyskens, Robb-Post, Stamp, Carsrud, & Reynolds, 2010; Morris, et al., 2001; Orser, Riding, & Manley, 2006; Riding, Haines, & Thomas, 1994) and research has associated organizational growth and survival with the initial amount of financial capital acquired by a new firm (Alsos, Isaksen, & Ljunggren, 2006; Cooper, Gimeno-Gascon, & Woo, 1994; Gavin, 2004; Hellmann & Puri, 2002; Meyskens, et al., 2010). Higher levels of initial financial capital allow new organizations to better withstand environmental downturns (Kuratko & Mathews, 2004), attract partnerships (Lee, et al., 2001; Meyskens, et al., 2010), and commit to innovation (Meyskens, et al., 2010). Furthermore, organizations are more likely to form in locations where financial capital is more abundant, available, and accessible (Alsos, et al., 2006; Decker, Kuhlmann, & Wohar, 2008; Reynolds; Reynolds, Storey, & Westhead., 1995; Sutaria & Hicks., 2004). As Uzzi (1999) explained, proximity to financial capital increases the likelihood that the new organization’s managers are within the social network of those who act as gatekeepers of financial resources. The closeness of the new organization to its financial backers means their collective values, beliefs, and assumptions about the

competitive environment are more likely to be congruent and monitoring costs for capital providers are reduced. The above justifies hypothesis 1.

*Hypothesis 1. Greater availability of financial capital increases the formation of nonprofits.*

The second hypothesis incorporates intellectual capital and applies similar relationships and logic. Again, intellectual capital is understood as a critical component of competitive advantage (Becker, 1964). Substantial value of intra- and inter-organizational networks is derived from their ability to acquire, develop, create, and leverage stocks of intellectual capital (Adler & Kwon, 2002; Burt, 1997; Kogut & Zander, 1992; Nahapiet & Ghoshal, 1998). For new firms, greater initial stocks of intellectual capital provide advantages with entrepreneurial motivation, problem solving, and attracting investors (Hayton, 2005; Peña, 2002; Truls, 2002). As confirmation, many studies have linked organizations' intellectual capital to their survival and growth rates (e.g. Bates, 1995; Hay & Ross, 1989; Hayton, 2005; Peña, 2002). Others provide evidence that new firms seek regions with more abundant intellectual capital to experience its advantages. Reynolds (1995) associated new venture formation with regional educational attainment measures and Zucker, Darby, & Brewer (1998) connected the location and timing of new biotech businesses with the presence of exceptional intellectual capital. Hence, the emergence of nonprofits, as predicted by the heterogeneity of demand, is reinforced by the availability of intellectual capital in the environment.

*Hypothesis 2. Greater availability of intellectual capital increases the formation of nonprofits.*

## Methodology

### *Data and Sample*

The central unit of analysis in this study is a US state. Within each state, the number of registered charities [501(C)(3)] as a proportion of the total number of organizations within an industry is observed. The study period extends from 2004 to 2007, incorporates seventeen industries (see Table 2), and contains 3,380 observations<sup>3</sup>.

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<sup>3</sup> Seventeen industries in fifty states over four years; less twenty records with unavailable data.

The data to construct variables come from the National Center for Charitable Statistics, the US Department of Commerce's Bureau of Economic Analysis, the US Census Bureau, the US National Science Foundation, the US Patent and Trademark Office, the US Department of Education's Institute of Education, the US Bureau of Labor Statistics, and the US Department of Health and Human Services' Centers for Medicare and Medicaid Services.

#### *Dependent Variable*

The dependent variable (*NPO Establishments*) is the proportion of charities to all organizations in a given state and industry. The National Center of Charitable Statistic's database identified how many charities within a National Taxonomy of Exempt Entity (NTEE) category were in each state. The US Census Bureau database then identified the total number of organizations within a specified category of the North American Industry Classification System (NAICS). Table 2 indicates how NTEE codes are grouped according to NAICS delineations.

An inverse transformation is applied to the dependent variable to improve its skewness and kurtosis. The resulting measure is then subtracted from a constant to make the direction and interpretation of the variable consistent with the hypotheses.

*Table 2 – Alignment of NAICS and NTEE industry codes<sup>4</sup>*

NAICS		National Taxonomy of Exempt Organizations	
611110	Elementary and Secondary Schools	<i>B20</i>	<i>Elementary &amp; Secondary Schools</i>
		<i>B24</i>	<i>Primary &amp; Elementary Schools</i>
		<i>B25</i>	<i>Secondary &amp; High Schools</i>
		<i>B29</i>	<i>Charter Schools</i>
611310	Colleges, Universities, and Professional Schools	<i>B40</i>	<i>Higher Education</i>
		<i>B42</i>	<i>Undergraduate Colleges</i>
		<i>B43</i>	<i>Universities</i>
		<i>B50</i>	<i>Graduate and Professional Schools</i>
611510	Technical & Trade Schools	<i>B30</i>	<i>Vocational &amp; Technical Schools</i>
611610	Fine Arts Schools	<i>A25</i>	<i>Arts Education</i>
		<i>A6E</i>	<i>Performing Arts Schools</i>
611699	All Other Miscellaneous Schools & Instruction	<i>B28</i>	<i>Special Education</i>
		<i>B60</i>	<i>Adult Education</i>
611710	Educational Support Services	<i>B80</i>	<i>Student Services</i>
		<i>B90</i>	<i>Educational Services</i>

<sup>4</sup> Grouping provided by the National Center of Charitable Statistics

NAICS		National Taxonomy of Exempt Organizations	
		B92	Remedial Reading & Encouragement
		Q20	Promotion of International Understanding
		Q21	International Cultural Exchange
		Q22	International Academic Exchange
		Q23	International Exchange N.E.C. <sup>5</sup>
621340	Offices of Physical, Occupational and Speech Therapy	E50	Rehabilitative Care
		E30	Ambulatory & Primary Health Care
		E32	Community Clinics
		F50	Addictive Disorders N.E.C.
		F52	Smoking Addiction
		F53	Eating Disorders & Addictions
		F54	Gambling Addiction
		F60	Counseling
		F70	Mental Health Disorders
		F99	Mental Health & Crisis Intervention N.E.C.
621340	Offices of Physical, Occupational and Speech Therapy	E50	Rehabilitative Care
		E30	Ambulatory & Primary Health Care
		E32	Community Clinics
		F50	Addictive Disorders N.E.C.
621498	All Other Outpatient Care Centers	E20	Hospitals
		E21	Community Health Systems
		E22	General Hospitals
622310	Specialty Hospitals (except Psychiatric and Substance Abuse)	E24	Specialty Hospitals
		E90	Nursing
		E91	Nursing Facilities
		P74	Hospices
623110	Nursing Care Facilities	A60	Performing Arts
711100	Performing Arts Companies	A65	Theater
711110	Theater Companies & Dinner Theaters	A62	Dance
		A63	Ballet
		A68	Music
		A69	Symphony Orchestras
		A6A	Opera
		A6B	Singing & Choral Groups
		A6C	Bands & Ensembles
711120	Dance Companies	A61	Performing Arts Centers
711310	Promoters of Performing Arts, Sports, and Similar E	A50	Museums
		A51	Art Museums
		A52	Children's Museums
		A54	History Museums
		A56	Natural History & Natural Science Museums
		A57	Science and Technology Museums
712110	Museums		

<sup>5</sup> N.E.C.: "Not Elsewhere Classified"

### *Independent Variables*

Financial capital (*Financial Capital*) is measured as the percentage of the state's population having income which exceeds \$100,000. The measure derives from personal income because gifts from individuals constitute roughly 75% of all giving (Center on Philanthropy at Indiana University, 2009, 2010, 2011) and \$100,000 is selected as the threshold because members of this income bracket, while representing a minority of the population, provide the majority of donations (in dollars) to nonprofits (Rooney, 2007; Roper Center for Public Opinion Research, 2006).

According to Hervas-Oliver and Dalmau-Porta (2007), the intellectual capital in an environment is based on technological, educational, governmental, and social factors. Their framework is applied here because of its conceptual rigor and orientation towards the underpinning competitive environments rather than specific industries or organizations. The technological and educational factors come from the ideas-driven endogenous growth theory (Romer, 1990) where the stock of human capital determines how investments create regional, economic growth. Governmental factors capture efforts to advance national innovation systems (Nelson, 1993) and social factors derive from cluster-based theory (Almeida & Kogut, 1999; Porter, 1990) where linkages based on micro and macro level interaction, integration, and competition foster the exchange, combination, and development of knowledge. Hervas-Oliver and Dalmau-Porta's (2007) factors related to government policy are excluded because states' general position towards free market competition, as reflected in economic freedom indexes from the Frazier Institute and Mercatus Center, strongly correlates with per capita government spending - a control variable in this study. Intellectual capital (*Intellectual Capital*) is the sum of the standardized values for each factor. The technology factor integrates patents (per 100,000 individuals) and research intensity (research and development expenditures as a percentage of Gross State Product – GSP). The sum of the standardized values for patents and research intensity becomes the proxy for the technology component of intellectual capital. The educational factor sums the standardized values for public expenditures per capita, enrollment percentages for secondary school, the percentage of the population over age eighteen with undergraduate degrees, and the percentage of the population over age eighteen with graduate degrees. Finally, the social factor is the standardized value of health expenditures as a percentage of GSP.



### Control Variables

The heterogeneity of demand (*Demand Heterogeneity*) for social goods is measured using demographic traits employed by others including age (Bielefeld, 2006; Bielefeld & Murdoch, 2004), income (inverted Gini index) (Bielefeld, 2006; Bielefeld & Murdoch, 2004; Chang & Tuckman, 1996; Deaton, 1997; Feigenbaum, 1980; Kingma, 2003; Weisbrod, 1975, 1986), and race (Bielefeld, 2006; Bielefeld & Murdoch, 2004; Chang & Tuckman, 1996). The calculation for each heterogeneity measure follows:

Age	$1 - \sum_{i=1}^n \left( \frac{\text{Age Cohort Population}_i}{\text{Total Population}} \right)^2$	Age Cohorts are 0 to 10, 11 to 20, 21 to 30, ..., 61 to 70, and 71 and older.
Income	$1 - \left( \frac{N+1}{N-1} - \frac{2}{N(N-1)\mu} \left( \sum_{i=1}^n P_i X_i \right) \right)$	Where $\mu$ is the population mean, $P_i$ is the rank of person $i$ with income $X$ ; highest income is ranked as 1 and the lowest income is given a rank of $N$ . (Deaton, 1997)
Race	$1 - \sum_{i=1}^n \left( \frac{\text{Racial Group Population}_i}{\text{Total Population}} \right)^2$	Racial Groups are Asian, Black, Multi-Racial, Native American, Pacific Islander, and White.

The three demographic measures are standardized and summed to create a single value. Ben-Ner and van Hoomissen's (1991) conception of "social cohesion" (*Social Cohesion*) is accounted for by squaring the demand heterogeneity value. This allows an inverted-U relationship between demand heterogeneity and nonprofit formation to be identified.

Gross state and local governmental spending per capita is the applied measure of government spending (*Government Spending*). The variable's skewness and kurtosis are corrected through an inverse transformation which is then subtracted from a constant to retain the asserted directionality of "crowding out" (Andreoni & Payne, 2001, 2011).

Finally, the effect of urbanization was controlled because new entities are more likely to form in densely populated and growing areas (Bartik, 1989; Wagner & Sternberg, 2004). The measure of urbanization (*Urban Growth*) applied is the percentage change in the urban population by state.

### Analysis

The proportion of charities to total establishments was estimated using ordinary least squares regression (OLS) multiple regression analysis. For each industry, a reduced model (Model I) incorporates *Demand Heterogeneity, Social Cohesion, Government Spending, and Urban Growth*. Accordingly, the analysis confirms or contests the accuracy of the Heterogeneity Hypothesis (positive coefficient), Ben-Ner and van Hoomissen's (1991) social cohesion principle (negative coefficient), and "crowding out" dynamics (negative coefficient) (Andreoni & Payne, 2001, 2011).

Hypotheses 1 and 2 are tested through regression models II, III, and IV. Significant and positive coefficients for *Financial Capital* in models II and IV offer support for hypothesis 1 while significant and positive coefficients for *Intellectual Capital* in models III and IV provide support for hypothesis 2. Comparing the Fischer ratios of all four models substantiates or retracts the evidence provided by significant coefficients.

### Results

Table 3 provides descriptive statistics. Evidence of multicollinearity amongst variables is absent; variance inflation factors (VIF) range from 1.01 to 1.77. Within each industry, models I through IV in Table 4 show the main effects of Demand Heterogeneity. As stated earlier, the framework begins with Weisbrod's Heterogeneity Hypothesis. Accordingly, model I incorporates the heterogeneity of demand, social cohesion, and government spending. Through model II, the Heterogeneity Hypothesis is amended to include financial capital. Similarly, model III considers the influence of intellectual capital. Finally, model IV, the full model, simultaneously accounts for financial and intellectual capital to predict the emergence of nonprofit organizations. All models include an intercept because a scenario where the independent variables are zero; demand for social goods is perfectly homogeneous, government spending per capita is zero, urban residence is unchanged, affluence is absent, and intellectual capital is missing; is not realistic.

Table 3 – Descriptive Statistics and Correlation Matrix

Variable	Mean	Std. Deviation	N	1	2	3	4	5	6
1 NPO Establishments	0.70	3.15	3380						
2 Demand Heterogeneity <sup>a</sup>	0.00	1.19	3400	.005					
3 Social Cohesion	1.42	2.59	3400	-.021	.085 **				
4 Government Spending	5354.01	1477.94	3400	.002	.107 **	.068 **			
5 Urban Growth	0.01	0.03	3400	.012	-.049 **	.005	-.043 *		
6 Financial Capital	0.16	0.06	3400	.019	.024	.238 **	.351 **	.177 **	
7 Intellectual Capital <sup>b</sup>	0.00	1.67	3400	.054 **	-.180 **	-.108 **	.265 **	-.154 **	.475 **

\*\* Correlation is significant at the 0.01 level (2-tailed).

a Demand Heterogeneity is the sum of standardized values for age diversity, race diversity, and income inequality.

b Intellectual Capital is the sum of standardized values representing public spending on education, secondary school enrollment, bachelor degrees, graduate degrees, and health care expenditures.

Table 5 summarizes how each industry's best-fit regression model in Table 4 supports or refutes the hypotheses. The determinations shown were formed by reviewing the value and statistical significance of standardized coefficients and Fischer ratios.

Hypothesis 1, which predicts a positive coefficient for *Financial Capital*, is supported in the General Medical & Surgical Hospitals industry and the Specialty Hospitals industry. A statistically significant, *negative* coefficient appears in three industries: All Other Miscellaneous Schools & Instruction, All Other Outpatient Care Centers, and Musical Groups & Artists. The related distinction between these groupings is their asset base. The two confirming industries have nonprofit members with average asset bases of over \$8.8M while the average asset base of the nonprofits in the three refuting industries ranges from roughly \$39,000 to \$499,000. Reason suggests financial capital in the environment is more important to nonprofit formation in asset-intense industries.

Hypothesis 2 is supported through positive coefficients for *Intellectual Capital*. The coefficients for the regression models in eight industries support this hypothesis while negative coefficients in four other industries indicate the relationship predicted should be inverted. Educational Support Industries; Nursing Care Facilities; Promoters of Performing Arts, Sports, & Similar Events; and Museums are the dissenting industries. Technical & Trade Schools, Performing Arts Companies, Theater Companies & Dinner Theaters, Dance Companies, All Other Outpatient Care Centers, General Medical & Surgical

Table 4 - Predictors of NPO Establishments

Independent Variable	611110 Elementary and Secondary Schools				611310 Colleges Universities and Professional Schools			
	Model I	Model II	Model III	Model IV	Model I	Model II	Model III	Model IV
(Constant)	-0.025	-0.028	-0.022	-0.023	-0.006	0.002	-0.004	0.013
Std. Error	0.075	0.075	0.075	0.076	0.074	0.074	0.074	0.074
B	0.035	0.033	0.017	0.018	-0.008	-0.004	-0.021	-0.033
Std. Error	0.071	0.071	0.074	0.074	0.070	0.070	0.073	0.073
Heterogeneity	0.035	0.033	0.017	0.018	-0.008	-0.004	-0.021	-0.033
B	0.025	0.029	0.022	0.023	0.006	-0.002	0.004	-0.013
Std. Error	0.027	0.028	0.027	0.029	0.027	0.028	0.027	0.028
Beta	0.065	0.074	0.056	0.059	0.015	-0.004	0.009	-0.033
B	-0.207 **	-0.190 *	-0.176 *	-0.174 *	0.255 **	0.219 **	0.278 **	0.249
Std. Error	0.073	0.079	0.080	0.082	0.072	0.078	0.079	0.081
Beta	-0.208	-0.190	-0.177	-0.175	0.256	0.220	0.279	0.249
B	-0.108	-0.096	-0.113	-0.110	-0.023	-0.047	-0.027	-0.073
Std. Error	0.072	0.075	0.072	0.077	0.071	0.074	0.071	0.076
Beta	-0.108	-0.096	-0.113	-0.110	-0.023	-0.047	-0.027	-0.073
B	-0.044	-0.044	-0.044	-0.044	0.092	0.092	0.156	0.156
Std. Error	0.080	0.080	0.080	0.092	0.079	0.079	0.090	0.090
Beta	-0.044	-0.044	-0.044	-0.044	0.092	0.092	0.156	0.156
B	-0.069	-0.069	-0.069	-0.069	-0.055	-0.055	-0.055	-0.131
Std. Error	0.091	0.091	0.091	0.091	0.079	0.079	0.079	0.090
Beta	-0.069	-0.069	-0.069	-0.069	-0.055	-0.055	-0.055	-0.131
N	200	200	200	200	200	200	200	200
Adj. R2	0.027	0.023	0.026	0.021	0.050	0.051	0.047	0.057
ΔR2 (Model I)	0.001	0.001	0.004	0.004	0.006	0.006	0.002	0.017
F Ratio	2.378	1.956	2.073	1.721	3.600 **	3.157 **	2.969 *	3.001 **

\* p &lt; .05

\*\* p &lt; .01

Table 4 - Predictors of NPO Establishments (Continued)

Independent Variable	61151 Technical and Trade Schools				611610 Fine Arts Schools			
	Model I	Model II	Model III	Model IV	Model I	Model II	Model III	Model IV
(Constant)	0.070	0.091	0.054	0.065	-0.015	-0.017	-0.021	-0.032
Std. Error	0.072	0.070	0.068	0.069	0.062	0.062	0.061	0.062
B	0.034	0.046	0.122	0.115	-0.010	-0.011	0.020	0.027
Std. Error	0.069	0.067	0.067	0.067	0.059	0.059	0.061	0.061
Heterogeneity	0.034	0.046	0.122	0.115	-0.010	-0.011	0.020	0.027
Beta								
B	-0.070 **	-0.091 **	-0.054 *	-0.065 *	0.015	0.017	0.021	0.032
Std. Error	0.026	0.026	0.025	0.026	0.022	0.023	0.022	0.024
Beta	-0.182	-0.237	-0.140	-0.169	0.040	0.044	0.054	0.083
B	0.165 *	0.063	0.014	-0.006	0.461 **	0.469 **	0.410 **	0.430 **
Std. Error	0.070	0.074	0.073	0.074	0.060	0.066	0.066	0.067
Beta	0.166	0.063	0.014	-0.006	0.462	0.470	0.410	0.431
B	-0.195 **	-0.263 **	-0.169 *	-0.201 **	-0.276 **	-0.271 **	-0.267 **	-0.236 **
Std. Error	0.069	0.070	0.066	0.070	0.059	0.062	0.059	0.063
Beta	-0.195	-0.263	-0.169	-0.201	-0.276	-0.271	-0.267	-0.236
B	0.258 **	0.258 **		0.106	-0.020	-0.020		-0.106
Std. Error	0.075	0.075		0.083	0.066	0.066		0.075
Beta	0.258	0.258		0.107	-0.020	-0.020		-0.106
B			0.360 **	0.308 **			0.122	0.174 *
Std. Error			0.072	0.083			0.065	0.075
Beta			0.361	0.309			0.123	0.174
N	200	200	200	200	200	200	200	200
Adj. R2	0.094	0.142	0.192	0.195	0.335	0.332	0.344	0.347
ΔR2 (Model I)		0.051 **	0.100 **	0.107 **		0.000	0.012	0.018
F Ratio	6.143 **	7.569 **	10.459 **	9.018 **	26.076 **	20.782 **	21.831 **	18.619 **

\* p &lt; .05

\*\* p &lt; .01

Table 4 - Predictors of NPO Establishments (Continued)

Independent Variable	611699 All Other Miscellaneous Schools and Instruction				611710 Educational Support Services			
	Model I	Model II	Model III	Model IV	Model I	Model II	Model III	Model IV
(Constant)	0.101	0.074	0.112	0.087	0.007	0.000	0.019	0.025
Std. Error	0.071	0.068	0.069	0.068	0.073	0.073	0.071	0.072
Demand	0.242 **	0.227 **	0.177 **	0.195 **	0.209 **	0.205 **	0.143 *	0.138
Std. Error	0.067	0.065	0.068	0.067	0.070	0.070	0.070	0.070
Heterogeneity	0.242	0.227	0.177	0.195	0.209	0.205	0.143	0.138
B	-0.101 **	-0.075 **	-0.113 **	-0.087 **	-0.007	0.000	-0.019	-0.025
Std. Error	0.026	0.025	0.025	0.026	0.026	0.027	0.026	0.028
Social Cohesion	-0.263	-0.194	-0.293	-0.226	-0.017	0.001	-0.048	-0.065
Beta	-0.127	-0.002	-0.017	0.030	-0.003	0.031	0.110	0.098
Government	0.069	0.072	0.073	0.074	0.071	0.077	0.076	0.078
Spending	-0.128	-0.002	-0.017	0.030	-0.003	0.031	0.110	0.099
B	-0.151 *	-0.068	-0.170 *	-0.097	-0.200 **	-0.177 *	-0.220 **	-0.238 **
Std. Error	0.068	0.068	0.066	0.069	0.070	0.073	0.068	0.073
Urban Growth	-0.151	-0.068	-0.170	-0.097	-0.200	-0.177	-0.220	-0.238
Beta	-0.317 **	0.072	-0.246 **	-0.246 **	-0.086	0.078	0.061	0.061
Financial	0.072	-0.318	0.082	0.082	0.087	0.078	0.087	0.087
Capital	-0.318	-0.318	-0.247	-0.247	-0.087	-0.087	-0.061	-0.061
B	-0.265 **	-0.265 **	-0.265 **	-0.144	-0.270 **	-0.300 **	-0.270 **	-0.300 **
Std. Error	0.073	0.073	0.073	0.082	0.075	0.075	0.075	0.087
Intellectual	-0.265	-0.265	-0.265	-0.144	-0.271	-0.301	-0.271	-0.301
Capital	Beta							
N	200	200	200	200	200	200	200	200
Adj. R2	0.128	0.203	0.179	0.211	0.069	0.070	0.122	0.120
ΔR2 (Model I)	0.078 **	0.078 **	0.054 **	0.090 **	0.006	0.006	0.057 **	0.059 **
F Ratio	8.285 **	11.128 **	9.668 **	9.884 **	4.660 **	3.979 **	6.520 **	5.502 **

\* p &lt; .05

\*\* p &lt; .01

Table 4 - Predictors of NPO Establishments (Continued)

Independent Variable	621340 Offices of Physical Occupational and Speech Therapy				621498 All Other Outpatient Care Centers			
	Model I	Model II	Model III	Model IV	Model I	Model II	Model III	Model IV
(Constant)	0.011	0.017	0.004	0.003	-0.026	-0.038	-0.031	-0.060
Std. Error	0.076	0.077	0.076	0.077	0.074	0.074	0.074	0.073
Demand	0.047	0.050	0.088	0.088	0.214 **	0.206 **	0.243 **	0.263 **
Std. Error	0.073	0.073	0.075	0.075	0.070	0.070	0.073	0.072
Heterogeneity	0.047	0.050	0.088	0.088	0.214	0.206	0.243	0.263
B	-0.011	-0.017	-0.004	-0.003	0.026	0.038	0.031	0.060 *
Std. Error	0.028	0.028	0.028	0.029	0.027	0.027	0.027	0.028
Beta	-0.029	-0.045	-0.010	-0.007	0.067	0.100	0.081	0.157
Government	-0.005	-0.034	-0.074	-0.073	0.078	0.138	0.027	0.080
Std. Error	0.074	0.081	0.081	0.083	0.072	0.078	0.079	0.079
Beta	-0.005	-0.034	-0.075	-0.073	0.078	0.138	0.027	0.080
Urban Growth	-0.055	-0.074	-0.043	-0.040	0.007	0.047	0.016	0.098
Std. Error	0.073	0.076	0.073	0.078	0.071	0.074	0.071	0.074
Beta	-0.055	-0.074	-0.043	-0.040	0.007	0.047	0.016	0.098
Financial		0.075		-0.009		-0.151		-0.278 **
Std. Error		0.081		0.093		0.078		0.088
Beta		0.076		-0.009		-0.152		-0.278
Intellectual			0.167 *	0.171			0.121	0.257 **
Std. Error			0.080	0.093			0.078	0.088
Beta			0.167	0.171			0.121	0.258
N	200	200	200	200	200	200	200	200
Adj. R2	-0.015	-0.015	0.002	-0.003	0.046	0.059	0.052	0.094
ΔR2 (Model I)		0.004	0.022 *	0.022		0.018	0.011	0.057 **
F Ratio	0.288	0.402	1.094	0.908	3.373 *	3.483 **	3.195 **	4.439 **

\* p &lt; .05

\*\* p &lt; .01

Table 4 - Predictors of NPO Establishments (Continued)

Independent Variable	622110 General Medical and Surgical Hospitals				622310 Specialty (except Psychiatric and Substance Abuse)			
	Model I	Model II	Model III	Model IV	Model I	Model II	Model III	Model IV
(Constant)	0.021	0.068	0.001	0.047	0.015	0.029	-0.007	0.011
Std. Error	0.072	0.062	0.065	0.060	0.078	0.076	0.076	0.075
Demand	0.217 **	0.245 **	0.330 **	0.298 **	0.133	0.148 *	0.206 **	0.191 **
Std. Error	0.069	0.058	0.064	0.059	0.073	0.070	0.073	0.072
Heterogeneity	0.217	0.245	0.330	0.298	0.136	0.151	0.211	0.195
B	-0.021	-0.068 **	-0.001	-0.048 *	-0.015	-0.039	0.000	-0.022
Std. Error	0.026	0.023	0.024	0.023	0.028	0.027	0.027	0.028
Beta	-0.055	-0.177	-0.002	-0.124	-0.039	-0.104	0.001	-0.059
Government	0.147 *	-0.076	-0.045	-0.130 *	0.028	-0.104	-0.110	-0.154
Std. Error	0.070	0.065	0.070	0.065	0.078	0.082	0.083	0.084
Spending	0.147	-0.076	-0.045	-0.130	0.028	-0.101	-0.107	-0.150
B	-0.152 *	-0.300 **	-0.119	-0.252 **	0.026	-0.042	0.046	-0.008
Std. Error	0.069	0.061	0.063	0.062	0.082	0.081	0.079	0.081
Beta	-0.152	-0.300	-0.119	-0.252	0.023	-0.038	0.042	-0.008
Financial	0.564 **	0.564 **	0.447 **	0.447 **	0.315 **	0.315 **	0.315 **	0.219 *
Std. Error	0.065	0.065	0.073	0.073	0.079	0.079	0.079	0.089
Capital	0.566	0.566	0.448	0.448	0.317	0.317	0.317	0.221
Intellectual	0.458 **	0.458 **	0.239 **	0.239 **	0.307 **	0.307 **	0.307 **	0.200 *
Std. Error	0.069	0.069	0.073	0.073	0.080	0.080	0.080	0.090
Capital	0.459	0.459	0.240	0.240	0.308	0.308	0.308	0.200
N	200	200	200	200	190	190	190	190
Adj. R2	0.098	0.346	0.260	0.377	0.000	0.075	0.069	0.094
ΔR2 (Model I)	0.246 **	0.246 **	0.163 **	0.280 **	0.078 **	0.078 **	0.073 **	0.102 **
F Ratio	6.408 **	22.019 **	15.000 **	21.065 **	0.991	4.055 **	3.802 **	4.268 **

\* p &lt; .05

\*\* p &lt; .01



Table 4 - Predictors of NPO Establishments (Continued)

Independent Variable	623110 Nursing Care Facilities				7111 Performing Arts Companies			
	Model I	Model II	Model III	Model IV	Model I	Model II	Model III	Model IV
(Constant)	0.037	0.035	0.047	0.061	-0.006	0.003	-0.019	-0.023
B					0.075	0.075	0.073	0.073
Std. Error	0.057	0.058	0.055	0.055				
Demand	-0.020	-0.020	-0.078	-0.087	-0.137	-0.132	-0.066	-0.063
B					0.071	0.071	0.072	0.072
Std. Error	0.055	0.055	0.055	0.054				
Heterogeneity	-0.020	-0.020	-0.078	-0.087	-0.137	-0.132	-0.066	-0.063
Beta								
Social Cohesion	-0.037	-0.036	-0.047 *	-0.061 **	0.006	-0.003	0.019	0.024
B					0.027	0.028	0.026	0.028
Std. Error	0.021	0.021	0.020	0.021				
Beta	-0.096	-0.093	-0.123	-0.159	0.016	-0.008	0.049	0.061
Government	0.632 **	0.638 **	0.731 **	0.706 **	0.149 *	0.106	0.027	0.036
B					0.073	0.079	0.077	0.079
Std. Error	0.056	0.061	0.059	0.060				
Spending	0.633	0.640	0.732	0.707	0.150	0.106	0.028	0.036
Beta								
Urban Growth	0.381 **	0.386 **	0.364 **	0.325 **	-0.076	-0.105	-0.055	-0.042
B					0.072	0.075	0.070	0.075
Std. Error	0.055	0.058	0.053	0.057				
Beta	0.381	0.386	0.364	0.325	-0.076	-0.105	-0.055	-0.042
Financial								
Capital	-0.017	-0.017		0.131	0.109	0.109		-0.045
B					0.080	0.080		0.089
Std. Error	0.061	0.061		0.067				
Beta	-0.017	-0.017		0.131	0.109	0.109		-0.045
Intellectual								
Capital								
B								
Std. Error								
Beta								
N	200	200	200	200	200	200	200	200
Adj. R2	0.425	0.422	0.466	0.474	0.025	0.029	0.087	0.083
ΔR2 (Model I)					0.009	0.009	0.065 **	0.067 **
F Ratio	37.791 **	30.103 **	35.770 **	30.869 **	2.261	2.193	4.785 **	4.014 **

\* p &lt; .05

\*\* p &lt; .01

Table 4 - Predictors of NPO Establishments (Continued)

Independent Variable	711110 Theater Companies and Dinner Theaters				711120 Dance Companies			
	Model I	Model II	Model III	Model IV	Model I	Model II	Model III	Model IV
(Constant)	0.123	0.131	0.107	0.097	0.059	0.066	0.036	0.047
Std. Error	0.071	0.071	0.067	0.067	0.077	0.077	0.078	0.078
B	-0.111	-0.106	-0.024	-0.017	-0.047	-0.040	-0.006	-0.014
Std. Error	0.067	0.067	0.066	0.066	0.072	0.072	0.075	0.075
Beta	-0.111	-0.106	-0.024	-0.017	-0.048	-0.041	-0.006	-0.014
B	-0.124 **	-0.132 **	-0.108 **	-0.097 **	-0.060 *	-0.072 *	-0.051	-0.061 *
Std. Error	0.026	0.026	0.024	0.026	0.027	0.028	0.028	0.029
Beta	-0.321	-0.342	-0.280	-0.253	-0.160	-0.192	-0.135	-0.163
B	0.003	-0.035	-0.145 *	-0.126	-0.079	-0.141	-0.163	-0.178
Std. Error	0.069	0.075	0.071	0.073	0.081	0.087	0.091	0.092
Beta	0.003	-0.035	-0.145	-0.126	-0.075	-0.132	-0.153	-0.167
B	-0.159 *	-0.184 **	-0.134 *	-0.103	0.001	-0.039	0.004	-0.023
Std. Error	0.068	0.071	0.064	0.069	0.078	0.080	0.077	0.081
Beta	-0.159	-0.184	-0.134	-0.103	0.001	-0.037	0.004	-0.022
B	0.096	0.096	0.102	0.102	0.151	0.151	0.151	0.097
Std. Error	0.075	0.075	0.082	0.082	0.081	0.081	0.086	0.092
Beta	0.096	0.096	-0.102	-0.102	0.151	0.151	0.165	0.097
B			0.353 **	0.403 **			0.171 *	0.121
Std. Error			0.071	0.081			0.086	0.099
Beta			0.354	0.404			0.165	0.117
N	200	200	200	200	190	190	190	190
Adj. R2	0.128	0.131	0.222	0.225	0.018	0.031	0.033	0.033
ΔR2 (Model I)		0.007	0.096 **	0.103 **		0.018	0.020 *	0.026
F Ratio	8.292 **	6.982 **	12.376 **	10.604 **	1.853	2.202	2.286 *	2.091

\* p &lt; .05

\*\* p &lt; .01

Table 4 - Predictors of NPO Establishments (Continued)

Independent Variable	711130 Musical Groups and Artists				711310 Promoters of Performing Arts, Sports, and Similar Events			
	Model I	Model II	Model III	Model IV	Model I	Model II	Model III	Model IV
(Constant)	-0.011	-0.029	-0.016	-0.051	0.034	0.018	0.043	0.030
Std. Error	0.073	0.072	0.073	0.071	0.074	0.073	0.073	0.073
Demand	0.060	0.049	0.084	0.109	0.000	-0.010	-0.048	-0.039
Std. Error	0.070	0.069	0.072	0.070	0.070	0.069	0.072	0.072
Heterogeneity	0.060	0.049	0.084	0.109	0.000	-0.010	-0.048	-0.039
Beta								
Social Cohesion	0.011	0.029	0.016	0.051	-0.035	-0.018	-0.043	-0.030
Std. Error	0.027	0.027	0.027	0.027	0.027	0.027	0.027	0.028
Beta	0.029	0.075	0.041	0.133	-0.090	-0.048	-0.112	-0.077
Government	0.279 **	0.362 **	0.237 **	0.302 **	0.148 *	0.225 **	0.230 **	0.254 **
Std. Error	0.071	0.076	0.078	0.077	0.072	0.077	0.078	0.079
Spending	0.279	0.363	0.238	0.303	0.148	0.225	0.230	0.255
Beta								
Urban Growth	0.079	0.135	0.087	0.188 *	-0.172 *	-0.120	-0.186 **	-0.147
Std. Error	0.070	0.072	0.070	0.073	0.071	0.073	0.070	0.075
Beta	0.079	0.135	0.087	0.188	-0.172	-0.120	-0.186	-0.147
Financial		-0.211 **		-0.341 **		-0.195 *		-0.130
Capital		0.077		0.086		0.078		0.089
Beta		-0.211		-0.342		-0.195		-0.130
Intellectual			0.098	0.266 **			-0.196 *	-0.132
Capital			0.078	0.086			0.077	0.089
Beta			0.099	0.266			-0.196	-0.132
N	200	200	200	200	200	200	200	200
Adj. R2	0.067	0.097	0.070	0.135	0.050	0.075	0.076	0.081
ΔR2 (Model I)		0.034 **	0.007	0.076 **		0.029 *	0.030 *	0.039 *
F Ratio	4.558 **	5.282 **	3.978 **	6.186 **	3.622 **	4.234 **	4.252 **	3.920 **

\* p &lt; .05

\*\* p &lt; .01

Table 4 - Predictors of NPO Establishments (Continued)

Independent Variable	712110 Museums				
	Model I	Model II	Model III	Model IV	
(Constant)	B	-0.067	-0.081	-0.052	-0.051
	Std. Error	0.069	0.069	0.065	0.066
Demand Heterogeneity	B	-0.248 **	-0.256 **	-0.334 **	-0.334 **
	Std. Error	0.066	0.065	0.064	0.065
Social Cohesion	Beta	-0.248	-0.256	-0.334	-0.334
	B	0.067 **	0.082 **	0.052 *	0.052 *
Government Spending	Std. Error	0.025	0.025	0.024	0.025
	Beta	0.175	0.212	0.135	0.134
Urban Growth	B	-0.266 **	-0.198 **	-0.119	-0.119
	Std. Error	0.067	0.072	0.070	0.072
Financial Capital	Beta	-0.267	-0.199	-0.119	-0.120
	B	-0.202 **	-0.157 *	-0.227 **	-0.227 **
Intellectual Capital	Std. Error	0.066	0.068	0.063	0.067
	Beta	-0.202	-0.157	-0.227	-0.227
N	B	-0.171 *	-0.171 *	0.002	0.002
	Std. Error	0.073	0.073	0.080	0.080
Adj. R2	Beta	-0.171	-0.171	0.002	0.002
	B	-0.350 **	-0.350 **	-0.351 **	-0.351 **
ΔR2 (Model I)	Std. Error	0.069	0.069	0.069	0.080
	Beta	-0.351	-0.351	-0.352	-0.352
F Ratio	N	200	200	200	200
	Adj. R2	0.167	0.186	0.260	0.256
F Ratio	ΔR2 (Model I)	0.023 *	0.023 *	0.095 **	0.095 **
	F Ratio	10.960 **	10.073 **	14.990 **	12.427 **

\* p &lt; .05

\*\* p &lt; .01

Hospitals, and Specialty Hospitals support hypothesis 2. The charities belonging to the aforementioned industries were reviewed to understand the difference. Charities in the industries which contradicted hypothesis 2 are located in counties where labor is less expensive (see Table 6). The difference is about 4.6% of the weekly wage or \$40 per week. Hence, nonprofit formation negatively associates with intellectual capital when the industry is particularly labor intensive or the revenue productivity of its labor is low. For example, labor expenses in nursing care facilities can account for up to 80% of total costs (Gilpin, 1994). Locations with less intellectual capital and, in turn, less expensive labor will be sought by new nursing homes wanting to improve their economic viability. In addition, for the four industries contradicting hypotheses 2, average sales per employee averaged about \$78,000 while average sales per employee in the eight supporting industries averaged about \$82,000. Again, nonprofits seemingly compensate for lower sales per employee by forming in locations where stocks of intellectual capital are lower which, in turn, makes labor less expensive.

The environmental factors most responsible for the emergence of nonprofit organizations are observed by comparing the Fischer ratios of the four regression models in each industry. The data, however, do not produce uniform results. The check marks shown in Table 4 indicate which regression model is the best predictor for nonprofit formation in each industry. Of the seventeen industries in the study, two are best predicted through the reduced model (model I), one is best predicted through a model integrating financial capital (model II), eight are best fit to a model capturing intellectual capital (model III), four are best fit to the full model (model IV), and two industries avoid explanation by the regression analysis. Only two industries, General Medical & Surgical Hospitals and Specialty Hospitals, comply with both hypotheses.

Yet, in thirteen of the seventeen industries studied, financial capital and/or intellectual capital play a significant role in the formation of nonprofit organizations. Although the influence is not uniform across industries, the influence is substantial. The inclusion of supply-side environment factors increased nonprofit theory's explicative abilities between 1.5 (Dance Companies Adj.  $R^2$  changed from .018 to .033) to 27.9 (General Medical & Surgical Hospitals Adj.  $R^2$  changed .098 to .377) percentage points.

Table 5 – Tests of Hypotheses by Industry

Best-Fit Regression Model	H1 - Financial Capital	H2 - Intellectual Capital
<b>[No Model]</b>		
611110 Elementary and Secondary Schools		
621340 Offices of Physical Occupational and Speech Therapy		Not Applicable
<b>Model I - Reduced Model</b>		
611310 Colleges Universities and Professional Schools		Not Applicable
611610 Fine Arts Schools		
<b>Model II - Financial Capital</b>		
611699 All Other Miscellaneous Schools and Instruction	Contradicted	
<b>Model III - Intellectual Capital</b>		
61151 Technical and Trade Schools		Supported
611710 Educational Support Services		Contradicted
623110 Nursing Care Facilities		Contradicted
7111 Performing Arts Companies		Supported
711110 Theater Companies and Dinner Theaters		Supported
711120 Dance Companies		Supported
711310 Promoters of Performing Arts Sports and Similar Events		Contradicted
712110 Museums		Contradicted
<b>Model IV - Financial Capital and Intellectual Capital</b>		
621498 All Other Outpatient Care Centers	Contradicted	Supported
622110 General Medical and Surgical Hospitals	Supported	Supported
622310 Specialty (except Psychiatric and Substance Abuse)	Supported	Supported
711130 Musical Groups and Artists	Contradicted	Supported

### Discussion

This study investigates the environmental factors which best predict the emergence of nonprofit organizations. The most substantial findings of the statistics produced by four regression models across seventeen industries include the importance of strategic resources to nonprofit entrepreneurship, the inapplicability of nonprofit theory across industries, and the positive influence the public sector has on nonprofit formation.

The intention of this study is to analyze the validity of the entrepreneurship process to nonprofits. In thirteen of the seventeen industries included, the representations of resources, enterprising

Table 6 – Explanation of Mixed Results for Hypotheses 2

	Industries	N	Mean	Std. Deviation	Std. Error Mean	F	Sig. (2-tailed)
County Average Weekly Wage	Contradicting H2	21,365	855.99	263.568	1.803	121.345	0.000
	Supporting H2	38,793	895.29	294.754	1.497		

Table 7 – Nonprofit Theory's Applicability across Industries

Best-Fit Regression Model	Heterogeneity Hypothesis	Social Cohesion	Crowding Out
<b>[No Model]</b>			
611110 Elementary and Secondary Schools			
621340 Offices of Physical Occupational and Speech Therapy		Not Applicable	
<b>Model I - Reduced Model</b>			
611310 Colleges Universities and Professional Schools			Contradicted
611610 Fine Arts Schools			Contradicted
<b>Model II - Financial Capital</b>			
611699 All Other Miscellaneous Schools and Instruction	Supported	Supported	
<b>Model III - Intellectual Capital</b>			
61151 Technical and Trade Schools		Supported	
611710 Educational Support Services	Supported		
623110 Nursing Care Facilities		Supported	Contradicted
7111 Performing Arts Companies			
711110 Theater Companies and Dinner Theaters		Supported	Supported
711120 Dance Companies			
711310 Promoters of Performing Arts Sports and Similar Events			Contradicted
712110 Museums	Contradicted	Contradicted	
<b>Model IV - Financial Capital and Intellectual Capital</b>			
621498 All Other Outpatient Care Centers	Supported	Contradicted	
622110 General Medical and Surgical Hospitals	Supported	Supported	Supported
622310 Specialty (except Psychiatric and Substance Abuse)	Supported		
711130 Musical Groups and Artists			Contradicted

people, or both augment the predictive abilities of nonprofit theory as formed from the Heterogeneity Hypothesis. Unfortunately, the size and direction of the supply-side factors are inconsistent across industries. The availability of financial capital supports the formation of nonprofits in asset intensive industries and the availability of intellectual capital improves the formation of nonprofits in labor intensive industries. The effects of financial capital and intellectual capital also offer a word of caution to community leaders and government agencies. Namely, nonprofits may be ineffective methods of providing social goods and services if the complimentary foundation of financial and intellectual capital is misaligned with industry needs. This is particularly relevant to rural locations where some social goods are scarce and where financial capital and intellectual capital are less abundant.

Our study also contests the existence of nonprofit theory. As Table 5 indicates, the only consistent support for both hypotheses comes from the General Medical & Surgical Hospital and the Specialty Hospital industries. The predictors for nonprofit formation were inconsistent, contradicted, or not significant in the other fifteen industries. The regression models also indicate the more established relationships of nonprofit theory are not stable across industries.

Table 7 summarizes how well the best-fit regression models align with the Heterogeneity Hypothesis (Weisbrod, 1975) and the expected requirement for social cohesion (Ben-Ner & van Hoomissen, 1991).

For the Heterogeneity Hypothesis, five industries show the expected, statistically significant relationship while one industry, Museums, provides contradictory evidence. Substantially lower total asset turnover ratios (TAT) account for the difference. In the sample, nonprofit museums have an average annual TAT of 0.34 over the study period while the five contrasting industries have an average annual TAT between 1.04 and 9.07. Museums seemingly compensate for their asset-intense operations by seeking locations with relatively uniform demand. In regards to social cohesion, where curvilinear relationship (inverted U-shaped) between demand heterogeneity and nonprofit formation is expected, five industries align with this expectation while two industries, All Other Outpatient Care Centers and Museums, produce coefficients which are positive and statistically significant (U-shaped). Here, competition is responsible for the direction of the *Social Cohesion* coefficient. For the five industries with statistically significant, negative coefficients (i.e. nonprofit formation is greater at moderate levels of demand heterogeneity), the average number of competitors (nonprofit and for-profit) per state, per year is two or more. Conversely, for the two industries where the *Social Cohesion* coefficient is positive, the average number of competitors per state, per year is less than one. Thus, competition causes emerging nonprofits to be more selective in their search for an unfulfilled, yet economically viable social good.

The only industry which provides uniform support for the doctrines of nonprofit theory is the General Medical & Surgical Hospital industry. Based on its lack of predictive abilities across industries, nonprofit theory is better conceived as “Nonprofit Hospital Theory” and the availability and abundance of hospital data (Biel, 2002; Bielefeld & Murdoch, 2004; Newhouse, 1970) is the likely reason why nonprofit scholarship built a theory so tailored to a specific industry.

Finally, government spending does not “crowd-out” nonprofits (Andreoni & Payne, 2001, 2011). Table 7 displays seven industries where government spending has a statistically significant relationship to nonprofit formation. In five of these seven industries, nonprofit formation is augmented, rather than “crowded out,” by government spending. The Heterogeneity Hypothesis asserts nonprofits fulfill demand



for social goods by the non-median voter. If this is true, then increases in government spending should negatively associate with fewer nonprofits since greater government spending equates to the production of more social goods and, in turn, less unfulfilled demand. However, this analysis finds positive relationship between government spending and the emergence of nonprofits. This suggests nonprofits, via grants and service contracts, thrive in environments where government resources are relatively abundant. The finding indicates the Heterogeneity Hypothesis needs clarification; nonprofits fulfill demand for social goods by the non-median voter *where public support is available*. This interpretation is consistent with the perpetual efforts of nonprofit managers to improve the efficiency and efficacy of their grant writing and government contracting activities (Ashley & Faulk, 2010; Baykoucheva, 2011; Connor & Wagner, 1998; Haas, 1998; Hedy Jiaying & Hooper, 2011; Kerlin & Pollak, 2011).

#### Limitations

Other empirical studies concerning nonprofit theory or market structure use market share (total firm revenue as a proportion of industry sales) as their dependent variable (Ben-Ner & van Hoomissen, 1991; Brush, Bromiley, & Hendrickx, 2000; McGee & Thomas, 1986; R. A. Miller, 1982). This study, on the other hand, calculates the dependent variable as the count of nonprofit establishments to total establishments. Important differences between these methods exist. The measure used in this study does not account for organizational size or growth of existing nonprofits, but it does allow the analysis to observe the emergence of nascent nonprofits where revenues in early years are likely to be minimal. The dependent variable used here also accounts for nonprofits not required to produce financial reports; nonprofits with less than \$25,000 in revenues are not required to file annually with the IRS (§501(C)(3) of the Internal Revenue Service Code). Hence, if the dependent variable used here was based on market share, it would have excluded numerous nonprofits. In some industries and states, up to 73% of all nonprofits would have been excluded (The Urban Institute, Public Charities, 2002-2008).

Another limitation of this study is its proxy for financial capital. Other variables such as demand heterogeneity and intellectual capital were multi-dimensional in their construction. Conversely, the measure of financial capital in the environment is based on the percentage of relatively affluent

households. While the variable is legitimate, there are other sources of financial capital (e.g. foundations and trusts) which are not accounted for in the study's model.

Finally, the use of state level data is a limitation of the research. Critics may claim states are not uniform in their size or composition, but this problem persists at all geographic levels (city, county, MSA, or region). Furthermore, many data points are not available at a more micro geographic level because of data providers' concerns for anti-trust activities.

#### Summary

In this study nonprofit theory is advanced by amending supply-side environmental factors to the Heterogeneity Hypothesis. The intention is to supplement demand-side explanations of nonprofit organizations. The statistical models reviewed are based on 3,380 observations in seventeen industries over a four year period. In general, the analysis replicates the fundamentals of the Heterogeneity Hypothesis for hospitals, a common subject of nonprofit research, but is not as predictive in other industries. In addition, financial capital and intellectual capital are salient to the formation of nonprofits. Again, the direction of the influence is not uniform across industries, but the effects are significant. Hence, extant nonprofit theory describes a specific subset of nonprofits. More progress needs to be made to build nonprofit theory which is consistently applicable to numerous industries.

## CHAPTER 2

## THE PURSUITS OF NONPROFITS

## Introduction

Existing research about nonprofits lacks efforts predicting the simultaneous pursuits of financial and social performance. Admitting difficulty in identifying, comparing, explaining, and attributing social performance, some research intentionally limits analysis to financial performance measures (e.g. Chabotar, 1989; Chang & Tuckman, 1991; Duque-Zuluaga & Schneider, 2008; Green & Griesinger, 1996; Hallock, 2002; Jackson & Holland, 1998; Ritchie & Kolodinsky, 2003). While many of these studies provided robust findings, their normative implications may be insufficient if financial performance is not uniformly related to social performance or inappropriate if donors and taxing authorities prefer charities with financial vulnerabilities (Chang & Tuckman, 1991; Knox, Blankmeyer, & Stutzman, 2006) or fiscal efficiency sacrifices output quality (Kushner & Poole, 1996). For research incorporating financial and social performance, such measures commonly consist of organization-specific measures, subjective survey responses, or tenuous relationships between organizational activities and social benefits (e.g. Camarero & Garrido, 2009; Heinrich, 2000; Mottner & Ford, 2005; Siciliano, 1996). Missing, and the focus of this paper, is research exploring when financial and social performance are pursued in tandem or isolation.

Nonprofits constitute a substantial and fast-growing segment of the US economy. The nonprofit form is employed by charities, trade unions, non-governmental organizations (NGOs), and community organizations in their efforts to advance social interests such as healthcare, education, economic development, natural resources, arts and culture, public safety, and recreation. Each year from 2000 through 2006, nonprofit institutions serving households (NPISH) have accounted for at least 6% of the GDP and about 15% of total wages (Wing, et al., 2008). The importance of nonprofits is also demonstrated in the increasing amounts of support they receive. From 1996 to 2006, private giving increased more than 200% to \$295B, volunteers increased 26.7% to 61.2M people, and donations from corporate giving programs and foundations increased 69% to \$12.7B (Wing, et al., 2008).

As their economic importance has grown, nonprofits have become the subjects of increasingly sophisticated research. Theories explaining the existence and need for nonprofits (Easley & O'Hara, 1983;

Hansmann, 1980; Weisbrod, 1986) segued into debates regarding the conceptualization and construction of valid and reliable performance metrics (Chabotar, 1989; Chang & Tuckman, 1991; Feigenbaum, 1987; Glazer, Jaenicke, Tanenbaum, & Williams, 1996; Henderson, Chase, & Woodson, 2002; "New Role for NPO CPAs," 1997; Ritchie & Kolodinsky, 2003; Sorensen & Grove, 1977; Speckbacher, 2003; Stone, Cutcher-Gershenfeld, Flynn, & Hodgkinson, 2001). Through these studies, nonprofit performance became multi-dimensional. Traditional measures, such as net income and ROA, and nonprofit-specific measures, such as fundraising expense ratios, represented *financial* performance while program outcome indicators, such as regional literacy rates of targeted populations, characterized *social* performance<sup>6</sup>. As measures became more refined, and as the privatization of social services became more accepted (Rosenau, 2003), researchers started comparing the performance of nonprofits against their for-profit rivals (Heinrich, 2000; Mark, 1996; Reeves & Ford, 2004; Rosenau, 2003; Rosenau & Linder, 2003; Schlesinger, 1998). Simultaneously, traditional strategic management approaches were used to explore drivers of nonprofits' performance. For example, management boards (Brown, 2005; Green & Griesinger, 1996), institutional forces (K. D. Miller, 2002), control systems (Cairns, Harris, Hutchison, & Tricker, 2005; Seok-Eun, 2005), marketing strategies (Mottner & Ford, 2005), and strategic resources (McHargue, 2003; K. D. Miller, 2002) have been found to influence various measures of financial and social performance.

The performance of nonprofits is scrutinized by numerous stakeholders with distinct interests. First, governing authorities searching for revenues evaluate performance to identify those nonprofits receiving unjustifiable tax exemptions (Gaul & Borowski, 1993; Kuhn, 2001; Martinez, 2009; *National Directory of Nonprofit Organizations*, 2009; Rein, 2002; Steinwald, 2008). Such reviews are more intense in urban areas where budgetary stresses are greater and a disproportionate amount of taxable assets are controlled by nonprofits (Anderson et al., 2003). Second, beneficiaries are concerned with performance and survival because an overall decline in government spending on social programs (Stone, Hager, & Griffin, 2001; Teegen, Doh, & Vachani, 2004; Toikka, Gais, Nikolov, & Billen, 2004) has increased their dependence on charitable social service providers. Third, donors survey performance to avoid failing

<sup>6</sup> Some prefer the term "organizational effectiveness" (E.g. Baruch & Ramalho, 2006; Duque-Zuluaga & Schneider, 2008; Green & Griesinger, 1996; Green, Madjidi, Dudley, & Gehlen, 2001; Heinrich, 2000; Napoli, 2006; Nobbie & Brudney, 2003)

nonprofits and to maximize their gifts' impact (Nichols, 2001). And fourth, managers use organizational performance evaluations to proxy their own performance, determine which programs require resources, and compare their organization's strategic position relative to nonprofit and for-profit rivals (Dart, 2004; Sorensen & Grove, 1977). Therefore, robust performance evaluations need to account for and integrate these numerous stakeholder perspectives (Baruch & Ramalho, 2006; Herman & Renz, 1999, 2008; Sowa, Selden, & Sandfort, 2004). The multiple constituency approach is ideally suited for such tasks (Connolly, Conlon, & Deutsch, 1980).

Based on social constructivism, the multiple constituency approach captures organizational performance as whatever relevant constituents deem it to be (Herman & Renz, 2004). The approach does not inherently favor nonprofits' financial or social performance; this is essential considering the interdependence of the two constructs (Baruch & Ramalho, 2006; Moore, 2000). Operationally, the approach observes performance through integrating surveys from several stakeholders' perspectives with the use of multiple outcome measures (e.g. size, growth, discounted goods or services) aligned with various stakeholders' interests (Connolly, et al., 1980; Duque-Zuluaga & Schneider, 2008; Mottner & Ford, 2005; Schmid, 2002; Sowa, et al., 2004).

Thus, predictions concerning nonprofits' performance through Stakeholder Theory should consider performance indicators other than profit maximization and efficiency. Such flexibility is justified by the inapplicability of property rights to nonprofits (Speckbacher, 2003); regulations and charitable missions restrict profit distribution and, despite presumptions of altruistic behavior or stewardship, various stakeholders have numerous opportunities to expropriate resources (Valentinov, 2008).

#### Stakeholder Theory

Stakeholder Theory contends organizational performance is based on the effective management of stakeholders' interests (Freeman, 1984; Mitchell & Agle, 1997) where a stakeholder is "any group or individual who can affect or is affected by the achievement of the organization's objectives" (Freeman, 1984, p. 46).

Effective stakeholder management requires prioritizing stakeholders by salience as determined by their power, legitimacy, and urgency. Power is stakeholders' ability to influence the organization's

actions (Mitchell & Agle, 1997; Pfeffer, 1992). Power comes in numerous forms (e.g. coercive, affiliation, reward, etc) and the type employed has implications for future organization-stakeholder exchanges (Ward, 1998). Legitimacy signifies the right to make a claim against the organization as defined by societal rules, practices, customs, values, and beliefs. It captures the degree to which stakeholders' relationships and interactions with an organization are reasonable (Mitchell & Agle, 1997). Finally, urgency represents "the degree to which stakeholder claims call for immediate attention" (Mitchell & Agle, 1997, p. 864).

Both for-profits and nonprofits need to prioritize stakeholders. For-profits prioritize for the singular purpose of maximizing owners' economic returns. Nonprofits, however, prioritize constituents' claims according to financial *and* social standards. Mandated ownership restrictions (i.e. no private inurement) guide such prioritization so strategic decisions will optimize benefits for all constituencies (Schmid, 2002). Furthermore, the efficient and effective production of financial and social outcomes requires combining various constituents' knowledge, resources, and interests (Kaplan, 2001; Kushner & Poole, 1996; McHargue, 2003; Mottner & Ford, 2005; Ostrander, 2007; Seok-Eun, 2005; Speckbacher, 2003). Stakeholder Theory, with a foundation based on integrating numerous stakeholder interests, is particularly well-suited for the study of organizations charged with balancing competing financial and social preferences (Dunn, 2010).

The next section explains how outcomes produced by nonprofits are influenced by the salience of four stakeholder groups: managers, board members, donors, and beneficiaries.

#### Theoretical Framework

The purpose of this research is to predict the outcomes of nonprofits based on stakeholders' relative salience. The purported causal understanding requires stakeholders have the intention and means to influence nonprofits' activities. Hence, for each stakeholder group, the basis of their salience, the mechanics and conditions which facilitate their influence, and the interests they seek to advance are all identified. As will be demonstrated, stakeholders' interests are diverse and, at times, competing (Connolly, et al., 1980; Easley & O'Hara, 1983; Hansmann, 1980; Herman & Renz, 1997, 2008; Seok-Eun, 2005; Tsui, 1990; Zammuto, 1984). The performance of a nonprofit is anticipated to be dependent upon the interests of one or more highly salient stakeholders.

## *Managers*

### *Salience*

We start with the presumption managers are the dominant coalition (Cyert & March, 1963) in the nonprofit. By default, managers' salience approximates or surpasses the salience of all other stakeholders. Their power is established through formalized hierarchical structures; their legitimacy is created by regulations and employment contracts; and their urgency is motivated by individual and organizational performance appraisals.

### *Influence*

Managers' control over hiring, marketing, resource allocation, strategic decisions, and fundraising provides them with the means to influence organizational outcomes. In the absence of other salient stakeholders, managers will leverage their autonomy to produce outcomes associated with their interests. This dynamic is facilitated by the missions, activities, and organizational structures particular to nonprofits (Glaeser, 2003). First, missions require the production of social benefits which are often intangible and difficult to identify, quantify, and compare (Baruch & Ramalho, 2006; Easley & O'Hara, 1983; Hansmann, 1980; Herman & Renz, 1999, 2008; Kaplan, 2001; Nobbie & Brudney, 2003; Siciliano, 1996; Sorensen & Grove, 1977; Sowa, et al., 2004; Speckbacher, 2003). Moreover, the absence of market evaluations (e.g. stock price) inhibits other stakeholders from validating and auditing the effectiveness of strategic decisions (Baber, Daniel, & Roberts, 2002; Glaeser, 2003; Williamson, 1983). Second, the relationship between organizational activities and social benefits is enigmatic. The abstract characteristics of social performance minimize certainty that the activities chosen to produce social benefits are optimally efficient or effective (Stone, Bigelow, & Crittenden, 1999; Stone, Cutcher-Gershenfeld, et al., 2001; Stone & Ostrower, 2007). Furthermore, observed social improvements are difficult to attribute to specific organizations or their activities (Haugh, 2005; Sorensen & Grove, 1977). Third, nonprofits' organizational structures rely on voluntary board members to provide strategic controls. Bebchuk and Fried (2003) explained how time constraints and inadequate economic incentives inhibited the monitoring of board members in for-profit organizations. In nonprofits, where board members volunteer their governance services, such realities are equally, if not more, relevant (Baber, et al., 2002; Brown, 2005;

Callen, Klein, & Tinkelman, 2003; de Andres-Alonso, Cruz, & Romero-Merino, 2006; Green & Griesinger, 1996; Hatten, 1982; Inglis, 1994; Jackson & Holland, 1998; Nobbie & Brudney, 2003; O'Regan & Oster, 2005; Preston & Brown, 2004; Provan, 1980; D. H. Smith & Shen, 1996). Taken together, these three organizational distinctions provide managers with abundant uncertainty and discretion to prioritize their interests (Ben-Ner & Gui, 2003; Hansmann, 1980; Valentinov, 2008).

### *Interests*

In for-profit research, managers' interests are advanced through unrelated organizational growth (Brush, et al., 2000), compensation (Bebchuk & Fried, 2003; Gibbons, 1998), and employment tenure (Eisenhardt, 1989). For nonprofits, such outcomes are not necessarily contradictory to other stakeholders' interests. In fact, better pay may attract and retain higher caliber managers who are more adept at managing the production of efficient and effective social benefits (Feigenbaum, 1987; K. D. Miller, 2002). Yet, holding all else constant, unrelated organizational growth, pay, or employment tenure serves the interests of managers more than other stakeholders.

### *Board Members*

#### *Salience*

Board members of nonprofits have their legitimacy and power established through tax codes, legal regulations, and organizational by-laws. They also derive power from their knowledge, skills, and experience; their access to affluent social networks; their generosity; and their ability to motivate and lead other organizational members (Abzug & Galaskiewicz, 2001; Bradshaw, Murray, & Wolpin, 1992; Callen, et al., 2003; Dart, Bradshaw, Murray, & Wolpin, 2006; Green & Griesinger, 1996; Harlan & Sidel, 1994; Jackson & Holland, 1998; Miller-Millesen, 2003; Murray, Bradshaw, & Wolpin, 1992; O'Regan & Oster, 2005; Preston & Brown, 2004). Board members' urgency is based on their ability to enforce change. Managers of nonprofits will be more responsive to board members' claims as board members indicate a greater willingness to terminate employment relationships or substantially alter resource allocations (Herman & Renz, 2004; Mathiasen, 1990; Miller-Millesen, 2003; Murray, et al., 1992).

#### *Influence*



Regulatory authorities (e.g. IRS, State Departments of Revenue) legitimize and supervise the activities of nonprofits (Fisman & Hubbard, 2003; Hansmann, 1980). However, the ability of regulatory agencies to monitor is generally perceived as ineffective because their regulations do not target specific organizations and the proportion of nonprofits subject to rigorous disciplinary review is negligible (de Andres-Alonso, et al., 2006; Fisman & Hubbard, 2003; Glaeser, 2003; O'Regan & Oster, 2005). The exception is when a societal issue pressures regulatory agencies to take precedent-setting enforcement actions. For example, popular distaste for predatory lending activities motivated the IRS to challenge the tax exempt status of consumer credit groups engaged in red-flagged activities ("IRS, Trying to Hit Consumer Credit Groups, Swings Wildly," 2005). In the end, although regulatory authorities establish a distinct set of acceptable behaviors for charities, the burden of controlling nonprofits' strategies and outputs rests with their board members.

Nonprofit research has paralleled the efforts of for-profit research to predict the intensity of monitoring by board members. The similarity is justified by the fact nonprofits, akin to for-profits, separate decision management and residual risk. This offers managers the opportunity to expropriate resources (Fama & Jensen, 1983; Hansmann, 1980). The variables to forecast monitoring are varied. First, as Miller-Milleson argued (2003), board members monitor less when managers are more professional and nonprofits are vulnerable (Miller-Millesen, 2003; Price, 1963; Provan, 1980). Board members believe more professional (i.e. educated) managers need less guidance and failing organizations require a unified endorsement of leadership rather than critical performance assessments. Second, the nonprofit's source of funding serves as a determinant of monitoring (Andreoni & Payne, 2001; Horne, Johnson, & Van Slyke, 2005; Pfeffer, 1973; Pfeffer & Salancik, 1978; Zald, 1967). The relationship derives from board members' perception that fundraising, rather than governance, is more crucial to organizational success (Zald, 1967). Power dynamics make this belief more pronounced as private gifts constitute a greater proportion of the nonprofit's revenues (Pfeffer, 1973; Pfeffer & Salancik, 1978). Conversely, when government grants

predominate, attracting revenue becomes a responsibility of managers via grant writing and board members emphasize monitoring over fundraising activities<sup>7</sup> (Andreoni & Payne, 2001; Pfeffer, 1973).

Forecasting the degree of monitoring represents an incremental step in predicting board members' influence. To advance understanding, the dynamics between monitoring and organizational performance must be identified. Green and Griesinger (1996) did not associate monitoring (manager selection, evaluation, and termination) with the performance-based, ranking of nonprofits by external stakeholders. Conversely, Herman and Renz (1997) connected monitoring activities (manager performance appraisals) to organizational performance as measured by the subjective evaluation of other nonprofit representatives. Jackson and Holland (1998) asserted self-report measures of board members' performance, which incorporated monitoring practices, positively correlated with nonprofits' financial performance. But the use of self-report measures is vulnerable to criticisms of validity and causality (i.e. healthy financial results inflate the evaluation of governance competencies) (Podsakoff & Organ, 1986). Olson (2001) associated financial performance with board members' tenure, board membership, and business experience. The explanation expected board members who were more experienced or serving on larger boards to monitor managers with greater competency. This expectation was confirmed by Brown (2005) who found larger boards better understood the organization's mission and historical importance – necessary for effective monitoring. Unfortunately, the link between board size and organizational performance (financial and social) has not been specifically identified (Bradshaw, et al., 1992; Brown, 2005).

In summary, board members' influence increases with board size and government grants. Larger boards have greater breadth and depth of governance knowledge, skills, abilities, and experience which increases board members' monitoring competency. Government grants improve board members' availability to monitor organizational outcomes.

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<sup>7</sup> An alternate explanation is government grants "crowd out" private giving – where private donors give less based on the perception government funds reduce the charity's need. However, Horne, Johnson, and Van Slyke (2005) demonstrated private donors do not have accurate knowledge of government grants to adjust their giving accordingly. Hence, the negative correlation between private gifts and government grants must be caused by board members' directives to attract government grants rather than donors' perceptions of reduced need.

### *Interests*

Board members' interests derive from their motivations to serve including developing their human capital, advancing their reputation, contributing to society, leveraging social networks for personal gain, exercising authority, working with others, enhancing self-worth, and self-healing (Clary et al., 1998; Inglis, 1994; Inglis & Cleave, 2006; Searle, 1989). Thus, organizational outcomes associated with these motivations serve board members' interests. Unfortunately, only some of these motivations are manifested through objective organizational metrics. One example is the amount of financial assistance the nonprofit offers. This outcome indicates the degree to which board members have fulfilled their desire to contribute to society. Another example is the economic exchange between the nonprofit and board members (identified by the IRS as "Interested Parties"). Exchanges suggest board members successfully leverage their position for personal gain. Finally, financial performance improves the nonprofit's reputation which, in turn, improves the reputation of affiliated board members. Financial performance is observed through efficiency (e.g. asset turnover, lower administrative expenses) (Brown, 2005; T. Carroll, Hughes, & Luksetich, 2005; Nobbie & Brudney, 2003; Ritchie & Eastwood, 2006; Ritchie & Kolodinsky, 2003; Siciliano, 1996) and organizational growth (Golensky, 2008; Siciliano, 1996). This association is confirmed by Chang and Tuckman (1991) who found board members flee financially vulnerable nonprofits for fear of reputational harm.

### *Donors*

#### *Salience*

The salience of donors derives from their giving. Dependency Theory predicts donors' power is directly related to the degree of uncertainty resolved through giving (Hambrick, 1981; Hillman & Dalziel, 2003; Pfeffer, 1981; Pfeffer & Salancik, 1978; Ulrich & Barney, 1984). Nonprofits resisting donors' influence risk losing a source of revenue (Seok-Eun, 2005). Donors' urgency is described through their financial commitment. The degree to which donors monitor their gifts and nonprofits is positively correlated to gift size (Barman, 2008; Benjamin, 2008a, 2008b; DiMaggio & Anheier, 1990; K. D. Miller, 2002). By design, restricted gifts, where the application of the gift is stated explicitly, essentially serve as manifestations of donors' urgency (Froelich, 1999). Given a choice, managers prefer unrestricted gifts

because the need to respond to donors' demands is absent (Barman, 2008; Oster, 2003). Finally, the legitimacy of donors is established by exchanges with the nonprofit (Mitchell & Agle, 1997). Each donor represents an exchange relationship which suggests donors' salience increases as the number of donors increases.

### *Influence*

Donors influence the amount and type of resources nonprofits receive (V. D. Alexander, 1998; Brulle, 2000; DiMaggio, 1986) as well as their application (Barman, 2008; Ostrander, 2007). Through their influence, donors make nonprofits more efficient and managerially competent (Chambré, 2001; Ebaugh, Chafetz, & Pipes, 2005; D. McCarthy, 2004; Ostrander, 2007; Tinkelman & Mankaney, 2007; Trussel, 2003; Vanderwoerd, 2004; Williamson, 1983), more sensitive to stakeholders' expectations (Benjamin, 2008a; Callen, et al., 2003; Olson, 2000), and more homogeneous in structure (Froelich, 1999). Donors pressure managers of nonprofits in manners similar to those used by for-profit stockholders (T. Carroll, et al., 2005; K. D. Miller, 2002; Olson, 2000; Tuckman, 1998). Instead of stock price fluctuations, donors express their confidence in management through gift restrictions, reductions, and increases. As a result, nonprofits treat donors as customers and engage in marketing activities to attract gifts (Clohesy, 2003; Dunn, 2010). Hence nonprofits prioritize the interests of donors as a means of fulfilling gift conditions and in an effort to affect gift volume, size, frequency, and form.

### *Interests*

The set of interests belonging to donors are distinct (Barman, 2008; Nichols, 2001; Oster, 2003; Rose-Ackerman, 1987). Based on the propensity for certain nonprofit traits to attract donors, donor interests are identified as organizational stability, prestige, and efficiency (Bowman, 2006; Chang & Tuckman, 1991; Feigenbaum, 1987; Green & Griesinger, 1996; Kushner & Poole, 1996; D. H. Smith & Shen, 1996). Stable nonprofits assure donors their gifts will be applied to mission-related causes rather than remediating vulnerable financial positions (Green & Griesinger, 1996; Hibbert & Horne, 1996; Kushner & Poole, 1996; Myers, 1990; D. H. Smith & Shen, 1996). Prestigious nonprofits offer donors potential affiliation benefits (e.g. recognition in annual reports, gift plaques, and banquets) and reduce donors' needs to scrutinize or monitor the charity (Chang & Tuckman, 1991; Kottasz, 2004; Myers, 1990; Sojka,

1986; Williamson, 1983). From the donors' perspective, nonprofits requiring diligent supervision, by definition, are not prestigious. Finally, efficient nonprofits promise donors their gifts are valued and allocated as intended (Bowman, 2006; Feigenbaum, 1987; Sargeant & Lee, 2002).

### *Beneficiaries*

#### *Saliency*

Beneficiaries are defined by mission statements (Ostrander, 2007) and validated by the approval of regulatory agencies (e.g. IRS) (Easley & O'Hara, 1983; Hansmann, 1980). The specificity of nonprofits' product policies (Shapiro, 1974), what outputs are offered to whom, limits managerial discretion in part through the establishment of beneficiaries' legitimacy (Moore, 2000). For example, the mission of Safe Harbor of Greater West Chester, PA states it "is an independent, nonprofit organization providing food, shelter, friendship, counseling and recovery opportunities to homeless men and women in Chester County, Pennsylvania." The specific identification of outputs (food, shelter, friendship, etc.) and eligibility (homeless in Chester County) makes distinguishing those beneficiaries with a right to make a claim from those without a right fairly easy. Conversely, the Metropolitan Museum of Art's<sup>8</sup> identification of "the public" as its target beneficiary hinders such discrimination. These examples suggest missions provide managers with varying opportunity and autonomy to induce "mission creep" (Moore, 2000) - modifying organizational activities to, in effect, change the mission. Hence, beneficiaries' legitimacy is identified through the specificity of mission statements.

Beneficiaries' urgency, the need for nonprofits to respond to beneficiaries' claims (Mitchell & Agle, 1997), is defined by competition. For beneficiaries with limited means, nonprofits often represent the sole source of necessary goods and services (Easley & O'Hara, 1983; Green & Griesinger, 1996; Hansmann, 1980; Schervish, 2007; Wallis, 2006). Hence, when competition is absent (i.e. few providers of social goods) and performance expectations are not met, beneficiaries have greater motivation to make claims and their urgency, as perceived by managers, increases (Agle, Mitchell, & Sonnenfeld, 1999).

<sup>8</sup> Metropolitan Museum of Art's mission statement: "to collect, preserve, study, exhibit, and stimulate appreciation for and advance knowledge of works of art that collectively represent the broadest spectrum of human achievement at the highest level of quality, all in the service of the public and in accordance with the highest professional standards."

Beneficiaries' power derives from the revenue they provide. This reality indicates the beneficiaries of nonprofits serving financially disadvantaged populations have little to no power (Tuckman, 1998). However, many nonprofits charge beneficiaries program fees or request honorariums for mission-related services. In these circumstances, Dependency Theory asserts beneficiaries gain power as they provide a greater proportion of nonprofits' revenue (Hambrick, 1981; Hillman & Dalziel, 2003; Pfeffer, 1981; Pfeffer & Salancik, 1978; Ulrich & Barney, 1984).

### *Influence*

Fundamentally, nonprofits exist to meet the demand not offered by the private or public sector (Weisbrod, 1986). Through their continued utilization of the nonprofits' goods and services, beneficiaries influence nonprofits to start, modify, and terminate production activities (Bennett, 2005; Bruce, 1995; Camarero & Garrido, 2009; Feigenbaum, 1987; Gruber, 1994; Tobelem, 1997). Beneficiaries also act collectively through intermediaries (e.g. insurance companies, social advocates, politicians) to influence nonprofits' organizational structure, policies, products, and pricing (Daake & Anthony, 2000; Feldstein, 1971; Thomas, Clark, & Gioia, 1993; Tuckman, 1998).

Beneficiaries' influence increases as substantial growth in the nonprofit sector (BoardSource, 2010) and the emergence of for-profit alternatives intensifies the competition for clients (Bennett, 2005; Bruce, 1995; Camarero & Garrido, 2009; Feigenbaum, 1987; Tobelem, 1997). By attracting more clients, nonprofits validate their reason for existence which, in turn, facilitates the acquisition of government grants and private gifts (Bennett, 2005). Without significant competition, nonprofits compete for grants and giving by emphasizing organizational prestige and efficiency (Clohesy, 2003; Dunn, 2010) rather than maximizing beneficiaries' needs (Baruch & Ramalho, 2006; Bruce, 1995; Easley & O'Hara, 1983; Hansmann, 1980; Herman & Renz, 1999, 2008; Kaplan, 2001; Nobbie & Brudney, 2003; Siciliano, 1996; Sorensen & Grove, 1977; Sowa, et al., 2004; Speckbacher, 2003). This explanation is confirmed by Gruber (1994) who found hospitals try to improve organizational stability (by reducing the provision of non-reimbursable services) when confronted with competition and Tobelem (1997) who found museums re-orient organizational activities towards visitors as competition increases.

### *Interests*

Beneficiaries' interests include organizational stability, related organizational growth, subsidies, and product quality (Baruch & Ramalho, 2006; Boyne, 2003; Cairns, et al., 2005; Hallock, 2002; Hasenfeld & Schmid, 1989a; Jackson & Holland, 1998; Moore, 2000; Napoli, 2006; Nichols, 2001; Rosenau & Linder, 2003; Young, 1998). Stability is important for many beneficiaries because nonprofits serve as one of the few, if not sole, providers of necessities such as healthcare, food, clothing, or shelter (Green & Griesinger, 1996). Organizational stability reduces beneficiaries' uncertainty about the future availability of necessities. Similarly, organizational growth, as related to the mission, is desired by beneficiaries because larger nonprofits provide more goods and services which further reduces beneficiaries' uncertainty (Galaskiewicz & Bielefeld, 1998; Golensky, 2008; K. D. Miller, 2002; Olson, 2000).

The value of nonprofits' outputs, from the beneficiaries' perspective, is determined by price<sup>9</sup> relative to quality<sup>10</sup> (Garvin, 1984). The circumstances (e.g. disability, disease, addiction, socio-economic status) defining their eligibility compels beneficiaries to rely on the lower-priced outputs offered by nonprofits (Baruch & Ramalho, 2006; Cairns, et al., 2005; Napoli, 2006; Rosenau & Linder, 2003). These price discounts are related to the proportion of revenues they receive from endowment income, government grants, and private giving (Hasenfeld & Schmid, 1989a; Moore, 2000; Nichols, 2001; Young, 1998). As these sources increase their yield, nonprofits can offer greater discounts to beneficiaries. Thus, the price dimension of value is the nonprofits' revenue subsidy; the proportion of revenue provided by endowment income, government grants, and private giving. However, price discounts supported by revenue subsidies are not without limits. Beneficiaries will not demand nonprofits' outputs if minimal quality expectations are unfulfilled. Quality, as the other dimension of value, is captured as the charities' proportion of program expenses. Greater program-specific expenses are associated with the provision of higher quality outputs (Boyne, 2003; Hallock, 2002; Jackson & Holland, 1998).

<sup>9</sup> The amount paid by beneficiaries for nonprofits' products. Some nonprofits offer products without charge while others have a tiered pricing system based on needs.

<sup>10</sup> Quality refers to the products' ability to satisfy beneficiaries' needs.

Table 8 – Stakeholder Salience and Interests

Stakeholder	Salience Determinants	Interests
Managers	[Salient by Default]	Unrelated Growth Tenure Compensation
Board Members	Board Size Government Grants	Charitable Contributions 'Interested Party' Exchange Financial Performance <sup>a</sup> Organizational Growth <sup>b</sup>
Donors	Private Giving Restricted Giving	Stability <sup>c</sup> Prestige Efficiency <sup>a</sup>
Beneficiaries	Competition Program Fees Mission Specificity	Stability <sup>c</sup> Program Growth <sup>b</sup> Revenue Subsidy Product Quality

<sup>a b c</sup> Similar interests shared by multiple stakeholders

Table 8 summarizes the above discussion of stakeholders by listing the determinants of their salience and their interests in nonprofits. The overall theme of this research is nonprofits' performance aligns with the interests of relatively salient stakeholders. For example, as donors' salience increases, they influence the nonprofit to pursue performance outcomes serving their interests which are identified as organizational stability, prestige, and efficiency. Thus, the first testable hypothesis is formulated as:

*Hypothesis 1. Stakeholders' salience determines the nonprofits' performance.*

However, managers as stakeholders deserve special consideration. As stipulated, managers' salience surpasses or matches the salience of all other stakeholder groups. The particular circumstances of nonprofits, intangible mission statements, abstract relationships between organizational activities and social products, and hard-to-attribute social impact; augment managers' ability to advance their interests



(i.e. unrelated organizational growth, tenure, and compensation). To the extent that compensation and tenure are unexplained by performance, or organizational growth does not advance the nonprofit's mission, the advancement of managers' interest is inefficient. Yet, such inefficiency can be controlled by the presence of other salient stakeholders. Thus, when the salience of other stakeholders is low, managers have greater discretion to advance their interests. Alternatively, the relationship is constructed as:

*Hypothesis 2. The salience of board members, donors, and beneficiaries controls the advancement of managers' interests.*

The final prediction of this study relates to the interests shared by more than one stakeholder. The previous review of stakeholders' interests indicates managers and board members share organizational growth as a common interest (although the form of growth differs) and beneficiaries and donors share organizational stability as a common interest. Hypothesis 1 predicts nonprofits' performance is determined by its congruence with the interests of a highly salient stakeholder. This prediction is extended to assert stakeholders' salience has an interactive effect on the advancement of a shared interest. For example, donors' salience and beneficiaries' salience have an interactive effect on organizational stability. The explanation of this relationship is based on two possible dynamics. The first is salient stakeholders with shared interests will coordinate their efforts to influence the nonprofit's performance with greater efficiency and effectiveness. The second explanation is constituents who occupy multiple stakeholder roles (e.g. beneficiaries who donate) have disproportionate influence. Such dual-stakeholders are awarded greater influence because they have more interactions with managers and because managers seek their counsel as a more efficient method of gaining multiple perspectives (Nichols, 2001). Accordingly, the final hypothesis is:

*Hypothesis 3. Stakeholders' salience strengthens the influence of other salient stakeholders who share similar interests.*

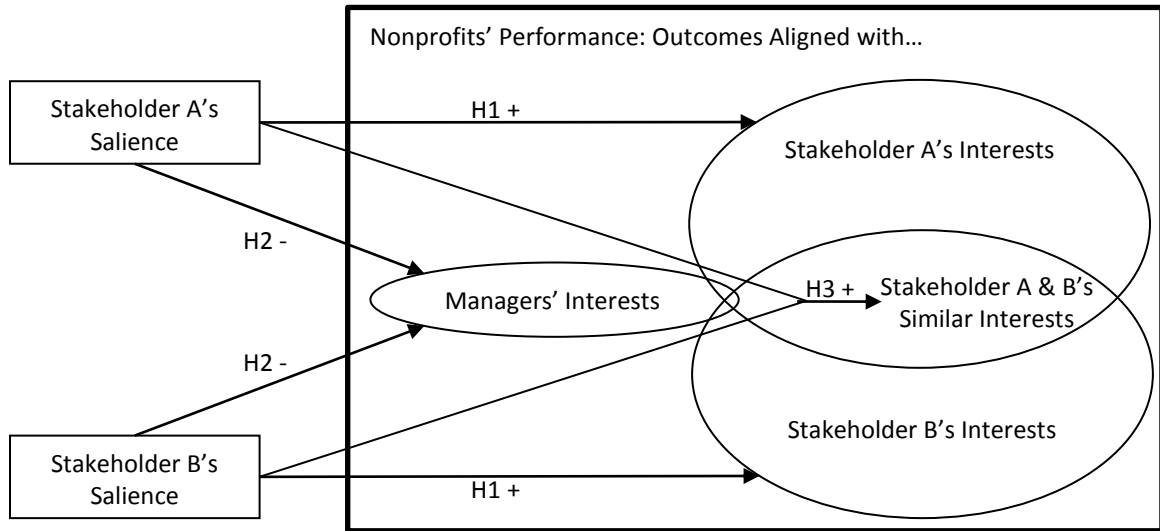


Figure 2 – Nonprofits' Performance

Figure 2 summarizes the three hypotheses.

#### Methodology

#### Data and Sample

The data come from GuideStar<sup>11</sup>, the National Center for Charitable Statistics (NCCS), and directly from the nonprofits included in the research sample. The study includes five years of data (2004 through 2008) for 134 charities, the most significant<sup>12</sup> tax-exempt category of nonprofits (Wing, et al., 2008). The 134 charities were chosen at random from 1358 organizations that (1) filed as 501(C)(3) organizations for each year of the study; (2) reported greater than zero values for Total Revenue, Total Expenses, and Total Assets in each year; (3) continued activities beyond 2009; and (4) were classified according to the National Taxonomy of Exempt Entities (NTEE) decile groups as Symphony Orchestras, Theater, Rehabilitative Care, Residential Mental Health Treatment, Employment Preparation & Procurement, or Senior Citizens Housing & Retirement Communities. These NTEE decile groups were chosen because they represent the three largest major groups of charities (Arts, Culture, & Humanities; Health; and Human Services) and

<sup>11</sup> <http://www.guidestar.com>

<sup>12</sup> Determination is based on the number of organizations, total expenses, and total assets.

because the size of their 10% samples would not dominate, or be dominated by, the study population.

Table 9 describes the research sample.

*Table 9 – Summary of Study Sample*

NTEE		Assets (2008)			
Major Group	Decile Group	Code	NPOs	Average	Std Dev
Arts, Culture, & Humanities	• Theater	A65	27	8,456,234	12,091,817
	• Symphony Orchestras	A69	17	6,841,494	8,239,652
Health	• Rehabilitative Care	E50	21	3,930,667	6,116,248
	• Residential Mental Health Treatment	F33	23	4,714,081	5,759,133
Human Services	• Employment Preparation & Procurement	J20	16	2,421,281	2,944,156
	• Senior Citizens Housing & Retirement Communities	L22	30	11,562,422	22,648,128
Total			134	6,874,662	13,065,584

#### *Dependent Variables*

The dependent variables capture outcomes associated with the interests of managers, board members, donors, and beneficiaries.

Extant for-profit research identifies managers' interests as unrelated growth (Brush, et al., 2000), employment tenure (Eisenhardt, 1989), and compensation (Bebchuk & Fried, 2003; Gibbons, 1998). Unrelated growth is the one-year percentage change in unrelated business revenue as a proportion of total revenue (*Managers' Interests – Unrelated Growth*). Employment tenure (*Managers' Interests – Tenure*) is the number of years the current top executive has occupied his or her position (Heinrich, 2000).

Compensation is the senior executive's total compensation as a proportion of total expenses (*Managers' Interests – Compensation*) (Heinrich, 2000).

Board members' motivations to volunteer identify the organizational outcomes aligned with their interests. First, board members' need to contribute to society is fulfilled through the charitable contributions of goods and services. Charities disclose cash and non-cash assistance provided to other organizations, individuals, and members. Bad debts are added to these amounts to eliminate inter-charity accounting discrepancies concerning the treatment of bad debts (Clement, White, & Valdmanis, 2002). The dollar value of cash grants, non-cash assistance, and bad debts as a proportion of total expenses is the measure of charitable contributions (*Board Members' Interests – Charitable Contributions*). Second, board members' desire to benefit personally from volunteering is represented by interested party exchange (*Board Members' Interests - Interested Party Exchange*); this is the sum of loans, business transactions, grants, and excess benefits received by current and former trustees, directors, and officers as a proportion of total expenses. And third, board members' advance their reputation through affiliations with *efficient* and *growing* charities (Chang & Tuckman, 1991; Clary, et al., 1998; Inglis, 1994; Inglis & Cleave, 2006; Searle, 1989). Measures of charities' efficiency include (1) program-specific operating margins (Siciliano, 1996), (2) total margins (Brown, 2005; T. Carroll, et al., 2005; Chabotar, 1989; Chang & Tuckman, 1991; Hallock, 2002; Kushner & Poole, 1996; Nobbie & Brudney, 2003; Ritchie & Eastwood, 2006; Ritchie & Kolodinsky, 2003; Siciliano, 1996), and (3) return on assets (Ritchie & Kolodinsky, 2003). The standardized value of each efficiency measure is summed to represent organizational efficiency (*Board Members' Interests – Financial Performance*). Organizational growth is the four-year percentage increase in (1) assets (K. D. Miller, 2002) and (2) total revenue (Galaskiewicz & Bielefeld, 1998; K. D. Miller, 2002; Olson, 2000). Again, the standardized values of these calculations are summed to create a measure of organization growth (*Board Members' Interests – Organizational Growth*).

Donors' interests include organizational stability, prestige, and efficiency. Stability equates to a lack of revenue volatility (Chang & Tuckman, 1991) and items which negatively associate with revenue

volatility including unrestricted reserves<sup>13</sup>, revenue diversity, administrative costs, and operating margins (D. A. Carroll & Stater, 2009; Chang & Tuckman, 1991; Hager, 2001; Tuckman & Chang, 1991). All of these serve as coffers from which the charity can withdraw to stabilize itself in times of financial stress. Operationally, revenue volatility is the average percent change in total revenues during the study period (Galaskiewicz & Bielefeld, 1998; K. D. Miller, 2002; Olson, 2000), unrestricted reserves are the proportion of unrestricted net assets to total net assets for nonprofits following SFAS 117<sup>14</sup> or the proportion of retained earnings to total net assets for nonprofits not following SFAS 117 (Chang & Tuckman, 1991), revenue diversity is calculated as one less the sum of squared revenue shares<sup>15</sup> (Chabotar, 1989; Chang & Tuckman, 1991), administrative costs are the proportion of management and general expenses to total expenses (Chang & Tuckman, 1991; Duque-Zuluaga & Schneider, 2008), and operating margins are calculated by dividing total revenues less total expenditures by total revenues (Chabotar, 1989; Chang & Tuckman, 1991; Hallock, 2002; Kushner & Poole, 1996; Ritchie & Kolodinsky, 2003). The sum of these standardized calculations represents organizational stability (*Donors Interests - Stability*). The star-rating methodology of CharityNavigator.org is used to calculate organizational prestige (*Donors Interests - Prestige*). CharityNavigator.org designed its star-rating system “to guide intelligent giving” ([www.charitynavigator.org/methodology](http://www.charitynavigator.org/methodology)). Hence, the ratings are oriented towards donors and evaluate charities’ efficiency and effectiveness. The importance of the ranking is evidenced by its popularity with donors (e.g. over 3 million unique users in 2010) and the attention it receives from professional associations (e.g. Association of Fundraising Professionals) and trade publications (e.g. The Chronicle of Philanthropy) (Pilon, 2010; Strom, 2010). Donors’ interest in efficiency concerns the productive use of inputs to acquire resources. Feigenbaum’s (1987) definitions of such efficiency are (1) fundraising expenditures as a proportion of total revenue and (2) administrative expenditures as a proportion of total

<sup>13</sup> Unrestricted reserves are equity reserves which managers have access and permission to expend.

<sup>14</sup> Among other stipulations, SFAS 117 requires the classification of net assets and revenues, expenses, gains, and losses to be based on the existence or absence of donor-imposed restrictions (<http://www.fasb.org/st/summary/stsum117.shtml>).

<sup>15</sup>  $1 - \sum_{i=1}^n \left( \frac{\text{Revenue Source}_i}{\text{Total Revenue}} \right)^2$  where  $n$  is the number of revenue sources and  $i$  is the revenue source. A derivation of the HHI (Hirschman, 1980).

revenue. Efficiency (*Donors Interests - Efficiency*) is the sum of the standardized calculations for fundraising and administrative efficiency.

Charities' stability, growth in mission-related activities, revenue subsidies, and high product value are the outcomes desired by beneficiaries. Stability (*Beneficiaries' Interests - Stability*), to review, is based on revenue volatility, revenue diversity, administrative costs, and operating margins. Growth of mission-related activities is represented by the four-year growth of (1) mission-related revenue as a proportion of total revenue and (2) program expenses as a proportion of total expenses. The sum of the two standardized growth measures represents mission-related growth (*Beneficiaries' Interests – Program Growth*). Revenue Subsidy (*Beneficiaries' Interests – Revenue Subsidy*) is the proportion of revenues not originating from beneficiaries to mission-related program expenses. Beneficiaries' value (*Beneficiaries' Interests – Product Quality*) is identified as the ratio of beneficiaries' cost to output quality. The cost incurred by beneficiaries is expressed as program revenues divided by program expenses while output quality is measured by program expenses divided by total expenses (Callen, et al., 2003; Chabotar, 1989; Greenlee & Bukovinsky, 1998).

#### *Independent Variables*

Board members' salience is represented as the number of board members serving the charity (*Board Members' Salience – Board Size*) (Olson, 2000) and the proportion of government grant revenue to total revenue (*Board Members' Salience – Government Grants*).

Donors' salience is linked to their giving. Private giving (*Donors Salience – Private Giving*) is the proportion of direct contributions to total revenue. Restricted giving (*Donors Salience – Restricted Giving*) is the proportion of average restricted net assets to average total net assets.

Beneficiaries' salience is constructed from descriptions of competition, revenues, and mission statements. Competition (*Beneficiaries' Salience – Competition*) is measured as the revenue market share belonging to charities with greater than \$5M in total revenue. The market is delineated by charities' NTEE code (Amirkhanyan, Hyun Joon, & Lambright, 2008; Nobbie & Brudney, 2003) and state (Feigenbaum, 1987). The measure replicates the concept underpinning the Herfindahl-Hirschman Index (HHI) (R. A. Miller, 1982) where greater values signify a task environment with less intense competition. Since a

negative correlation is predicted between beneficiary salience and competition, the competition proxy is subtracted from a constant to aid interpretation. The revenue description (*Beneficiaries' Salience – Program Fees*) is calculated as the proportion of program service revenue provided by beneficiaries to total revenue. Finally, a measure of beneficiaries' salience is derived from the specificity of charities' mission statements (*Beneficiaries' Salience – Mission Specificity*). The urgency and legitimacy of beneficiaries is determined by the mission statement. Specific mission statements narrowly define the targeted beneficiary by traits such as age, gender, or condition and they establish the nonprofit's uniqueness. Hence, the beneficiaries of nonprofits with relatively specific mission statements are not likely to have their needs met by other organizations. This suggests such beneficiaries will experience greater urgency to make a claim and the nonprofit is likely to attribute greater legitimacy to their claims. Both conditions increase beneficiaries' salience. To measure the specificity of nonprofits' missions, an instrument (Appendix) was created. It assessed the degree to which the sampled nonprofits defined their beneficiaries by needs, demographic traits, and geographic membership. Three business administration doctoral students and a manager of a charitable organization completed a seven-point, Likert scale evaluation for the 134 organizations in the sample. The inter-rater reliability of their assessments was confirmed with a Cronbach's Alpha score of 0.885 (Cronbach, 1951; D. George & Mallery, 2003) and an average Pearson correlation of 0.703.

#### *Control Variables*

Larger charities have several competitive advantages including superior human resources through greater and more robust compensation, economies of scale in soliciting donations and executing programs, and greater tolerance for competitive threats and environmental shocks (Feigenbaum, 1987; Golensky, 2008; Jobome, 2006; Olson, 2000; Oster, 1998; Ritchie & Eastwood, 2006; Ritchie, Kolodinsky, & Eastwood, 2007; Siciliano, 1996; Zimmermann & Stevens, 2006). Financial performance has been associated with many of the outcomes predicted by this study including manager tenure, manager compensation, and various measures of social performance (Chang & Tuckman, 1991; Gibelman, 2000; Gray & Benson, 2003; Oster, 1998; Sorensen & Grove, 1977; Van Slyke, Ashley, & Johnson, 2007; Zingheim, Schuster, & Thomsen, 2005). For these reasons, average net assets represents size

(*Organizational Size*) and total margin represents financial performance (*Organizational Performance*) as control variables. Financial performance is excluded as a control when it is a component of the dependent variable. Finally, industry effects (McGahan & Porter, 1997; Rumelt, 1991; Schmalensee, 1985) are accounted for through a dummy variable derived from charities' NTEE categorization (Duque-Zuluaga & Schneider, 2008; Nobbie & Brudney, 2003). The Theater industry (NTEE = A65) is the referent industry in the analysis. Consequently, industry effects are presented as *Symphony Orchestras*, *Rehabilitative Care*, *Mental Health & Crisis Intervention*, *Employment Preparation & Procurement*, and *Low-Income & Subsidized Rental Housing*.

### Analysis

The interest of stakeholders was estimated using ordinary least squares regression (OLS) multiple regression analysis. For each industry, the reduced model (Model I) is based on the control variables for the charities (size and performance) and the industries.

The tests for hypotheses 1 and 2 are conducted by examining regression models which incorporate various measures of stakeholders' salience. Hypothesis 1 is supported by positive and significant coefficients for the independent variables in Model II of Table 11, Table 12, and Table 13. Hypothesis 2 is supported through negative and significant coefficients for the independent variables in Model II of Table 14. For hypothesis 3, which asserts stakeholders with similar interests coordinate efforts to strengthen their influence, this study identifies financial performance, efficiency, organizational growth, program growth, and stability as similar interests. Interaction terms were then created from the components of stakeholders' salience confirmed as statistically significant predictors for these shared interests (Table 11, Table 12, and Table 13). Thus, hypothesis 3 is supported through positive and significant coefficients for the independent variables and the associated interaction terms in Models III and V of Table 15 (the similar interests of board members and donors); and Models III, V, VII, and IX of Table 16 (the similar interests of donors and beneficiaries).

### Results

Table 10 provides descriptive statistics. Evidence of multicollinearity amongst variables is absent; variance inflation factors (VIF) ranged from 1.013 to 2.425. The sampled organizations substantially differ



in terms of size (mean Assets are \$5,007 with a standard deviation of \$8,781) and have an average board size of 22 members<sup>16</sup>.

The regressions results displayed in Table 11, Table 12, and Table 13 represent board members', donors', and beneficiaries' respective influence on the outcomes produced by nonprofits. A review of the three tables provided a validity assessment of hypothesis 1: stakeholders determine nonprofits' performance. Each table presents two regression models for each stakeholder's interest. Model I is the reduced model and controls for organizational size, organizational performance, and latent industry differences through a dummy variable (Theater, A65 is the referent industry). Model II amends the reduced model with the components of the associated stakeholder's salience. For example, in Table 11, board members' salience is defined by board size and government grants; these elements of salience are used as predictors for board members' interests including charitable contributions, interested party exchange, financial performance, and organizational growth.

For some stakeholders' interests (e.g. beneficiaries' interest in stability), organizational performance was eliminated as a control variable since it is a component of the dependent variable. Also, for the regression models predicting revenue subsidy (Table 13), program fees was eliminated as an independent variable because of its inverse relationship to the dependent variable.

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<sup>16</sup> Nonprofits in BoardSource surveys have boards with an average of 16 members (BoardSource, 2007, 2010)

Table 10 – Descriptive Statistics and Correlation Matrix

Variable	Mean	Std. Deviation	N	1	2	3	4	5	6	7	8	9	10
1 Organizational Size	5,007,186	8,781,408	670										
2 Organizational Performance	0.04	0.18	670	0.048									
3 Managers Interest - Unrelated Growth	0.00	0.09	536	-0.006	0.126 **								
4 Managers Interest - Tenure	12.08	9.57	652	0.079 *	0.039	-0.011							
5 Managers Interest - Compensation	0.04	0.04	665	-0.223 **	0.160 **	0.049	0.053						
6 Board Members Interests - Charitable Contributions	0.02	0.07	670	-0.002	0.256 **	0.066	-0.044	-0.064					
7 Board Members Interests - Interested Party Exchange	0.00	0.01	670	-0.018	0.084 *	0.060	-0.054	0.053	0.138 **				
8 Board Members Interests - Financial Performance	0.00	2.03	670	0.029	0.791 **	0.064	-0.003	0.168 **	0.076 *	0.048			
9 Board Members Interests - Organizational Growth	0.00	1.58	670	0.079 *	0.252 **	-0.030	-0.062	-0.042	0.194 **	0.017	0.222 **		
10 Donors and Beneficiaries Interests - Stability	0.00	2.48	670	0.150 **	0.546 **	0.102 *	-0.027	0.319 **	0.267 **	0.056	0.445 **	0.406 **	
11 Donors Interests - Prestige	2.03	0.86	670	0.140 **	0.103 **	-0.029	0.018	-0.127 **	-0.054	-0.100 **	0.046	0.441 **	0.070
12 Donors Interests - Efficiency	(0.00)	1.50	670	0.096 *	-0.284 **	0.048	-0.144 **	0.124 **	-0.041	-0.011	-0.187 **	0.139 **	0.322 **
13 Beneficiaries' Interests - Program Growth	0.00	1.39	670	0.051	-0.012	-0.186 **	-0.017	-0.055	0.051	-0.096 *	0.012	-0.046	-0.128 **
14 Beneficiaries' Interests - Revenue Subsidy	0.68	0.91	670	-0.024	0.525 **	0.065	-0.056	0.181 **	0.553 **	0.014	0.371 **	0.226 **	0.551 **
15 Beneficiaries' Interests - Product Quality	0.88	0.57	670	0.088 *	0.046	-0.048	0.022	0.146 **	-0.203 **	0.035	0.120 **	-0.012	0.147 **
16 Board Members Saliency - Board Size	22.05	17.66	670	0.233 **	0.080 *	-0.029	-0.089 *	-0.069	-0.009	-0.069	0.116 **	0.072	0.130 **
17 Board Members Saliency - Government Grants	0.17	0.29	670	-0.223 **	-0.070	-0.035	0.060	-0.011	0.018	-0.037	-0.146 **	-0.139 **	-0.128 **
18 Donors Saliency - Private Giving	0.22	0.23	670	0.106 **	0.201 **	0.070	-0.150 **	0.137 **	0.027	-0.079 *	0.198 **	0.296 **	0.373 **
19 Donors Saliency - Restricted Giving	0.39	1.07	670	-0.003	-0.007	0.009	-0.019	-0.067	-0.031	-0.001	0.017	0.132 **	-0.224 **
20 Beneficiary Saliency - Competition	1.47	0.26	670	-0.038	0.036	-0.004	-0.129 **	0.136 **	0.092 *	0.067	0.086 *	0.099 *	0.071
21 Beneficiary Saliency - Program Fees	0.56	0.31	670	0.069	-0.184 **	-0.114 **	0.089 *	-0.122 **	-0.209 **	0.024	-0.076 *	-0.100 **	-0.297 **
22 Beneficiary Saliency - Mission Specificity	2.84	1.06	670	-0.115 **	-0.051	-0.022	0.031	-0.022	-0.106 **	0.030	-0.088 *	-0.132 **	-0.160 **

\* p ≤ .05 level (2-tailed)

\*\* p ≤ .01 level (2-tailed)

Table 10 – Descriptive Statistics and Correlation Matrix (Continued)

Variable	Mean	Std. Deviation	N	11	12	13	14	15	16	17	18	19	20	21
1 Organizational Size	5,007.186	8,781.408	670											
2 Organizational Performance	0.04	0.18	670											
3 Managers Interest - Unrelated Growth	0.00	0.09	536											
4 Managers Interest - Tenure	12.08	9.57	652											
5 Managers Interest - Compensation	0.04	0.04	665											
6 Board Members Interests - Charitable Contributions	0.02	0.07	670											
7 Board Members Interests - Interested Party Exchange	0.00	0.01	670											
8 Board Members Interests - Financial Performance	0.00	2.03	670											
9 Board Members Interests - Organizational Growth	0.00	1.58	670											
10 Donors and Beneficiaries Interests - Stability	0.00	2.48	670											
11 Donors Interests - Prestige	2.03	0.86	670											
12 Donors Interests - Efficiency	(0.00)	1.50	670	-0.198 **										
13 Beneficiaries' Interests - Program Growth	0.00	1.39	670	0.170 **	-0.176 **									
14 Beneficiaries' Interests - Revenue Subsidy	0.68	0.91	670	-0.047	0.090 *	-0.160 **								
15 Beneficiaries' Interests - Product Quality	0.88	0.57	670	-0.153 **	0.236 **	0.004	-0.305 **							
16 Board Members Saliency - Board Size	22.05	17.66	670	0.057	0.271 **	0.069	0.079 *	-0.071						
17 Board Members Saliency - Government Grants	0.17	0.29	670	0.038	-0.169 **	-0.060	0.212 **	-0.565 **	-0.158 **					
18 Donors Saliency - Private Giving	0.22	0.23	670	0.065	0.432 **	-0.121 **	0.337 **	-0.201 **	0.440 **	-0.290 **				
19 Donors Saliency - Restricted Giving	0.39	1.07	670	0.069	0.170 **	-0.058	0.037	0.002	0.180 **	-0.087 *	0.193 **			
20 Beneficiary Saliency - Competition	1.47	0.26	670	0.002	-0.033	0.145 **	0.048	0.037	-0.014	-0.114 **	0.071	-0.004		
21 Beneficiary Saliency - Program Fees	0.56	0.31	670	-0.038	-0.177 **	0.168 **	-0.597 **	0.689 **	-0.202 **	-0.660 **	-0.448 **	-0.052	0.022	
22 Beneficiary Saliency - Mission Specificity	2.84	1.06	670	0.022	-0.169 **	0.065	-0.133 **	-0.073	-0.151 **	0.121 **	-0.152 **	-0.120 **	-0.155 **	0.031

\* p ≤ .05 level (2-tailed)

\*\* p ≤ .01 level (2-tailed)

The statistical analysis offers varying degrees of support for hypothesis 1. Board members' influence over their interests (Table 11) is limited to nonprofits' financial performance. However, the elements of board members' salience do not have a consistent effect on financial performance. While larger boards are associated with improving financial performance<sup>17</sup>, the relationship between government grants and financial performance is statistically significant and negative. Thus, increasing nonprofits' stock of human capital on the board may benefit financial performance, but the relationship is vulnerable. As board members are given more opportunity to control the organization; because acquiring government grants is a staff function and redirects board members' time and efforts towards monitoring; their influence becomes counterproductive to the advancement of nonprofits' financial performance.

More consistent support for hypothesis 1 is provided by the analysis of donors' influence (Table 12). Although no determinant of donors' salience significantly associates with organizational prestige, their salience as defined by private giving significantly and positively associates with organizational stability and efficiency. Interestingly, restricted giving has a statistically significant, negative association with organizational stability. This relationship is understood by contrasting private giving and restricted giving. Private giving represents revenues not related to government grants, trust and endowment investment income, or services to beneficiaries. To the extent no condition is attached to private gifts, nonprofits can use the funds for any purposes connected to their mission. Hence, private giving improves nonprofits' flexibility and provides revenue streams which may compensate for financially vulnerable programs. Such applications of private giving improve nonprofits' stability. Restricted giving, on the other hand, does not provide the same utility. Restricted gifts are designated by donors towards a specific purpose such as physical assets, endowments, or program expenses. These gifts commonly have conditions regarding matching gifts or time horizons. Such conditions create spending mandates for the nonprofit; the nonprofit is forced to engage in supplemental fundraising activities or assume the cost of ancillary expenses in order to bring the gift's restricted purpose to fruition. In addition, expenditures associated with the restricted gifts (e.g. building expansion, endowment campaign, specialized

<sup>17</sup> A quadratic term for Board Size was created to observe if the relationship between the board and various forms of charities' performance is curvilinear. No analysis produces statistically significant coefficients, statistically significant models, or improved F-ratios.

equipment) are typically non-recurring and, therefore, perpetuating them on an annual basis is more difficult (relative to unrestricted gifts). For these reasons, donors who make restricted gifts to preserve their intentions do so at the expense of nonprofits' stability.

Table 11 – Predictors of Board Members' Interests

Independent Variable	Charitable Contributions		Interested Party Exchange		Financial Performance		Organizational Growth		
	Model I	Model II	Model I	Model II	Model I	Model II	Model I	Model II	
(Constant)	B Std. Error	-0.007 0.006	-0.013 0.007	0.001 * 0.000	0.001 * 0.001	0.333 0.187	0.095 0.238	0.544 ** 0.142	0.687 ** 0.182
Organizational Size	B Std. Error Beta	0.000 0.000 0.016	0.000 0.000 -0.005	0.000 0.000 -0.029	0.000 0.000 -0.030	0.000 0.000 0.005	0.000 0.000 -0.029	0.000 0.000 0.037	0.000 0.000 0.039
Organizational Performance	B Std. Error Beta	0.099 ** 0.014 0.266	0.097 ** 0.014 0.260	0.002 0.001 0.075	0.002 * 0.001 0.075	<del>0.000</del> <del>0.000</del> <del>0.005</del>	<del>0.000</del> <del>0.000</del> <del>-0.029</del>	<del>0.000</del> <del>0.000</del> <del>0.037</del>	<del>0.000</del> <del>0.000</del> <del>0.039</del>
Symphony Orchestras	B Std. Error Beta	0.004 0.009 0.021	0.001 0.009 0.004	-0.001 0.001 -0.059	-0.001 0.001 -0.050	-0.084 0.280 -0.014	-0.219 0.284 -0.036	-0.251 0.213 -0.053	-0.206 0.217 -0.044
Rehabilitative Care	B Std. Error Beta	0.016 0.008 0.089	0.020 * 0.008 0.110	-0.001 0.001 -0.062	-0.001 0.001 -0.068	-0.337 0.266 -0.060	-0.162 0.271 -0.029	-0.700 ** 0.201 -0.162	-0.734 ** 0.207 -0.170
Mental Health & Crisis Intervention	B Std. Error Beta	0.024 ** 0.008 0.136	0.030 ** 0.009 0.173	-0.001 0.001 -0.060	-0.001 0.001 -0.054	-0.829 * 0.258 -0.154	-0.507 0.274 -0.094	-1.075 ** 0.196 -0.257	-1.071 ** 0.209 -0.257
Employment Preparation & Procurement	B Std. Error Beta	0.039 ** 0.009 0.193	0.050 ** 0.010 0.246	0.000 0.001 0.029	0.001 0.001 0.060	-0.640 * 0.290 -0.102	-0.083 0.336 -0.013	-0.931 ** 0.220 -0.192	-0.822 ** 0.257 -0.169
Low-Income & Subsidized Rental Housing	B Std. Error Beta	0.028 ** 0.007 0.178	0.033 ** 0.008 0.211	0.001 * 0.001 0.116	0.001 * 0.001 0.106	-0.250 0.240 -0.051	-0.026 0.253 -0.005	-0.628 ** 0.182 -0.166	-0.677 ** 0.193 -0.179
Board Members Salience - Board Size	B Std. Error Beta		0.000 0.000 0.073		0.000 0.000 -0.045		0.011 * 0.005 0.096		-0.004 0.004 -0.048
Board Members Salience - Govt Grants	B Std. Error Beta		-0.016 0.010 -0.070		-0.001 0.001 -0.071		-0.881 ** 0.327 -0.126		-0.309 0.250 -0.057
	N	670	670	670	670	670	670	670	670
	Adj. R2	0.095	0.099	0.028	0.300	0.012	0.026	0.053	0.054
	ΔR2	0.105 **	0.007	0.039 **	0.005	0.021 *	0.017 **	0.061 **	0.004
	F Ratio	11.067 **	9.212 **	3.797 **	3.319 **	2.357 **	3.254 **	7.232 **	5.758 **

\* p < .05

\*\* p < .01

The influence of beneficiaries' salience on their interests; stability, program growth, revenue subsidy and product quality; is not uniform. For program growth and product quality, the positive and statistically significant coefficients for salience are consistent with hypothesis 1. However, for stability, the statistically significant coefficients for salience are negative - contradicting hypothesis 1. Furthermore, the direction of statistically significant predictors for revenue subsidy fluctuates; competition is positive while mission specificity is negative.

Table 12 – Predictors of Donors' Interests

Independent Variable	Stability		Prestige		Efficiency		
	Model I	Model II	Model I	Model II	Model I	Model II	
(Constant)	B	0.906 **	-0.014	2.094 **	1.923 **	0.743 **	0.146
	Std. Error	0.220	0.258	0.079	0.103	0.124	0.158
Organizational Size	B	0.000 **	0.000 *	0.000	0.000	0.000	0.000
	Std. Error	0.000	0.000	0.000 **	0.000 **	0.000	0.000
	Beta	0.114	0.079	0.135	0.135	0.054	0.044
Symphony Orchestras	B	-0.838 *	-1.314 **	-0.292	-0.358	0.305	0.055
	Std. Error	0.330	0.303	0.118 *	0.121 **	0.186	0.186
	Beta	-0.113	-0.176	-0.113	-0.138	0.068	0.012
Rehabilitative Care	B	-0.852 **	-0.730 *	-0.111	-0.028	-0.930 **	-0.689 **
	Std. Error	0.313	0.289	0.112	0.116	0.176	0.178
	Beta	-0.125	-0.107	-0.047	-0.012	-0.225	-0.167
Mental Health & Crisis Intervention	B	-1.603 **	-1.080 **	-0.218 **	-0.107	-1.210 **	-0.833 **
	Std. Error	0.304	0.292	0.109	0.117	0.171	0.179
	Beta	-0.244	-0.164	-0.095	-0.047	-0.304	-0.209
Employment Preparation & Procurement	B	-1.741 **	-1.305 **	-0.088	0.028	-0.996 **	-0.618 **
	Std. Error	0.342	0.324	0.123	0.130	0.192	0.199
	Beta	-0.228	-0.171	-0.033	0.010	-0.215	-0.134
Low-Income & Subsidized Rental Housing	B	-1.539 **	-0.719 *	-0.120	0.017	-1.588 **	-1.097 **
	Std. Error	0.283	0.287	0.101	0.115	0.159	0.177
	Beta	-0.259	-0.121	-0.058	0.008	-0.441	-0.305
Donors Salience - Private Giving	B		4.413 **		0.355		1.618 **
	Std. Error		0.458		0.183		0.282
	Beta		0.409		0.094		0.247
Donors Salience - Restricted Giving	B		-0.732 **		0.063		0.060
	Std. Error		0.080		0.032		0.049
	Beta		-0.317		0.078		0.043
	N	670	670	670	670	670	670
	Adj. R2	0.078	0.265	0.022	0.030	0.204	0.242
	ΔR2	0.086 **	0.188 **	0.031 **	0.011 *	0.211 **	0.039 **
	F Ratio	10.368 **	31.139 **	3.513 **	3.628 **	29.579 **	27.630 **

\* p &lt; .05

\*\* p &lt; .01

The influence of beneficiaries' salience on their interests; stability, program growth, revenue subsidy and product quality; is not uniform. For program growth and product quality, the positive and statistically significant coefficients for salience are consistent with hypothesis 1. However, for stability, the statistically significant coefficients for salience are negative - contradicting hypothesis 1. Furthermore, the direction of statistically significant predictors for revenue subsidy fluctuates; competition is positive while mission specificity is negative. Although the full regression model for revenue subsidy is statistically significant, its Fisher ratio is substantially reduced after the inclusion of competition and mission specificity. Hence, the regression models associated with revenue subsidy can be ignored to conclude that, overall, the relationships related to beneficiaries' salience support hypothesis 1; the significant

predictors of program growth and product quality are positive. For beneficiaries, the negative relationship found between the determinants of beneficiaries' salience and nonprofit' stability can be justified. Program fees are revenues provided by those the nonprofit is charged with serving. Dependence on buyers who are identified as needing charity suggests the continuation of associated revenues is less certain and more limited. In addition, as the mission targets an increasingly narrow subset of beneficiaries (i.e. mission specificity), the probability of successfully soliciting donors sympathetic to the targeted need is reduced. Hence, although beneficiaries prefer stable organizations to reduce the uncertainty of receiving future services, the fact that the nonprofit form is necessary to serve their needs suggests that beneficiaries' increasing salience causes nonprofits to become more unstable.

Hypothesis 2, stakeholders' salience limits managers' interests, is evaluated through the regression results displayed in Table 14. For unrelated growth, all statistically significant indicators of board members', donors', and beneficiaries' salience have negative coefficients indicating stakeholders do, in fact, control the advancement of managers' interests. For tenure, the two significant determinants of stakeholders' salience are government grants and program fees. However, contrary to hypothesis 2, the associated coefficients are positive. This relationship is explained by managers' performance appraisals (T. Carroll, et al., 2005). Government grants are perceived by board members as a staff responsibility. Hence, increasing grant revenue is an indicator of managers' performance which justifies continued employment and lengthens managers' tenure. Likewise, increasing program fees suggest managers effectively design and implement programs for targeted beneficiaries. Finally, for compensation, the remaining dependent variable used to test hypothesis 2, all statistically significant salience coefficients are negative except for competition. While competition is an effective measure of beneficiaries' salience (its influence as shown in Table 14 is consistent with hypothesis 1), competition has a distinct effect on managers' compensation. Competition forces nonprofits to increase managers' compensation as a method of attracting and retaining competent senior leadership (T. Carroll, et al., 2005; Hamid, 1995; Oster, 1998; Werner & Gemeinhardt, 1995).

Table 13 – Predictors of Beneficiaries' Interests

Independent Variable	Stability		Program Growth		Revenue Subsidy		Product Quality	
	Model I	Model II	Model I	Model II	Model I	Model II	Model I	Model II
(Constant)	B 0.906 ** Std. Error 0.220	3.442 ** 0.733	-0.115 0.125	-1.816 ** 0.444	0.631 ** 0.071	0.417 0.234	1.077 ** 0.049	0.553 ** 0.132
Organizational Size	B 0.000 ** Std. Error 0.000 Beta 0.114	0.000 ** 0.000 0.117	0.000 0.000 0.034	0.000 0.000 0.048	0.000 0.000 -0.039	0.000 0.000 -0.037	0.000 0.000 0.025	0.000 0.000 0.002
Organizational Performance	<del>B Std. Error Beta</del>	<del>  </del>	<del>  </del>	<del>  </del>	2.740 ** 0.169 0.530	2.730 ** 0.167 0.528	<del>  </del>	<del>  </del>
Symphony Orchestras	B -0.838 * Std. Error 0.330 Beta -0.113	-1.306 ** 0.321 -0.175	-0.190 0.188 -0.045	0.025 0.194 0.006	0.149 0.106 0.054	0.203 0.108 0.074	-0.376 ** 0.073 -0.220	-0.211 ** 0.058 -0.123
Rehabilitative Care	B -0.852 ** Std. Error 0.313 Beta -0.125	-0.444 0.301 -0.065	-0.153 0.178 -0.040	-0.253 0.182 -0.066	-0.122 0.101 -0.048	-0.038 0.103 -0.015	-0.177 * 0.069 -0.113	-0.253 ** 0.054 -0.161
Mental Health & Crisis Intervention	B -1.603 ** Std. Error 0.304 Beta -0.244	-1.360 ** 0.302 -0.207	0.006 0.174 0.002	0.031 0.183 0.008	-0.121 0.098 -0.050	0.007 0.104 0.003	-0.276 ** 0.068 -0.183	-0.299 ** 0.055 -0.198
Employment Preparation & Procurement	B -1.741 ** Std. Error 0.342 Beta -0.228	-2.523 ** 0.346 -0.330	-0.124 0.195 -0.029	0.115 0.209 0.027	0.274 * 0.110 0.097	0.379 ** 0.114 0.135	-0.657 ** 0.076 -0.374	-0.303 ** 0.062 -0.172
Low-Income & Subsidized Rental Housing	B -1.539 ** Std. Error 0.283 Beta -0.259	-0.830 ** 0.276 -0.140	0.669 ** 0.161 0.201	0.453 ** 0.167 0.136	-0.195 * 0.091 -0.089	-0.168 0.092 -0.077	-0.002 0.063 -0.002	-0.215 ** 0.050 -0.158
Beneficiaries Saliency - Competition	B Std. Error Beta	-0.195 0.381 -0.020		0.697 ** 0.230 0.128		0.258 ** 0.129 0.072		-0.060 0.069 -0.027
Beneficiaries Saliency - Program Fees	B Std. Error Beta	-3.105 ** 0.313 -0.392		0.592 ** 0.189 0.133	<del>  </del>	<del>  </del>		1.236 ** 0.056 0.679
Beneficiaries Saliency - Mission Specificity	B Std. Error Beta	-0.225 * 0.088 -0.096		0.121 * 0.053 0.091		-0.080 ** 0.030 -0.092		-0.024 0.016 -0.044
	N 670 Adj. R2 0.078 ΔR2 0.086 ** F Ratio 10.368 **	670 0.202 0.127 ** 19.787 **	670 0.047 0.055 ** 6.480 **	670 0.071 0.028 ** 6.639 **	670 0.300 0.307 ** 41.862 **	670 0.311 0.013 ** 34.521 **	670 0.140 0.148 ** 19.182 **	670 0.509 0.367 ** 77.970 **

\* p < .05  
\*\* p < .01

Hypothesis 3: stakeholders' influence is strengthened by the saliency of other stakeholders who share similar interests, is examined through regression models III and V in Table 15 and models III, V, VII, and IX in Table 16. No model produced statistically significant coefficients for the indicators of stakeholders' saliency and the related interactive terms. Hypothesis 3, then, is not supported by the regression results.



Table 14 – Predictors of Managers' Interests

Independent Variable	Unrelated Growth		Tenure		Compensation		
	Model I	Model II	Model I	Model II	Model I	Model II	
(Constant)	B	-0.001	0.243 **	13.960 **	7.455	0.046	0.095 **
	Std. Error	0.010	0.050	0.817	4.914	0.003	0.020
Organizational Size	B	0.000	0.000	0.000 **	0.000 **	0.000	0.000 **
	Std. Error	0.000	0.000	0.000	0.000	0.000	0.000
	Beta	-0.008	-0.030	0.098	0.117	-0.246	-0.261
Organizational Performance	B	0.068 **	0.016	1.709	4.030	0.036	0.026 **
	Std. Error	0.023	0.024	2.053	2.112	0.008	0.008
	Beta	0.130	0.031	0.030	0.071	0.162	0.115
Symphony Orchestras	B	0.005	0.000	-9.471 **	-8.924 **	-0.005	-0.004
	Std. Error	0.015	0.016	1.216	1.310	0.005	0.005
	Beta	0.017	-0.001	-0.332	-0.313	-0.049	-0.038
Rehabilitative Care	B	-0.003	-0.008	-3.444 **	-4.045 **	-0.007	-0.007
	Std. Error	0.014	0.015	1.152	1.228	0.005	0.005
	Beta	-0.011	-0.029	-0.132	-0.155	-0.065	-0.064
Mental Health & Crisis Intervention	B	0.012	0.013	3.317 **	1.795	-0.006	-0.001
	Std. Error	0.014	0.015	1.120	1.282	0.005	0.005
	Beta	0.047	0.051	0.132	0.072	-0.066	-0.012
Employment Preparation & Procurement	B	0.003	0.005	-1.187	-2.138	-0.011	-0.007
	Std. Error	0.015	0.018	1.275	1.509	0.005	0.006
	Beta	0.009	0.016	-0.040	-0.072	-0.096	-0.059
Low-Income & Subsidized Rental Housing	B	-0.012	-0.020	-5.435 **	-6.512 **	-0.008	-0.007
	Std. Error	0.013	0.015	1.060	1.252	0.004	0.005
	Beta	-0.052	-0.087	-0.232	-0.278	-0.085	-0.075
Board Members Salience - Board Size	B		-0.001 *		-0.006		0.000 **
	Std. Error		0.000		0.023		0.000
	Beta		-0.113		-0.012		-0.117
Board Members Salience - Govt Grants	B		-0.248 **		12.371 **		-0.072 **
	Std. Error		0.040		4.228		0.017
	Beta		-0.762		0.371		-0.565
Donors Salience - Private Giving	B		-0.201 **		7.791		-0.045 **
	Std. Error		0.042		4.387		0.018
	Beta		-0.490		0.187		-0.276
Donors Salience - Restricted Giving	B		0.001		0.204		-0.003 **
	Std. Error		0.004		0.326		0.001
	Beta		0.012		0.023		-0.090
Beneficiaries Salience - Competition	B		-0.001		-2.925		0.016 **
	Std. Error		0.018		1.504		0.006
	Beta		-0.003		-0.078		0.108
Beneficiaries Salience - Program Fees	B		-0.245 **		13.897 **		-0.075 **
	Std. Error		0.038		4.177		0.017
	Beta		-0.811		0.446		-0.624
Beneficiaries Salience - Mission Specificity	B		0.000		-0.111		-0.001
	Std. Error		0.004		0.346		0.001
	Beta		-0.001		-0.012		-0.025
	N	536	536	536	536	536	536
	Adj. R2	0.010	0.077	0.170	0.194	0.077	0.136
	ΔR2	0.023	0.079 **	0.176 **	0.033 **	0.087 **	0.068 **
	F Ratio	1.759	4.195 **	20.006 **	12.184 **	8.895 **	8.461 **

\* p &lt; .05

\*\* p &lt; .01

Table 15 - Predictors of Board Members' and Donors' Shared Interests

Independent Variable	Financial Performance						Efficiency					
	Model I	Model II	Model III	Model IV	Model V	Model VI	Model I	Model II	Model III	Model IV	Model V	Model VI
(Constant)	B 0.333 Std. Error 0.187	-0.539 * 0.264	-0.651 * 0.300	-0.280 0.240	-0.257 0.243	-0.391 0.236	0.743 ** 0.124	0.185 0.174	0.085 0.197	0.232 0.158	0.250 0.160	0.197 0.155
Organizational Size	B 0.000 Std. Error 0.005	0.000 0.000 -0.017	0.000 0.000 -0.018	0.000 0.000 -0.017	0.000 0.000 -0.017	0.000 0.000 -0.011	0.000 0.000 0.054	0.000 0.000 0.041	0.000 0.000 0.041	0.000 0.000 0.036	0.000 0.000 0.036	0.000 0.000 0.045
Symphony Orchestras	B -0.084 Std. Error 0.280	-0.454 0.287 -0.074	-0.415 0.291 -0.068	-0.375 0.282 -0.061	-0.358 0.284 -0.059	-0.433 0.291 -0.071	0.305 0.186 0.068	0.065 0.189 0.015	0.100 0.186 0.022	0.074 0.186 0.016	0.087 0.187 0.019	0.095 0.192 0.021
Rehabilitative Care	B -0.337 Std. Error 0.266	-0.001 0.272	-0.009 0.272	-0.059 0.266	-0.079 0.269	-0.037 0.273	-0.930 ** 0.176	-0.721 ** 0.179	-0.728 ** 0.179	-0.718 ** 0.176	-0.734 ** 0.177	-0.744 ** 0.180
Mental Health & Crisis Intervention	B -0.829 ** Std. Error 0.258	-0.312 0.275	-0.294 0.276	-0.296 0.273	-0.319 0.277	-0.358 0.277	-1.210 ** 0.171	-0.862 ** 0.181	-0.847 ** 0.182	-0.827 ** 0.180	-0.846 ** 0.182	-0.881 ** 0.182
Employment Preparation & Procurement	B -0.640 * Std. Error 0.290	-0.150 0.302	-0.140 0.302	0.071 0.333	0.079 0.334	-0.181 0.304	-0.996 ** 0.192	-0.654 ** 0.199	-0.645 ** 0.199	-0.541 * 0.220	-0.534 * 0.220	-0.669 ** 0.200
Low-Income & Subsidized Rental Housing	B -0.250 Std. Error 0.240	0.423 0.272	0.444 0.274	0.333 0.265	0.327 0.265	0.363 0.268	-1.588 ** 0.159	-1.126 ** 0.180	-1.107 ** 0.180	-1.132 ** 0.175	-1.138 ** 0.175	-1.143 ** 0.176
Board Members Sallience - Board Size	B 0.007 Std. Error 0.005	0.007 0.005	0.013 0.009	0.013 0.009	0.009 0.005	0.008 0.013	0.000 0.004	0.000 0.004	0.005 0.006	0.005 0.006	0.005 0.006	-0.005 -0.005
Board Members Sallience - Govt Grants	B 0.329 Std. Error 0.087	-0.695 0.359	-0.611 0.329	-0.611 0.329	-0.695 0.359	-0.300 2.117				-0.258 0.217	-0.325 0.237	0.176 1.394
Donors Sallience - Private Giving	B 1.997 ** Std. Error 0.435	1.997 ** 0.435	2.394 ** 0.662	1.944 ** 0.435	1.816 ** 0.487	1.913 ** 0.591	1.624 ** 0.286	1.624 ** 0.286	1.976 ** 0.302	1.564 ** 0.239	1.461 ** 0.223	1.743 ** 0.389
Board Members Sallience - Board Size * Donors Sallience - Private Giving	B -0.018 Std. Error 0.022	-0.018 0.022	-0.018 0.022	-0.018 0.022	-0.018 0.022	-0.016 0.106						
Board Members Sallience - Govt Grants * Donors Sallience - Private Giving	B 1.351 Std. Error 0.292	1.351 2.292	1.351 2.292	1.351 2.292	1.351 2.292	1.351 2.292					1.079 1.511	0.009 0.029
	N	670	670	670	670	670	670	670	670	670	670	670
	Adj. R2	0.012	0.046	0.046	0.049	0.043	0.204	0.240	0.240	0.241	0.241	0.239
	AR2	2.357 **	5.036 **	4.544 **	5.266 **	4.314 **	29.579 **	27.386 **	24.475 **	27.620 **	24.589 **	24.356 **
	F Ratio											

\* p &lt; .05

\*\* p &lt; .01

Table 16 - Predictors of Donors' and Beneficiaries' Shared Interests

Independent Variable	Stability									
	Model I	Model II	Model III	Model IV	Model V	Model VI	Model VII	Model VIII	Model IX	Model X
(Constant)	B 0.906 ** Std. Error 0.220	1.255 ** 0.377	1.264 ** 0.391	-0.007 0.336	-0.573 0.444	3.181 ** 0.259	2.911 ** 0.268	2.066 ** 0.305	1.952 ** 0.325	2.387 ** 0.402
Organizational Size	B 0.000 ** Std. Error 0.114	0.000 ** 0.110	0.000 ** 0.110	0.000 * 0.089	0.000 * 0.084	0.000 ** 0.109	0.000 ** 0.105	0.000 ** 0.093	0.000 ** 0.093	0.000 ** 0.087
Symphony Orchestras	B -0.838 * Std. Error 0.330	-1.546 ** 0.311	-1.544 ** 0.312	-1.456 ** 0.319	-1.545 ** 0.322	-1.116 ** 0.294	-1.383 ** 0.314	-0.660 * 0.310	-0.636 * 0.314	-1.382 ** 0.290
Rehabilitative Care	B -0.852 ** Std. Error 0.313	-0.348 0.293	-0.356 0.304	-0.106 0.310	-0.038 0.312	-1.052 ** 0.280	-1.093 ** 0.278	-1.073 ** 0.310	-1.078 ** 0.310	-0.560 * 0.285
Mental Health & Crisis Intervention	B -1.603 ** Std. Error 0.304	-0.987 ** 0.300	-1.000 ** 0.329	-0.473 0.315	-0.470 0.315	-1.931 ** 0.272	-1.907 ** 0.269	-1.782 ** 0.303	-1.767 ** 0.303	-1.142 ** 0.292
Employment Preparation & Procurement	B -1.741 ** Std. Error 0.342	-1.840 ** 0.362	-1.854 ** 0.390	-0.690 ** 0.343	-0.648 0.343	-3.106 ** 0.317	-2.997 ** 0.316	-2.059 ** 0.334	-2.069 ** 0.334	-2.134 ** 0.345
Low-Income & Subsidized Rental Housing	B -1.539 ** Std. Error 0.283	-0.374 0.292	-0.388 0.326	-0.195 0.303	-0.109 0.306	-1.379 ** 0.259	-1.416 ** 0.257	-1.823 ** 0.277	-1.822 ** 0.277	-0.629 * 0.279
Donors Sallience - Private Giving	B 2.631 ** Std. Error 0.535	2.666 ** 0.604	2.666 ** 0.604	4.319 ** 0.484	6.385 ** 1.166	-0.232 0.591	-0.238 0.591	-0.307 0.591	-0.307 0.591	2.776 ** 0.500
Donors Sallience - Restricted Giving	B -0.721 ** Std. Error 0.079	0.079 0.079	0.079 0.079	0.079 0.079	0.079 0.079	-0.721 ** 0.079	0.275 0.288	0.719 ** 0.085	0.338 0.085	0.740 ** 0.077
Beneficiaries Sallience - Program Fees	B -2.276 ** Std. Error 0.367	-2.276 ** 0.367	-2.264 ** 0.367	-2.264 ** 0.367	-2.264 ** 0.367	-3.116 ** 0.292	-2.715 ** 0.311	-0.311 0.323	-0.147 0.323	-2.261 ** 0.323
Beneficiaries Sallience - Mission Specificity	B -0.233 ** Std. Error 0.088	-0.233 ** 0.125	-0.233 ** 0.125	-0.233 ** 0.125	-0.233 ** 0.125	-0.394 0.441	-0.343 0.441	-0.248 ** 0.088	-0.202 * 0.099	-0.253 ** 0.080
Donors Sallience - Private Giving * Beneficiaries Sallience - Program Fees	B -0.178 Std. Error 1.816	-0.178 1.816	-0.178 1.816	-0.178 1.816	-0.178 1.816	-0.681 0.350	-0.681 0.350	-0.681 0.350	-0.681 0.350	-0.681 0.350
Donors Sallience - Private Giving * Beneficiaries Sallience - Mission Specificity	B -0.681 Std. Error 1.816	-0.681 1.816	-0.681 1.816	-0.681 1.816	-0.681 1.816	-1.572 ** 0.438	-1.572 ** 0.438	-1.572 ** 0.438	-1.572 ** 0.438	-1.572 ** 0.438
Donors Sallience - Restricted Giving * Beneficiaries Sallience - Mission Specificity	B -0.172 Std. Error 0.168	-0.172 0.168	-0.172 0.168	-0.172 0.168	-0.172 0.168	-0.172 0.168	-0.172 0.168	-0.172 0.168	-0.172 0.168	-0.172 0.168
N	670	670	670	670	670	670	670	670	670	670
Adj. R2	0.078	0.223	0.222	0.181	0.185	0.285	0.297	0.172	0.172	0.324
ΔR2		0.000	0.000	0.005	0.005	0.014 **	0.014 **	0.001	0.001	0.001
F Ratio	10.368 **	25.058 **	22.242 **	19.529 **	17.853 **	34.287 **	32.348 **	18.335 **	16.416 **	33.042 **

\* p &lt; .05

\*\* p &lt; .01

## Discussion

This study investigated how stakeholders' salience determines outcomes produced by nonprofits. The most substantial findings include the varying strength of stakeholders' influence, the impact external stakeholders have on controlling managers' interests, and the inability of stakeholders to coordinate their influence for the sake of mutual interests.

### *Stakeholders' Influence*

Stakeholder Theory predicts stakeholders influence organizational behavior according to their salience as derived from their power, urgency, and legitimacy. The analysis indicates some components of stakeholders' salience have more influence than others. Specifically, the determinants of salience which were related to financial resources have stronger effects. Government grants (board members), private and restricted giving (donors), and program fees (beneficiaries) were more effective predictors of the associated stakeholder's interests than other salience determinants such as board size, competition, or mission specificity. The implication of this result is stakeholders who have a greater proportion of their salience determined by their control over financial resources are prioritized. In this study, donors' salience was entirely connected to the financial resources they control. Thus, their influence was more consistent in producing outcomes associated with their interests. This is aligned with others who found managers modify organizational activities and resources for the purpose of attracting gifts (Barman, 2008; Benjamin, 2008a, 2008b; DiMaggio & Anheier, 1990; Froelich, 1999; K. D. Miller, 2002; Mitchell & Agle, 1997; Oster, 2003; Seok-Eun, 2005).

This study's findings also offer a word of caution to managers of nonprofits based on the effects of board members' salience. The analysis replicated the expectation of others (Abzug & Galaskiewicz, 2001; Brown, 2005; Brown & Iverson, 2004; Callen, et al., 2003; Jackson & Holland, 1998) who asserted or found board size impacts nonprofits' performance; however performance is defined. Although the measures of board members' salience were only significant for predicting nonprofits' financial performance, their contradicting influence suggests board members can be *too* involved. Board size is positively associated with financial performance; a larger board (more volunteer board members) provides the nonprofit with larger stocks of social and human capital. The nonprofit improves its financial

performance by leveraging its access to a larger network of, hopefully, affluent and sympathetic individuals (i.e. potential donors) and a more refined and diverse set of knowledge, skills, abilities and experience. As board members get more involved in monitoring the nonprofit, their net impact on the nonprofits' performance is reversed. This claim is substantiated by the negative relationship between government grants and financial performance (and the negative but not significant coefficients used to predict other outcomes associated with board members' interests). Again, government grants represent a staff function and partially alleviate board members from fundraising activities (Andreoni & Payne, 2001; Horne, et al., 2005; Pfeffer, 1973; Pfeffer & Salancik, 1978; Zald, 1967). Greater proportions of government grants result in additional monitoring by board members. This study suggests the additional monitoring is counterproductive to the nonprofits' financial performance and, in turn, board members' interests. Thus, managers would be wise to tailor the commitment and responsibilities of board members based on the need to leverage board members as fundraisers (which is inversely related to government grants).

#### *Stakeholders' Control over Managers*

Tests of hypothesis 2 indicated numerous stakeholders impact outcomes associated with managers' interests. The most convincing support emerges from stakeholders' influence on unrelated growth – the influence of all stakeholders is negative and the particular outcome is relatively more aligned with managers' interests than the interests of board members, donors, or beneficiaries. The findings suggest stakeholders without monetary motivations are still effective at controlling the strategic decisions of nonprofits' managers.

#### *Stakeholders' Inability to Coordinate Influence*

Finally, this study did not produce evidence that stakeholders sharing mutual interests collaborate. Stakeholders' interests are not effectively managed through a silo structure where the needs of one are isolated from the needs of others. This study indicates such coordination is not simply based on sharing mutual interests. Further theory building and research needs to identify the contexts under which distinct stakeholders recognize and exploit opportunities to integrate their influence.

### Limitations

All statistical studies have limitations and this effort is no exception. First, not all stakeholder groups were included in the analysis. Employees, government entities, suppliers, and rivals are a few of the many stakeholder groups not represented. Yet a large scale statistical study which could practically capture multi-dimensional salience measures for a comprehensive set of stakeholders is hard to imagine. Second, the regression models contain determinants of stakeholders' salience (e.g. competition) which are representations for alternative influences on organizational behavior. As possible, the unspecified influences were accounted for through the use of dummy variables (to capture latent industry effects) and organizational traits (e.g. size and performance) known to impact organizational outcomes.

### Summary

This research applied Stakeholder Theory to predict the performance outcomes of nonprofits. Overall, the pursuit of social or financial performance is determined by the salience of stakeholders whose interests are aligned with the outcome. Stakeholders external to the nonprofit (i.e. donors and beneficiaries) have the necessary clout to control the production of outcomes which primarily serve the interests of managers. Thus, although the absence of owners with residual rights seemingly provides managers with the necessary discretion to exploit the nonprofit for their personal gain, other sources of control effectively prevent such expropriation. The implication of these findings is regulators, donors, communities, or others who have specific expectations for nonprofits can affect the production of desired outcomes by monitoring the salience of stakeholders who possess the associated interest.

## CHAPTER 3

## WHO'S IN CHARGE? RECONCILING THE STRATEGIC DECISIONS OF NONPROFITS

## Introduction

This study investigates the relationship between environmental uncertainty and the strategic behavior of nonprofits. Nonprofits are substantial and critical contributors to social and economic welfare (Weisbrod, 1997; Wing, et al., 2008) and confront increasingly uncertain task environments. The relative decline of available resources (e.g. government grants, volunteers, donations) (Hall, 2010a; Wing, et al., 2008), the transfer of social responsibilities from government entities to nonprofits (Bush, 1992; Lammers, 1990), and the growing population of for-profit rivals in markets traditionally served by nonprofit ownership forms (e.g. healthcare, education) (Bielefeld & Murdoch, 2004; Wolff & Schlesinger, 1998) all represent how nonprofits' competitive environments are becoming increasingly uncertain. The underpinning presumption of scholars' research and prescriptive advice is that nonprofits undertake strategic actions to improve organizational stability as environmental uncertainty increases (D. A. Carroll & Stater, 2009; Chang & Tuckman, 1994; Kingma, 1993). These scholars explicitly reason that nonprofits which assume a more entrepreneurial and competitive orientation (Bush, 1992; Marwell & McInerney, 2005; Wolff & Schlesinger, 1998), or employ more professionally trained managers (Bush, 1992; Lammers, 1990), or adopt the policies and practices of for-profit organizations (Wolff & Schlesinger, 1998), or create alliances across nonprofit and for-profit governance structures (Abzug & Webb, 1999; Biel, 2002; O'Regan & Oster, 2000) all do so in an effort to counter environmental uncertainty.

However, some inconsistencies in the empirical findings exist. Alexander and Weiner (1998) did not detect a significant relationship between competition (a dimension of environmental uncertainty) and the structure of nonprofits' board of managers. Here, the structure of the board of managers represents an ability to stabilize the organization through superior decision-making and resource acquisition processes. Benjamin (2008b) concluded that nonprofits create instability through their efforts to attract relatively uncertain resources. Bielefeld (1992) found efforts by nonprofits to acquire additional revenue sources, advance their reputation, or retrench were influenced by the perceived need to reduce environmental uncertainty, but this influence was not consistent across or within industries.

This research reconciles the inconsistent relationship through an application of Stakeholder Theory. Stakeholder Theory, with a foundation based on integrating numerous stakeholder interests, is particularly well-suited for the study of organizations charged with balancing competing financial and social preferences (Connolly, et al., 1980; Dunn, 2010; Freeman, 1984; Mitchell & Agle, 1997). This study predicts stakeholders' salience moderates the relationship between environmental uncertainty and nonprofits' strategic decisions. More specifically, nonprofits' strategic decisions are based on the ability of salient stakeholders to diversify their (monetary or non-monetary) interests beyond the focal nonprofit.

#### Stakeholder Theory

Stakeholder Theory contends organizational behavior is guided by the need to manage stakeholders'<sup>18</sup> interests (Freeman, 1984; Mitchell & Agle, 1997). Stakeholders possess a variety of knowledge, capital, skills, and approvals nonprofits need to achieve their mission (Kaplan, 2001; Kushner & Poole, 1996; McHargue, 2003; Mottner & Ford, 2005; Ostrander, 2007; Seok-Eun, 2005; Speckbacher, 2003). Nonprofits jeopardize access to these critical resources and, in turn, the probability of achieving their mission if stakeholders' needs are not met. However, meeting all stakeholders' needs may not be efficient or possible. Thus, Stakeholder Theory suggests nonprofit managers should prioritize stakeholders (and their needs) according to salience; the combination of stakeholders' power (influence over organizational actions), legitimacy (reasonableness of stakeholder-organization interaction as defined by societal rules, practices, customs, values, and beliefs), and urgency (immediacy of stakeholder claims) (Mitchell & Agle, 1997; Pfeffer, 1992).

Stakeholder Theory has been applied to predict a variety of nonprofit outcomes or behaviors including financial and social performance (Harvey & Snyder, 1987; Hatten, 1982; Herman & Renz, 2008; J. McCarthy, 2007; Papadimitriou, 2007; Seok-Eun, 2005), collaborative service agreements (Abzug & Webb, 1999; Hee Soun & Feiock, 2007), accounting practices (Hyndman & McMahon, 2011), trust building (Dunn, 2010; Gugerty, 2009; Pirson & Malhotra, 2008), and online marketing (Saxton, Chao, & Brown,

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<sup>18</sup> Stakeholders include "any group or individual who can affect or is affected by the achievement of the organization's objectives" (Freeman, 1984, p. 46).



2007). This research concerns the use of Stakeholder Theory to predict nonprofits' response to environmental uncertainty.

#### Theoretical Framework

Not all nonprofits respond uniformly to environmental uncertainty (J. Alexander, 2000; J. Alexander, Nank, & Stivers, 1999; Biel, 2002; Chang & Tuckman, 1991; Grønbjerg, 1991a; Kingma, 1993; Miller-Millesen, 2003). Wolff and Schlesinger (1998) found increasing competition for clients caused nonprofit hospitals to admit more uninsured and underinsured patients. Such actions reduce the dependability of revenue streams and, in turn, the stability of the organization. Pearce and others (2010) discovered less munificent environments did not alter the effectiveness of an entrepreneurial orientation; their finding suggests environmental uncertainty should not influence nonprofits' strategic decisions. Contrasting findings such as these indicate the relationship between environmental uncertainty and nonprofits' strategic decisions is not completely understood.

This research asserts stakeholders moderate the relationship between environmental uncertainty and nonprofits' strategic behavior. The identification of stakeholders as the intervening factor is justified by the fact that nonprofits fulfill mandates to meet the needs of multiple constituents (Ben-Ner & Gui, 2003; Connolly, et al., 1980; Dunn, 2010; Easley & O'Hara, 1983; Hansmann, 1980). In addition, the perspective is supported by empirical findings in a for-profit context. Berman, Wicks, and others (1999) applied Stakeholder Theory and found stakeholders moderate the influence of strategy on organizational performance and that accounting for this effect weakened the influence of environmental uncertainty. However, not all stakeholders have equivalent influence and their influence varies across industries. Thus, a latent trait of stakeholders should account for the difference. This study contends the trait is the ability to diversify interests. The conclusion is based on the general presumption that nonprofits take actions to counter environmental uncertainty by improving organizational stability (Abzug & Webb, 1999; Biel, 2002; Bush, 1992; Lammers, 1990; Marwell & McInerney, 2005; O'Regan & Oster, 2000; Wolff & Schlesinger, 1998) and nonprofits emphasize the interests of their most salient stakeholders (Kaplan, 2001; Kushner & Poole, 1996; McHargue, 2003; Mottner & Ford, 2005; Ostrander, 2007; Seok-Eun, 2005; Speckbacher, 2003). Hence, the salient stakeholders define the uncertainty acceptable to the nonprofit. All else being

equal, salient stakeholders who *can* diversify their interests will encourage strategic decisions which reduce organizational stability (thereby exacerbating environmental uncertainty) and stakeholders who *cannot* diversify their interests will encourage strategic decisions which improve organizational stability (thereby mitigating environmental uncertainty). These relationships are summarized in Figure 3.

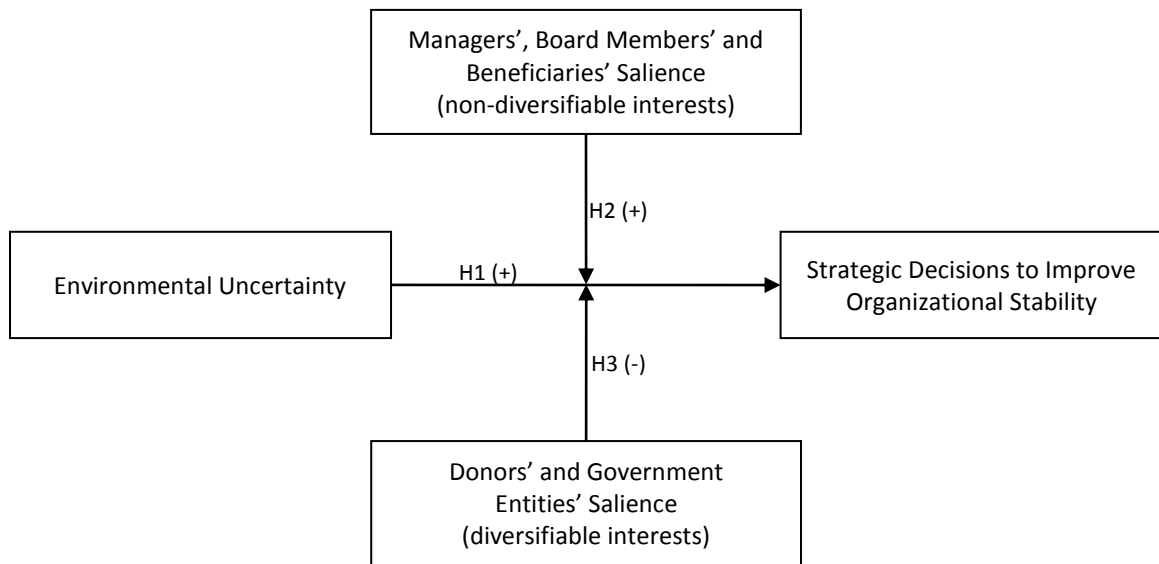


Figure 3 – Nonprofits' Strategic Decisions

#### Stakeholders with Less Diversifiable Interests

##### Managers

Senior managers typically derive the majority of their income and professional reputation from their employment. The majority of their time is guided by explicit and implicit employment contracts which encourage behavior consistent with their employer's interests (Bolton & Dewatripont, 2005; Gillan, Hartzell, & Parrino, 2009). Such contracts guide managers' financial relationships, interpersonal relationships, recreational activities, and social engagements. In addition, as their employment tenure increases, senior managers believe their knowledge, skills, competencies, and personal investments become increasingly specific to their employer (Bretz, Boudreau, & Judge, 1994). This inhibits managers' willingness to pursue alternative employment options because they believe their specialized human capital has less value to other employers. Thus, nonprofit senior managers, like their for-profit

counterparts, are unable to diversify or alter their economic and non-economic interests because their income is not diversified, their time and behavior is constrained by contract, and their evaluations regarding professional mobility are unfavorable (Bretz, et al., 1994; Eisenhardt, 1989; Jensen & Meckling, 1976).

#### *Board Members*

For board members of for-profit entities, the firm represents a minority share of their wealth and income (Bebchuk & Fried, 2003; Bloom & Milkovich, 1998; J. S. Miller, Wiseman, & Gomez-Mejia, 2002; Zajac & Westphal, 1994). This implies their economic investment in a relatively risky organization can be offset through additional investments in relatively safer organizations (i.e. investment diversification) (Eisenhardt, 1989; Jensen & Meckling, 1976). However, in nonprofit contexts, presumptions concerning risk tolerances require modification. Nonprofit board members do not have equity positions and do not receive financial compensation for governance services. Instead, they serve for altruistic and intrinsic reasons including the desire to develop their human and social capital, improve their reputation, contribute to society, enhance their self-worth, and engage in self-healing (Clary, et al., 1998; Inglis, 1994; Inglis & Cleave, 2006; Jamison, 2003; Laverie & McDonald, 2007; Randle & Dolnicar, 2009; Searle, 1989; Wymer Jr & Samu, 2002). Conclusions regarding nonprofit board members' risk tolerance should be based on their ability to diversify *altruistic* or *intrinsic* rather than economic investments. In fact, nonprofit board members' non-economic investments are minimally diversified. While some board members contribute gifts to numerous organizations, they generally donate their governance services (i.e. time) to one or two nonprofits (Inglis, 1994; Inglis & Cleave, 2006; Miller-Millesen, 2003; Preston & Brown, 2004; Searle, 1989). The Bureau of Labor Statistics reported 90% of volunteers, directors and non-directors, dedicate their time to a two or fewer nonprofits (2010) and BoardSource® reported nonprofit board members, on average, serve on two nonprofit boards (2010).

#### *Beneficiaries*

Beneficiaries are the individuals or groups who are defined by the nonprofit's mission as the intended recipients of the nonprofit's goods or services. While others such as employees, managers,

suppliers, and volunteers experience benefits from their relationship with the nonprofit, these constituents are not the nonprofit's reason for existence and, hence, are not included as beneficiaries.

Many beneficiaries are unable to diversify their interests because the nonprofit serves as one of the few, if not sole, providers of necessities such as healthcare, food, clothing, or shelter (Baruch & Ramalho, 2006; Boyne, 2003; Cairns, et al., 2005; Green & Griesinger, 1996; Hallock, 2002; Hasenfeld & Schmid, 1989a; Jackson & Holland, 1998; Moore, 2000; Napoli, 2006; Nichols, 2001; Rosenau & Linder, 2003; Young, 1998). Some theorized nonprofits exist for the purpose of fulfilling demand for public goods which is not provided by the private (economically unviable) or public (politically unviable) sectors (Langton, 1987; Weisbrod, 1986). Thus, beneficiaries are not given the opportunity to diversify their interests. If multiple good or service providers are available, often the circumstances (e.g. disability, disease, addiction, socio-economic status) defining beneficiaries' eligibility perpetuates their reliance on a single nonprofit (Baruch & Ramalho, 2006; Cairns, et al., 2005; Napoli, 2006; Rosenau & Linder, 2003). Thus, like managers and board members, beneficiaries too are unable to diversify their interests.

#### *Stakeholders with More Diversifiable Interests*

##### *Donors*

Statistics indicate individual donors, who through direct gifts and bequests account for 83% of all gifts (Center on Philanthropy at Indiana University, 2009, 2010), contribute a minority share of their wealth across numerous nonprofits. The individual gift, however, constitutes a minority of each nonprofit's gift revenue. In the US in 2009, annual median household giving was \$870 (Center on Philanthropy at Indiana University, 2010), or 1.7% of median household income (DeNavas-Walt, Proctor, & Smith, 2010). Studies (e.g. Eikenberry & Bearman, 2009; Hall, 2010b) also found individuals typically spread their gifts amongst eight to ten different nonprofits. Thus, relative to managers, board members, and beneficiaries, donors are indifferent to nonprofits' vulnerability because donors can diversify their interests.

##### *Governments*

Government entities are stable and substantial supporters of nonprofits. Their financial support for nonprofits includes grants, fee-for-service contract payments, forfeited tax receipts (on the

organization's income and the reduced tax liability of donors), and subsidies such as loan guarantees and no-interest loans. Between 1995 and 2005, government grants and contract payments ranged between 29% and 48% of total revenues for public charities. More precisely, government grants and contracted payments represented 9% and 20% respectively of the \$1.1 trillion in revenue for 876,164 organizations registered as public charities<sup>19</sup> in 2005. Thus, the average annual grant per public charity in 2005 totaled approximately \$113,000 (National Center for Charitable Statistics, 2009; Wing, et al., 2008) which means each charity received less than one-thousandth of a percent of the grants made by government entities. Hence, government entities' interests in nonprofit organizations are highly diversified.

The above describes the ability of various stakeholders to diversify their interests in nonprofits. Predictions regarding stakeholders' consequential impact on the strategic decisions of nonprofits require the establishment of an underpinning relationship between environmental uncertainty and the strategic decisions of nonprofits. Environmental uncertainty, as formulated by Dess and Beard (1984), consists of munificence, dynamism, and complexity. Munificence is the environment's capacity to sustain growth. Munificent environments represent less uncertainty because sales targets are achieved easier, resource reserves are built faster, and rivals' competitive actions are less significant and frequent. Dynamism is the proportion of unpredictable change in the environment. Unpredictable change increases uncertainty by disconnecting planning from organizing and inhibiting consensus during strategic decision processes (Haleblian & Finkelstein, 1993). Complexity is the range of possible alternatives for organizations to combine acquisition, production, and distribution activities. More complex markets, where a greater range of combinations is acceptable, increase uncertainty because managers face greater "information-processing requirements" (Dess & Beard, 1984, p. 56; Galbraith, 1973; Sakamoto, 1980). Based on the logic and findings of others (Child, 1997; Dess & Beard, 1984; Forbes & Milliken, 1999; Fredrickson & Mitchell, 1984; Iaquinto & Fredrickson, 1997; Schwenk, 1984; Swamidass & Newell, 1987), this study predicts managers create more structured, incremented, and rationalized strategic decisions processes when confronted with environmental uncertainty. These modifications have the intention of improving organizational stability.

<sup>19</sup> Public charities account for 63% of all nonprofits.

*Hypothesis 1. Increasing environmental uncertainty causes nonprofits to implement strategic decisions which improve organizational stability.*

The essence of this study is about how the relationship between environmental uncertainty and nonprofits' strategic decisions gets moderated by the salience of stakeholders. The second hypothesis emerges from the argument that some nonprofit stakeholders; managers, board members, and beneficiaries; share an inability to diversify their interests which causes them to encourage stability-reinforcing, strategic decisions as environmental uncertainty increases.

Managers' and board members' interests are linked to the nonprofit's performance. That is, the extent to which board members improve their reputation, contribute to society, or build their self-esteem depends on the performance of the nonprofit (Clary, et al., 1998; Inglis, 1994; Inglis & Cleave, 2006; Searle, 1989). Likewise, managers' employment, pay, and benefits continue and improve based on the nonprofit's success (T. Carroll, et al., 2005; Dart, 2004; Sorensen & Grove, 1977). The attribution of nonprofits performance on to managers' and board members' interests causes these stakeholders to prefer strategic decisions which prioritize organizational stability as environmental uncertainty increases. This conclusion is based on the fact that performance evaluations for nonprofits are complex and failed nonprofits cause disproportionate reputational harm to the affiliated managers and board members. First, the complexity of performance evaluations provides managers and board members with greater latitude in connecting their performance to positive outcomes produced by the charity. Nonprofits pursue relatively subjective and intangible missions through ambiguous processes which combine with exogenous factors to affect social conditions (Baruch & Ramalho, 2006; Easley & O'Hara, 1983; Hansmann, 1980; Herman & Renz, 1999; Kaplan, 2001; Nobbie & Brudney, 2003; Siciliano, 1996; Sorensen & Grove, 1977; Sowa, et al., 2004; Speckbacher, 2003). Such causal ambiguity encourages many practitioners, regulators, and researchers to adopt a social-constructivist (Berger & Luckmann, 1966) approach to measuring nonprofit performance; good performance is whatever stakeholders deem it to be (Amirkhanyan, et al., 2008; Boyne, 2003; Green & Griesinger, 1996; Green, et al., 2001; Herman & Renz, 1997; Knox, et al., 2006; Kushner & Poole, 1996; Napoli, 2006; Nobbie & Brudney, 2003; Siciliano, 1996). The implication is managers and board members advance their interests based on organizational

performance evaluations held by others. Second, managers and board members flee financially vulnerable charities as a means of protecting their professional reputation (Chang & Tuckman, 1991). Reputation has been associated with managers' ability to acquire, advance, and retain employment (Fizel & D'Itri, 1999; Giambatista, Rowe, & Riaz, 2005). Thus, managers and board members defect from nonprofits as failure becomes more likely out of a need to improve future employment opportunities. The above indicates managers and board members share a priority to preserve the nonprofit rather than maximize its impact. Encouraging conservative strategic decisions improves nonprofits' survival which has the dual benefit of avoiding reputational damage while perpetuating various assessment criteria by which managers and board members can confirm their competency and worth.

Beneficiaries' interests concern the quality and availability of products offered by nonprofits. Nonprofits often serve as one of the few, if not sole, providers of necessities such as healthcare, food, clothing, or shelter (Green & Griesinger, 1996b). As environmental uncertainty increases, nonprofits - especially adept at recognizing the needs of their beneficiaries (Fisman & Hubbard, 2003; LeRoux, 2005; Nichols, 2001) - are encouraged to take actions which maintain or improve the availability of such necessities. A common approach to stabilize the nonprofit and, in turn, its products is to develop supplemental revenue sources (J. Alexander, 2000; D. A. Carroll & Stater, 2009; Chang & Tuckman, 1994; Kingma, 1993). Subsidizing discounted or charitable services with government grants, non-mission-related revenues, or investment income allows nonprofits to diversify their revenue streams and improve the likelihood of their survival.

In sum, the increasing influence of stakeholders who cannot diversify their interests (i.e. managers, board members, and beneficiaries) encourages nonprofits to compensate for environmental uncertainty by implementing strategic decisions which improve organizational stability.

*Hypothesis 2. Stakeholders' salience moderates the effect of environmental uncertainty on nonprofits' strategic decisions. Increasing salience for stakeholders who cannot diversify their interests causes the nonprofit to implement strategic decisions which improve organizational stability.*

Conversely, the third hypothesis suggests stakeholders who can diversify their interests influence nonprofits to make strategic decisions which heighten organizational instability. Donors and government entities represent such stakeholders.

Donors' influence is based on the expectations for organizational efficiency. Donors prefer nonprofits direct gifts towards mission-related causes rather than financial vulnerabilities (Green & Griesinger, 1996; Hibbert & Horne, 1996; Kushner & Poole, 1996; Myers, 1990; D. H. Smith & Shen, 1996). Numerous resources (e.g. charitynavigator.com, the American Institute of Philanthropy, The Center on Philanthropy at Indiana University) assist donors with comparing nonprofits in terms of the proportion of resources directed toward mission-related services and fundraising efficiency<sup>20</sup>. Thus, to attract gifts, nonprofits' strategic decisions are formulated and executed to manage these ratios as a means of conveying efficiency and effectiveness (Crittenden, 2000; Froelich, 1999; Nichols, 2001; Riecken, Babakus, & Yavas, 1994; Trussel, 2003). In addition, donors have become more astute in designing gifts which assure compliance with donors' intentions (Kottasz, 2004; Nichols, 2001; Schervish, 2007; Shapiro, 1974; Van Slyke, et al., 2007). For example, matching gifts require nonprofits integrate support from other donors or stakeholders, restricted gifts mandate resource allocations, and staged or laddered gifts require nonprofits maintain commitments beyond the short term. The combination of nonprofits' efforts to attract gifts and fulfill gift conditions has the effect of concentrating nonprofits' revenue sources and expense allocations. These strategic decisions reduce the amount of discretionary resources available and, in turn, nonprofits' stability (Chang & Tuckman, 1991).

Government entities, similar to donors, also cause nonprofits to make strategic decisions which accept lower levels of stability. Generally, government entities award grants and fee-for-service contracts to nonprofits based on need, potential, and legitimacy (Moody, 1996; Rose-Ackerman, 1996; Yetman & Yetman, 2003). To demonstrate these traits, nonprofits tightly manage administrative expenses, limit revenue and expenses not related to the mission, and implement accounting policies which simultaneously convey organizational need and strength (Andreoni & Payne, 2001; Hallock, 2002; S. R. Smith & Lipsky, 1995). Administrative expenses are a source of slack (Antle & Eppen, 1985; G. George,

<sup>20</sup> Fundraising efficiency is the administrative cost of acquiring charitable contributions.



2005; L. J. Bourgeois, 1981; Singh, 1986) for nonprofits. By minimizing administrative expenses, nonprofits signal leanness or efficiency to government entities; this decreases their ability to counter competitive stresses through the elimination of indirect, administrative expenditures (Chang & Tuckman, 1991). In addition, government entities, similar to donors, bound nonprofits' expenditures and operational activities through contracted policies and procedures (Moody, 1996; S. R. Smith & Lipsky, 1995). Fee-for-service payments have stipulations regarding allowable expenses and project grants accompany conditions of use and require subsequent reports concerning project status and impact. Such controls have the effect of reducing activities and planning outside the scope of the grant. Thus, as government entities become more salient, nonprofits strategic decisions favor contract-associated activities. The preference produces a more circumscribed strategic posture for nonprofits which reduces their stability.

Thus, the increasing influence of stakeholders who can diversify their interests (i.e. donors and government entities) encourages nonprofits to take actions which reduce their stability and, in turn, their vulnerability to environmental uncertainty.

*Hypothesis 3. Stakeholders' salience moderates the effect of environmental uncertainty on nonprofits' strategic decisions. Increasing salience for stakeholders who can diversify their interests causes the nonprofit to implement strategic decisions which reduce organizational stability.*

## Methodology

### *Data and Sample*

The data come from GuideStar<sup>21</sup>, the National Center for Charitable Statistics (NCCS), and directly from the nonprofits included in the research sample. The study includes five years of data (2004 through 2008) for 134 charities, the most significant<sup>22</sup> tax-exempt category of nonprofits (Wing, et al., 2008). The 134 charities were chosen at random from 1358 organizations that (1) filed as 501(C)(3) organizations for each year of the study; (2) reported greater than zero values for Total Revenue, Total Expenses, and Total Assets in each year; (3) continued activities beyond 2009; and (4) were classified according to the National Taxonomy of Exempt Entities (NTEE) decile groups as Symphony Orchestras, Theater, Rehabilitative Care, Residential Mental Health Treatment, Employment Preparation & Procurement, or Senior Citizens

<sup>21</sup> <http://www.guidestar.com>

<sup>22</sup> Determination is based on the number of organizations, total expenses, and total assets.

Housing & Retirement Communities. These NTEE decile groups were chosen because they represent the three largest major groups of charities (Arts, Culture, & Humanities; Health; and Human Services) and because the size of their 10% samples would not dominate, or be dominated by, the study population. Table 9 describes the research sample.

#### *Dependent Variables*

The hypotheses predict if nonprofits' strategic decisions improve or reduce organizational stability. Nonprofits mitigate environmental uncertainty by (1) diversifying revenue sources (J. Alexander, 2000; J. Alexander, et al., 1999); (2) diversifying expenditures – to cultivate supplemental activities as insurance against tenuous business models (J. Alexander, 2000; J. Alexander, et al., 1999); (3) emphasizing government revenues - because it is relatively stable (Grønbjerg, 1991a, 1991b; Kingma, 1993); (4) reducing program expense volatility – to prepare for changes in revenue (J. Alexander, 2000; J. Alexander, et al., 1999); (5) increasing financial slack (Chang & Tuckman, 1991); and (6) establishing inter-organizational relationships – to share resources, absorb shocks, and accumulate knowledge (Biel, 2002; Miller-Millesen, 2003). From these choices, revenue diversification and expense diversification are selected to describe the effect of nonprofits' strategic decisions on organizational stability. These measures capture the revenue and expense constructs included in the other measures of government revenue, expense volatility, and slack; and they are distinct from the organizational traits used to create the independent variables. In addition, using both revenue and expense diversification eliminates ambiguity concerning the bi-directional relationship between them. From the fundraising perspective, nonprofit expense allocations reinforce and validate the organization's mission which attracts financial resources from donors and grant-makers (Crittenden, 2000; Froelich, 1999; Riecken, et al., 1994; Trussel, 2003). Conversely, from the accounting and governance perspective, revenue sources dictate expense allocations through gift conditions, gift forms, and temporary restrictions (Benjamin, 2008b; Cordes, Henig, Twombly, & Saunders, 1999; Froelich, 1999). To avoid complications produced by reciprocal causality, both forms of diversification are combined to represent the organizational stability produced by nonprofits' strategic decisions.

The formula for calculating revenue diversification is one less the sum of squared revenue sources as a share of Total Revenue for the nonprofit (Chabotar, 1989; Chang & Tuckman, 1991). Expense diversification is calculated similarly except expense allocations and Total Expenses are used in place of revenue sources and Total Revenues.

$$\text{Revenue Diversification} = 1 - \sum_{i=1}^n \left( \frac{\text{Revenue Source}_i}{\text{Total Revenue}} \right)^2$$

$$\text{Expense Diversification} = 1 - \sum_{i=1}^n \left( \frac{\text{Expense Allocation}_i}{\text{Total Expense}} \right)^2$$

The measure of organizational stability derived from nonprofits' strategic decisions (*Strategic Decisions*) is the sum of the two standardized diversification calculations. Increasing values of the dependent variable equate to increasing organizational stability and decreasing values equate to reducing organizational stability.

#### *Independent Variables*

Dess and Beard's (1984) dimensions of munificence, dynamism, and complexity are applied to capture environmental uncertainty. Munificence is the environment's capacity to sustain growth. Munificence is calculated as the study period's (five years) average growth of aggregated revenues for charities in the same state and with the same NTEE codes (Amirkhanyan, et al., 2008; Boyd, 1995; Harrington & Kendall, 2005). The measure of munificence is inversely related to environmental uncertainty.

Complexity describes the intensity and concentration of competition (Dess & Beard, 1984; Harrington & Kendall, 2005). Competition is measured as the revenue market share belonging to charities with greater than \$5M in total revenue. The market is set according to charities' NTEE code (Amirkhanyan, et al., 2008; Nobbie & Brudney, 2003) and state (Feigenbaum, 1987). The measure replicates the concept underpinning the Herfindahl-Hirschman Index (HHI) (R. A. Miller, 1982) where values approaching one represent monopolistic conditions and calculations approaching zero equate to highly competitive, complex, and uncertain environments (Boyd, 1995). The measure has been

demonstrated to correlate with alternative measures of complexity including industry size and the number of competitors (Harrington & Kendall, 2005).

Dynamism is measured as sales volatility for the study period. Again, total revenues are summed by state and NTEE code. These values are then regressed against the study-period's time variable (i.e. YR1, YR2, YR3, YR4, and YR5). Following Boyd's (1995) precedent, the standard error of the coefficient was divided by average total revenue for the five year period (Boyd, 1995; Harrington & Kendall, 2005; Li & Simerly, 1998). Greater values of dynamism represent increases in sales volatility and environmental uncertainty.

Environmental uncertainty (*Environmental Uncertainty*) is created through the following steps. First, all dynamism observations are subtracted from one (maximum value is 0.200943) so its relationship to environmental uncertainty (decreasing values equate to more uncertainty) parallel those of munificence and complexity. Second, munificence, complexity, and dynamism values are standardized and then summed. Third, the resulting sum is then subtracted from three (maximum value is 2.59) so greater values represent greater environmental uncertainty. Fourth, the resulting inverted value undergoes a square root transformation to compensate for its right-tailed distribution. The square root transformation changes skewness from 4.469 to 1.449 and kurtosis from 33.221 to 7.344.

The salience of stakeholders who cannot diversify their interests (*Salience – Stakeholders without Diversifiable Interests*) is the sum of standardized salience measures for managers, board members, and beneficiaries.

Managers' salience is the number of years the senior manager of the nonprofit has served as the senior manager. Each year of employment is a validation of performance by the supervising board of managers which improves senior managers' ability to influence and increases their vested interest in the nonprofit. This is evidenced by associations between senior manager tenure and pay, organizational performance, and organizational behavior (Jobome, 2006; Oster, 1998; Preston & Brown, 2004; Young, 2001).

Board members' salience is the number of board members serving the nonprofit (Olson, 2000). Board size has been associated with various strategic behaviors (e.g collaboration and commercial

endeavors) and numerous measures of nonprofit effectiveness and efficiency (de Andres-Alonso, et al., 2006; Eadie, 2006; Green & Griesinger, 1996; Herman & Renz, 1998, 1999, 2008; Jackson & Holland, 1998; Miller-Millesen, 2003; J. L. Miller, 2002; Provan, 1980).

Beneficiaries' salience is the sum of standardized values for (1) the proportion of Total Program Fees and Membership Dues to Total Revenue and (2) the relative specificity of the nonprofit's mission and impact statements. Pfeffer and Salancik (1978) explain power or the ability to influence is possessed by those who reduce uncertainty (Casciaro & Piskorski, 2005; Pfeffer, 1981; Pfeffer & Salancik, 1978). For nonprofits, where business models are vulnerable (J. Alexander, 2000; J. Alexander, et al., 1999; Easley & O'Hara, 1983; Hansmann, 1980), gatekeepers of revenue have substantial influence on organizational behavior (e.g. J. Alexander, 2000; Bielefeld, 1992; Grønbjerg, 1991a, 1991b; Kingma, 1993; LeRoux, 2005; Nichols, 2001) (Pfeffer, 1981; Pfeffer & Salancik, 1978). The amount of revenue provided by beneficiaries through program fees and membership dues represents the amount of uncertainty beneficiaries eliminate and their corresponding salience to the nonprofit. The second dimension of beneficiaries' salience is based on mission and impact statements. The urgency and legitimacy of beneficiaries is determined by how specifically nonprofits identify them. Specific mission statements narrowly define the targeted beneficiary by traits such as age, gender, or condition and they establish the nonprofit's uniqueness. Hence, the beneficiaries of nonprofits with relatively specific mission statements are not likely to have their needs met by other organizations. This suggests such beneficiaries will experience greater urgency to make a claim and the nonprofit is likely to attribute greater legitimacy to their claims. Both conditions increase beneficiaries' salience. To measure the specificity of nonprofits' missions, an instrument (Appendix) was created. It assessed the degree to which the sampled nonprofits defined their beneficiaries by needs, demographic traits, and geographic membership. Three business administration doctoral students and a manager of a charitable organization completed a seven-point, Likert scale evaluation for the 134 organizations in the sample. The inter-rater reliability of their assessments was confirmed with a Cronbach's Alpha score of 0.885 (Cronbach, 1951; D. George & Mallery, 2003) and an average Pearson correlation of 0.703.

Donors' and government entities' salience (*Salience – Stakeholders with Diversifiable Interests*) is calculated through their provision of revenue as gifts (i.e. donations and grants respectively). Donors' salience is calculated as the proportion of Total Public Support to Total Revenue (Brown, 2005; Duque-Zuluaga & Schneider, 2008; Greenlee & Bukovinsky, 1998; Ritchie & Kolodinsky, 2003; Ritchie, et al., 2007; Siciliano, 1996). The salience of government entities is the proportion of Government Grants to Total Revenue.

#### *Control Variables*

The control variables account for nonprofits' size and their relative performance. Organizational size has been associated with strategic decisions which reduce organizational stability. Smaller nonprofits tend to be newer, more unstable organizations because they are more specialized (Bess, 1998) and less attractive to prestigious community members (Dart, et al., 2006; Mathiasen, 1990; M. M. Wood, 1992). Newer nonprofits prioritize revenue and expense activities directly related to mission-defined beneficiaries. The supporting management processes, meanwhile, are neglected because they are perceived as less relevant to survival (Hasenfeld & Schmid, 1989b). Such decisions cause nonprofits to centralize their revenue sources and program expenses. Also, younger nonprofits fail more frequently (Bielefeld, 1994) and have less-refined reputations which inhibits the recruitment of prestigious community members as leaders. Thus, the leaders who accept service invitations are those less in demand because their social contacts are fewer and less lucrative. The fundraising efforts of these leaders produce fewer and smaller donations. By default, then, the nonprofit is less stable since it is more reliant on fewer revenue sources. Finally, smaller organizations are less restricted by asset commitments (Musella, Destefanis, & Young, 2009). Smaller nonprofits by definition have a smaller asset base with fewer restricted assets. Hence, any given strategic decision is perceived as less substantial because it jeopardizes fewer assets (Bess, 1998). Nonprofits' size (*Organizational Size*) is defined by their average net assets (Feigenbaum, 1987; Golensky, 2008; Jobome, 2006; Olson, 2000; Oster, 1998; Ritchie & Eastwood, 2006; Ritchie, et al., 2007; Siciliano, 1996; Zimmermann & Stevens, 2006).

This study also controls for the relative financial performance of the nonprofit (*Relative Organizational Performance*). Two arguments suggest strong performance will cause nonprofits to reduce

organizational stability. First, the accumulation of financial slack is associated with superior economic performance. As a result, negative strategic decision outcomes represent a smaller proportion of financial reserves for well-performing nonprofits (Bromiley, 1991; G. George, 2005; Singh, 1986). Thaler and Johnson's (1990) experiment supported this dynamic by finding decision-makers accept greater risk when prior performance produces surplus resources. The authors contended decision-makers were more willing to accept risk under these conditions because they were risking "house money." Second, the "Red Queen effect" (Derfus, Maggitti, Grimm, & Smith, 2008) implies nonprofits need to improve continually, not just maintain, their performance. Good performance escalates the reference point by which stakeholders evaluate future performance (Tversky & Kahneman, 1991). Furthermore, failing to achieve stakeholders' expectations produces a disproportionately negative effect for leaders (Rozin & Royzman, 2001). The combination of greater expectations and greater penalties increases leadership's need and willingness to reduce organizational stability. Nonprofits' relative financial performance is the difference between the focal nonprofit's total asset turnover and the average total asset turnover of other nonprofits sharing the same NTEE and state (Chabotar, 1989; Chang & Tuckman, 1991; Kushner & Poole, 1996; Ritchie & Kolodinsky, 2003).

#### *Analysis*

The strategic decisions of nonprofits were estimated using ordinary least squares regression (OLS) multiple regression analysis. Three regression models test the hypotheses. The reduced model (Model I) controls for organizational size, relative organizational performance, and latent factors in each industry through dummy variables (Theater, A65 is the referent industry).

Hypothesis 1 establishes the general relationship between environmental uncertainty and the strategic decisions of nonprofits. The relationship is tested through the second regression model (Model II). Confirmation that nonprofits make strategic decisions which reduce organizational stability is observed through a statistically significant, positive coefficient for environmental uncertainty (greater amounts of environmental uncertainty cause nonprofits' strategic decisions to increase the diversification of revenues and expenses).

Hypothesis 2 and 3 assert the salience of stakeholders moderates the effect of environmental uncertainty on nonprofits' strategic decisions. Salient stakeholders who cannot diversify their interests encourage strategic decisions which increase organizational stability while salient stakeholders who can diversify their interests embolden strategic decisions which reduce organizational stability. Both relationships are tested in the third regression model (Model III). The former relationship (hypothesis 2) is confirmed if the coefficient for the salience of stakeholders who cannot diversify their interests is positive in Model II. The later relationship (hypothesis 3) is confirmed if the coefficient for the salience of stakeholders who can diversify their interests is negative in Model II.

### Results

Table 17 provides descriptive statistics and a correlation matrix for the variables. Evidence of multicollinearity amongst variables is absent; variance inflation factors (VIF) ranged from 1.011 to 1.883. The sample organizations substantially differ in terms of size (mean Assets are \$5,007 with a standard deviation of \$8,781) and their relative performance (average TAT of 2.19 with a standard deviation of 23.73).

*Table 17 – Descriptive Statistics and Correlation Matrix*

Variable	Mean	Std. Deviation	N	1	2	3	4	5
1 Strategic Decisions	0.000	1.678	670					
2 Organizational Size	5,007,186	8,781,408	670	0.155 **				
3 Relative Organizational Performance	2.190	23.730	667	-0.055	-0.040			
4 Environmental Uncertainty	1.666	0.475	670	0.081 *	-0.020	-0.044		
5 Sallience - Stakeholders without Diversifiable Interests	0.000	1.191	670	0.341 **	-0.099 *	0.007	0.055	
6 Sallience - Stakeholders with Diversifiable Interests	0.020	1.567	652	-0.100 *	0.181 **	0.033	-0.141 **	-0.321 **

\* p ≤ .05 level (2-tailed)

\*\* p ≤ .01 level (2-tailed)

The regression results displayed in Table 18 represent environmental uncertainty's and stakeholders' influence on nonprofits' strategic decisions. The statistical significance and direction of the independent variables' coefficients in the three regression models support all hypotheses.



Hypothesis 1 is supported by the negative and statistically significant value for environmental uncertainty in Model II. Furthermore, the amended regression model retains statistical significance and its adjusted  $R^2$  value increases from 0.338 (Model I) to 0.343 (Model II).

For hypothesis 2 and 3, all the necessary regression values change as predicted. First, environmental uncertainty loses its statistical significance as the moderating variables are included. Second, the moderating variables (stakeholder salience) produce statistically significant coefficients in the predicted directions – positive for stakeholders who cannot diversify interests and negative for stakeholders who can diversify interests. And third, Model III remains statistically significant while producing an adjusted  $R^2$  value (0.405) greater than Model II.

#### Discussion

This study applied Stakeholder Theory to explain and demonstrate how stakeholders' salience moderates the relationship between environmental uncertainty and the strategic decisions of nonprofits. The findings contribute greater depth to Stakeholder Theory and require an important modification to future nonprofit research.

Stakeholder Theory contains a bias for the focal organization. The influence of stakeholders is based on the organization's perspective of which stakeholder is the most salient. This approach does not account for how salient the organization is to the stakeholder. The difference concerns stakeholders' motivation to influence the behavior of the organization. If stakeholders have numerous alternatives for affecting their will, their chosen alternative will likely be, from their perspective, the most salient one. Thus, the expected influence of salient stakeholders on an organization may not be observed because the salient stakeholders have chosen to enact their will through an organization more salient to them. This dynamic is demonstrated by comparing stakeholders who can diversify their interests against those who cannot. Nonprofits are relatively more salient to stakeholders who cannot diversify their interests. To protect their interests, such stakeholders encourage nonprofits to make decisions which improve organizational stability to counter environmental uncertainty. Statistically, the difference is shown in each stakeholder group's Beta coefficient. For stakeholders who cannot diversify their interests, the Beta of

Model III is 0.232. This effect is more than double the effect of stakeholders who can diversify their interests (Beta = -0.094).

*Table 18 – Predictors of Nonprofits' Strategic Decisions*

Independent Variable	Strategic Decisions			
		Model I	Model II	Model III
(Constant)	B	1.002 **	0.495 *	0.724 **
	Std. Error	0.123	0.244	0.235
Symphony Orchestras	B	0.382 *	0.359	0.120
	Std. Error	0.185	0.184	0.179
	Beta	0.079	0.074	0.025
Rehabilitative Care	B	-0.880 **	-0.856 **	-0.780 **
	Std. Error	0.175	0.174	0.168
	Beta	-0.198	-0.193	-0.176
Mental Health & Crisis Intervention	B	-1.634 **	-1.571 **	-1.505 **
	Std. Error	0.171	0.172	0.165
	Beta	-0.379	-0.364	-0.349
Employment Preparation & Procurement	B	-1.661 **	-1.597 **	-1.962 **
	Std. Error	0.193	0.195	0.191
	Beta	-0.328	-0.315	-0.387
Low-Income & Subsidized Rental Housing	B	-2.147 **	-2.156 **	-1.893 **
	Std. Error	0.161	0.160	0.166
	Beta	-0.539	-0.542	-0.476
Organizational Size	B	0.000 **	0.000 **	0.000 **
	Std. Error	0.000	0.000	0.000
	Beta	0.095	0.102	0.130
Relative Organizational Performance	B	-0.003	-0.002	-0.002
	Std. Error	0.002	0.002	0.002
	Beta	-0.039	-0.037	-0.034
Environmental Uncertainty	B		0.293 *	0.133
	Std. Error		0.122	0.118
	Beta		0.079	0.036
Salience - Stakeholders <u>without</u> Diversifiable Interests	B			0.320 **
	Std. Error			0.052
	Beta			0.232
Salience - Stakeholders <u>with</u> Diversifiable Interests	B			-0.098 **
	Std. Error			0.036
	Beta			-0.094
	N	648	648	648
	Adj. R2	0.338	0.343	0.402
	ΔR2	0.346 **	0.006 *	0.059 **
	F Ratio	48.352 **	43.343 **	44.479 **

\* p < .05

\*\* p < .01

A consequence of the preceding is, for nonprofits, salient stakeholders define where environmental uncertainty resides. For nonprofits dependent on donors or government grants, uncertainty resides in the future allocation of resources brokered by these stakeholders. Acquiescing to these stakeholders' preferences; reducing fundraising expenses, eliminating administrative structures, adhering to strict contract mandates, etc.; increases nonprofits' vulnerability to environmental uncertainty. Such nonprofits must confront the challenge of becoming more entrepreneurial as a

response to greater competition for government grants<sup>23</sup> while their simultaneous reliance on grants inhibits the accumulation of discretionary resources needed for entrepreneurial pursuits.

On the other hand, as the salience of managers, board members, and beneficiaries increases, the uncertainty faced by the nonprofit is defined as the continued employment of managers, the value of board members' voluntary service, and the availability of services demanded by beneficiaries. To compensate, nonprofits supplement service programs by marketing unrelated activities or soliciting alternative funding sources (e.g. corporate philanthropy, charitable gift annuities) all in an effort to protect the interests of these salient stakeholders who cannot diversify their interests. In such circumstances the challenge of the nonprofit is to resist excessive mission creep (Moore, 2000). Such creep can derive from efforts to attract beneficiaries in need of less help, grow income from unrelated business activities, or divest from capital-intensive, charitable activities.

#### Limitations

All statistical studies have limitations and this effort is no exception. First, not all stakeholder groups were included in the analysis. Employees, suppliers, and rivals are a few of the many stakeholder groups not represented. Yet a large scale statistical study which could practically capture multi-dimensional salience measures for a comprehensive set of stakeholders is hard to imagine. Second, the measure of salience combines stakeholders. Particular stakeholders are not distinguished for their disproportionate or contradicting influence over nonprofits' strategic decisions. Third, the study period represents a relatively stable economic period in the US. A more persuasive study would demonstrate the moderating effect of stakeholder salience during and after the financial crisis of 2008.

#### Summary

This research explains how stakeholders influence the strategic decisions of nonprofits based on stakeholders' ability to diversify interests. Empirical findings support predictions that this ability moderates the relationship between environmental uncertainty and nonprofits' strategic decisions. The study contributes to Stakeholder Theory because it has shown how salience is sensitive to perspective. To

<sup>23</sup> Greater competition for government grants based on declining tax bases as a result of economic stagnation and a 30% growth rate in the number of nonprofits (National Center for Charitable Statistics, 2009)

understand, predict, and prescribe nonprofits' strategic decisions, assessments of reciprocal salience, between the focal organization and its array of stakeholders, are necessary.

## CONCLUSION

The theoretical contributions produced by this research involve Nonprofit Theory and Stakeholder Theory. The first study integrated Nonprofit Theory and Entrepreneurship Theory to predict the formation of nonprofit organizations. The most impactful finding was the frequency with which principles of Nonprofit Theory were inapplicable. That is, Nonprofit Theory is better characterized as “Nonprofit Hospital Theory.” Furthermore, the limited predictive factors of nonprofit theory – demand heterogeneity, social cohesiveness, government spending – were critically altered by labor productivity, competition, asset intensity, and the abundance of financial and intellectual capital. These findings should better inform managers, donors, and those who set public policy about the contexts under which nonprofits thrive and advance social and economic conditions.

These studies also built Stakeholder Theory by comparing the determinants of stakeholders’ influence and demonstrating how such influence provides a governance function. The determinants of stakeholders’ influence which were related to financial resources had stronger effects. Government grants (board members), private and restricted giving (donors), and program fees (beneficiaries) were more effective predictors of the associated stakeholder’s interests than other salience determinants such as board size, competition, or mission specificity. The implication of this result is stakeholders who have a greater proportion of their salience determined by their control over financial resources are prioritized. However, the influence of stakeholders’ is not inherently preferable to that of managers. While stakeholders were associated with controlling the interests exclusive to managers (despite the absence of equity-based motivators), their increased salience was also associated with less desirable outcomes (e.g. increased board members salience decreased nonprofits’ financial performance). This research also found the influence of stakeholders not only depends upon their salience to the organization, but also the organization’s salience to stakeholders. The former dictates stakeholders’ ability to influence while the latter predicts how stakeholders will influence the nonprofit. In circumstances where the nonprofit is not salient to stakeholders, stakeholders’ influence may not be in the nonprofit’s interest.

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APPENDIX

## APPENDIX

## INSTRUMENT TO EVALUATE MISSION SPECIFICITY

The “mission specificity” variable was constructed from the assessments of four independent raters (three business administration doctoral students and a manager of a nonprofit hospital). Raters evaluated charities’ mission and impact statements according to the degree to which they specifically defined or identified beneficiaries. This appendix provides the instructions offered to raters, the methodology for calculating the mission specificity variable from the ratings, and statistical tests of reliability for the resulting variable.

## Instructions Provided to Raters

**Instructions**

The attached excel spreadsheet contains mission and impact statements for 134 charities\*. After reading each charity’s statements, assign a rating (whole numbers from 1 through 7 according to the shown Likert scale) for the following items.

The degree to which the charity’s mission and impact statements define beneficiaries by:

Need: The needs of the beneficiary or their qualifying condition  
Demographic trait: Age, gender, race, religion, culture, ethnicity, sexual orientation, etc.  
Membership: Geographic membership, residence, or location

**Likert Rating Scale**

*Not defined* ←————→ *Clearly and narrowly defined*

1      2      3      4      5      6      7

\* A few charities do not construct impact statements. Also, data was gathered directly from charities' IRS Form 990 filings. Grammatical and typographical errors within the data were not corrected.

## Calculating Mission Specificity

As requested, all four raters assessed the degree to which charities define their beneficiaries through mission and impact statements. Each returned spreadsheet contained 134 records with nonprofits’ identification fields and three additional fields labeled as need, condition, and membership. The values for need, condition, and membership (no missing values) were added to create the measure of mission specificity. The resulting sum was then analyzed for inter-rater reliability.

## Inter-Rater Reliability – Cronbach's Alpha Statistics

## Case Processing Summary

		N	%
Cases	Valid	134	100.0
	Excluded	0	.0
	Total	134	100.0

## Reliability Statistics

Cronbach's Alpha	N of Items
.885	4

## Item-Total Statistics

	Scale Mean if Item Deleted	Scale Variance if Item Deleted	Corrected Item- Total Correlation	Cronbach's Alpha if Item Deleted
Rater1	8.1863	9.286	.807	.832
Rater2	9.0448	12.404	.792	.860
Rater3	8.6836	11.437	.766	.852
Rater4	8.1363	8.763	.762	.864

## Scale Statistics

Mean	Variance	Std. Deviation	N of Items
11.3503	17.932	4.23460	4

## Pearson Correlation Statistics

	Rater1	Rater2	Rater3
Rater2	.746*		
Rater3	.699*	.718*	
Rater4	.717*	.668*	.667*

\* Correlation is significant at the 0.01 level (2-tailed)