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Rethinking nonprofits: marketization and management practices for financial sustainability

Patricia Valentin Castillo¹ & Jose I. Vega Torres²

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Abstract:

This paper examines managerial practices adopted by a sample of nonprofit corporations supported by United Way in Puerto Rico, including organizations that operate a social enterprise or are considering doing so. Aspects related to marketization such as motivations for, challenges of, and results from establishing a social venture as well as human resources strategies adopted are described and compared to those reported on the *Social Enterprise: A Portrait of the Field* study published in 2010.

Findings reflect many similarities between local parent organizations and their social enterprises and their counterparts in the US and Canada. Also, while marketization practices are seen by some as a threat that may lead to mission breach, from the perspective of local practitioners it is quite the opposite. A majority of practitioners view the adoption of market practices as an opportunity to garner the resources to assure the continuity of operations and achievement of the social mission. On the other hand, human resources related issues such as volunteer and board of directors' engagement seem to pose challenges or concerns for nonprofit administrators in their process of rethinking themselves for achieving financial sustainability.

Keywords: social enterprises, nonprofit corporations, marketization, earned income strategies, human resources.

¹ Patricia Valentin Castillo teaches human resources and entrepreneurship at the School of Business Administration in the University of Puerto Rico at Mayaguez and is faculty of various professional certifications aimed at practitioners of the nonprofit sector. She may be contacted at patricia.valentin1@upr.edu.

² Jose Vega Torres teaches marketing and entrepreneurship at the School of Business Administration in the University of Puerto Rico at Mayaguez and is faculty of various professional certifications aimed at practitioners of the nonprofit sector. He may be contacted at jose.vega18@upr.edu.

INTRODUCTION

Third sector organizations are internationally recognized actors for encouraging social innovation. (GEM, 2015). Nonprofit corporations in the US and Canada are third sector organizations whose management practices are evolving, including the launching of social enterprises as a mechanism for achieving organizational financial sustainability (Community Wealth Ventures, 2010). As nonprofits become more business-like in their practices and for profit entities increasingly embrace important social causes the scholar community copes with advancing a universal typology for social enterprises models (Defourny, J. and Nyssens, M., 2016).

This study focuses on examining the managerial practices adopted by a sample of nonprofit corporations supported by United Way in Puerto Rico which included organizations that operate a social enterprise or are considering doing so. Results are compared with those from nonprofits corporations in the United States and Canada as described in the *Social Enterprise: a Portrait of the Field* study published in 2010 by Community Wealth Ventures and the Center for the Advancement of Social Entrepreneurship (CASE) at Duke University's Fuqua School of Business. This report adopted the popular conceptual definition of "social enterprise" developed by the Social Enterprise Alliance (SEA) that states:

"An organization or venture (within an organization) that advances a social mission through market-based strategies. These strategies include receiving earned income in direct exchange for a product, service or privilege". (Community Wealth Ventures, 2010)

The widespread trend of incorporating market based strategies to generate earned income or launching social enterprises has been described as the marketization of the Third Sector. For decades, respected scholars and practitioners have argued that the trend towards marketization of nonprofit corporations may undermine their pursuit of core values and their capacity to garner public support. Detractors and proponents of the practice point to the need to undertake and disseminate research that documents empirically the effect on third sectors organizations of incorporating earned income strategies as mode of financing the accomplishment of its mission (Salamon, 2002) (Diaz, C., 2016).

Nonprofit corporations in Puerto Rico have been increasingly adopting earned income strategies, integrating the market more directly, through the formation of social purpose commercial activities or social enterprises (Estudios Tecnicos, 2015), (Vega, 2014). Some of these organizations have been transforming themselves by use of market means to obtain nonprofit objectives as well as affirmative human resource strategies to support the attainment of their mission. (Valentin, P., Feliciano, J. (2017) Of particular interest to the authors are aspects related to marketization such as motivations for, challenges of, and results from establishing a social business venture and their corresponding human resources strategies.

OBJECTIVES

This investigation aims to develop a profile of nonprofit corporations that have established social enterprises in Puerto Rico for comparison with their counterparts in the US and Canada with a focus on marketization and human resources strategies. The three main research questions are:

1. How do managerial practices of nonprofit corporations who have launched social enterprises compare to those in the US and Canada?

2. Which are the major threats and opportunities of marketization as identified by practitioners?
3. Which management strategies are being adopted in support of marketization and mission fulfillment?

METHODOLOGY

This investigation builds upon previous work of the authors on the theory and practice of social enterprises and draws upon a broader set of survey data from the doctoral dissertation of professor Patricia Valentin completed in May of 2015. The survey followed the methodological approach used in the report released on 2010 titled *Social Enterprise: a portrait of the field*. This report is based on the National Social Enterprises Field Study funded in 2008 by the Robert Enterprise Development Fund and conducted by a partnership between, Social Enterprise Alliance, Community Wealth Ventures, Inc. and Duke's University Center for Advancement of Social Entrepreneurship.

The survey instrument developed for the previously depicted study was used with permission and administered to the universe of 135 nonprofit corporations receiving assistance from United Way of Puerto Rico (UWPR). Authors experience and consultations among colleagues and practitioners led to the conclusion that this was a feasible and pertinent sampling frame that enabled the comparison with data from the national study which was a major objective of professor Valentin doctoral dissertation. The survey instrument was translated by a certified translator and subject to a reversed translation test as well as reviewed by a group of experts in the subject matter for assuring consistency and maintaining validity.

A database of the organizations supported by UWPR was developed and the instrument was sent to be self-administered online by means of the google docs application. To stimulate response a

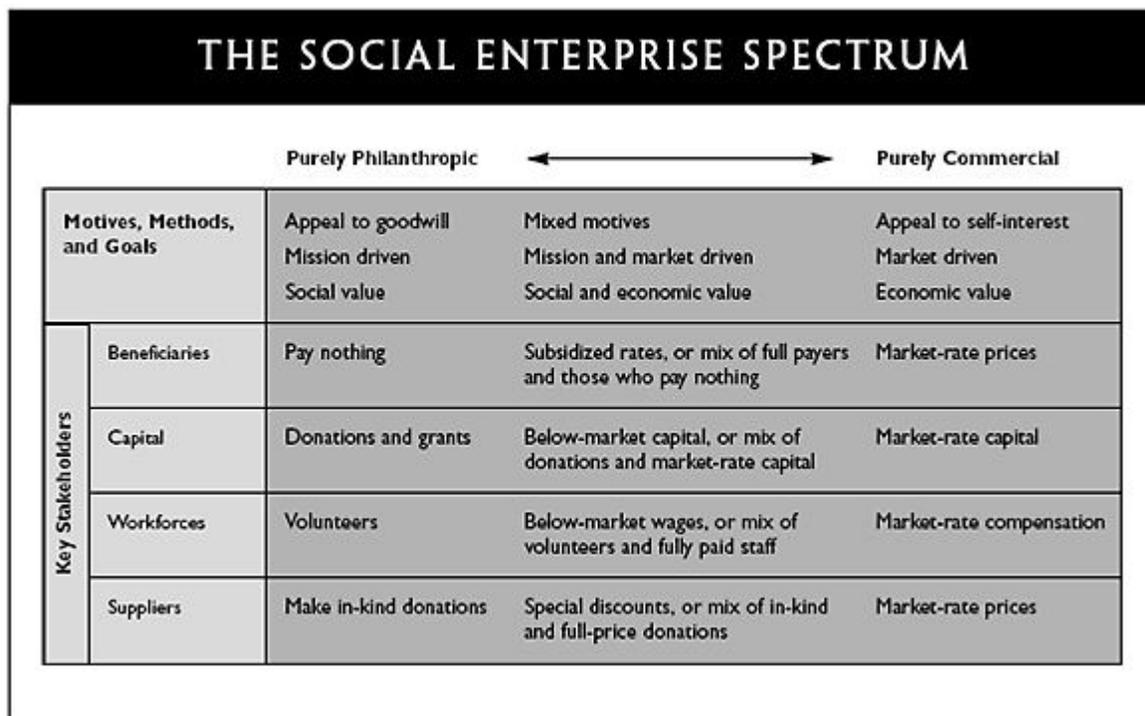
letter of support to the research objectives was sent by UWPR to the organizations in the data base. After several reminders, 79 usable questionnaires were received for a sample that represented 59% of the universe. Of these, 26 corresponded to organizations reporting they operate a venture that qualifies as a social enterprise according to the definition adopted for the study and 53 that reported they did not. The research conceptual model called for asking a set of questions to the first group to assess their motivations, challenges and results of applying market and human resources strategies in fulfilling their social mission. Also, the second group was probed on the reasons for not engaging in commercial activities associated with a social enterprise at the present time, including why they ceased to operate a venture should that be the case.

THEORETICAL PERSPECTIVE ON THE MARKETIZATION OF THE THIRD SECTOR

Trends observe by scholars include that of nonprofits becoming more “business like” in their strategies and income generating activities, while for-profits show an increasing tendency to embrace and advance important social and environmental causes. Literature reveals that marketization may imply changes in how nonprofits are funded, particularly by increasingly relying on earned income and competition for contracts, and in their organizational structure, culture and practice by having to act more like traditional commercial organizations (Hall, Alcock & Millar, 2012). Some scholars even place the practice of social enterprise as a result of the marketization trend among civil society organizations (Eikenberry & Drapal, 2004).

Salamon, for instance, argues that the generalized reduction in grant funding have motivated nonprofit organizations to adopt business policies and market strategies similar to those of for profit businesses (Young & Salamon, 2002). Dees establishes that spiraling operational costs,

competition for shrinking sources of grant funding as well as from for profit businesses entering the realm of social services are the forces behind the nonprofit organizations adopting commercial practices to generate additional resources that could lead to financial self-sustainability (Dees, 1998) (Dees, G., & Battle, B. 2006). As a result, it was argued by Dees as early as 1998 that social enterprises within the nonprofit sector operate in practice within a spectrum that may range from purely philanthropic to purely commercial as depicted in the following diagram.



Source: Dees, 1998.

We may come to think as marketization in the context of nonprofits as the evolution the organization experiences from being in the right end of the spectrum and progressing to the left depending on the magnitude and level of the commercial practices adopted. In a similar manner, as more private sector for profit businesses by applying the practices associated with the concept

of Corporate Social Responsibility (CSR) incorporate operational practices and objectives previously associated only with social mission driven entities and move toward the left it may be a process of reverse marketization. In related previous works authors have been developing an instrument that may help to ascertain how aspiring social enterprises in the context of nonprofits corporations might be located with respect to the spectrum of what in practice scholars are referring to hybridization (Vega & Valentin, 2015).

Scholars and practitioners worldwide have identified the threats and opportunities that marketization poses to the nonprofit entities. In general, the most frequently alluded threats or concerns are related to drift from or breach of the social mission. Mc Kay concludes that by increasing their share of commercial revenue through the adoption of market discipline strategies organizations are to some extent adopting the practices, structures and languages of the private sector and ‘succumbing to market forces’ (Mc Kay, 20011 cited by Hall, Alcock & Millar, 2012). Other scholars argue that by adopting approaches and values of the private sector democracy and citizenship might be at harm because of the negative impact on nonprofits ability to create and maintain a strong civil society (Eikenberry & Drupal, 2004). On the other hand, private sector representatives frequently argue that incursion of nonprofits in their market turf is a mode of unfair competition since these entities are usually exempted of paying taxes that apply to them (Diaz, 2016).

On the contrary, scholars and practitioners alike, also point out the opportunities brought by the evolution of reducing the dependency on philanthropy for financing the social mission of third sector organizations. Muhammad Yunus, novel prize awardee and precursor of microlending, for example is an avid defender of a more entrepreneurial approach towards advancing the social agenda for public good in his various publications on the topic of social enterprise (Yunus,

2011). Santiago and Vega found that income diversification has a crowding in effect in the diversification of revenues sources of nonprofit corporations (Santiago & Vega, 2016).

In Puerto Rico, public policy has been evolving to cope with the transformation of the nonprofit sector as it strives to achieve sustainability by adopting strategies and social business models consistent with opportunities brought by marketization. One of such actions was the update to the General Law of Corporations in 2015 to introduce the legal framework for the denominated Public Benefit Corporation and the Low Profit Limited Liability Company (Law 233 of December 22 of 2015). Since its enactment hundreds of social innovators have registered their new or evolving organizations under the new legal structures.

The following table summarizes the major threats and opportunities encouraged by marketization as described in the international literature.

Threats/ sources of concerns	Opportunities
Mission drift or breach	Financial self-sustainability
Adoption of an overly commercial culture by employees	Possibility of subsidizing non-revenue mission related activities
Loss of volunteers support	Foundation for program autonomy
Loss of democracy/ legitimacy	Model for empowerment

REFLECTIONS OF THE PRACTICE: FINDINGS OF THE SURVEY TO ADMINISTRATORS OF NONPROFIT CORPORATIONS IN PUERTO RICO

Are social enterprises a common practice?

A substantial number of respondents, roughly one third (33%) are operating a social enterprise at the present time as depicted in the following table. This percentage, nevertheless, is less than the one observed in the US national survey which was 54% (Community Wealth Ventures, 2010). It

does reflect a growing interest when considering data from the survey conducted every five years locally by the firm Estudios Tecnicos. (Estudios Tecnicos, 2015).

Social Enterprise	Percentage	Organizations
Currently operates a social enterprise	33%	26
Does not operates a social enterprise	63%	50
Operated one in the past	4%	3

Main reasons for not operating a social enterprise include: do not know how to or which are the best practices, difficulty to obtain financing to start operations and lack of time to dedicate to the effort. It is worth mentioning that more than half of these entities (26) indicated that they are interested in establishing a social enterprise. The reasons for discontinuing a social venture were unfavorable market conditions, employee turnover, and inability to meet financial expectations.

In general terms, more than half of respondents (54%) reported that directive boards of the organizations were positive towards the social enterprise venture although a significant group (22%) also expressed that their boards were not familiar with the concept. In the case of staff, 52% reported that the organization's employees supported the concept while 28% were not familiar.

Motivations for and benefits of establishing a social enterprise

Respondents indicated as their major motivations for establishing a social enterprise the possibility of producing revenues to fulfill their social mission. In that respect, when inquired on the benefits for the organization of launching the social enterprise the social enterprise positively impacted or impacted substantially on how the social enterprise impacted the organization the responses were:

- positively impacted the achievement of the mission 61%
- positively impacted the generation of revenues 58%
- positively impacted the enterprising skills and mentality 46%
- positively impacted capacity to attract and retain donors 35%
- positively impacted capacity to attract and retain employees 35 %
- positively impacted capacity to attract and retain board members 27 %

Challenges or concerns when establishing the venture

At the beginning the major challenges and concerns were:

Financing the Start up	58%
Securing Partners or Collaborators	27%
Identifying a feasible business	23%
Potential conflict with mission	23%
Lack of knowledge of concept or best practices	19%
Lack of time or expertise to develop the business plan	19%

The major concern in the US national survey also was financing the startup (66%). Conflict with mission is neither on the top of the list for the US national survey with a 20%.

Some representative comments of respondents regarding major challenges or concerns were:

“It is difficult to access start up capital and technical assistance for assessing the feasibility and best fit of ventures with the organization”

“Educating clients which are used to received free services since we recieve governmental funds is a challenge”

“Educating governmental agencies that charging for certain services do not means we are for profit entities is an effort to be made”

“Recruitment of trustworthy and qualified staff committed to the venture that could function with minimum supervision is difficult”

Challenges concerning management practices:

Marketing	Developing marketing plans (35%) Financing marketing activities (23%), Customer service (20%), customer database management (35%), new product/service development (15%)
Human resources	Reasonable compensation of employees (62%), training in best practices (12 %), recruitment and retention of competent employees (15 %), securing commitment from board of directors (12%)
Finances	Obtaining growth capital (58%), education of financial institutions for understanding of social enterprises (19%) early stage financing (15%)

Aligning operational objectives with mission is a major priority of business policies as indicated by a 39% of respondents.

Salient characteristics of social enterprises

Legal Structure	A division or department within the organization (42%) or a nonprofit subsidiary (23%)
Type of business	Educational services (23%), thrift store (9%), Counseling (7%), Child Care (7%), and Elderly Care (7%)
Level of Employees	Less than five employees (46 %)
Volunteers	Up to 35 volunteers collaborate in the social venture (69%)

Defining the appropriate legal structure was mentioned as a challenge by 58% of respondents.

A COMPARISON WITH THE US AND CANADA

A comparison of selected elements of nonprofit corporations with social enterprises in the US and Canada with those on the Island is summarized in the following table.

Aspect	US & Canada	Puerto Rico
Motivation for launching social enterprise	48 % driven by prospects of revenues and mission impact	58 % driven by prospects of revenues and mission impact
Number of social enterprises in operation	45% have more than one and 87% anticipated launching others	A majority operates one and 80% anticipates launching others
Types of social ventures	Top five: education and training, retail/thrift shop, consulting services, food services/ catering, and arts.	Educational services , thrift store, Counseling, Child Care, and Elderly or child Care
Legal structures	A majority, 64 %, operate their social enterprises as a division or as a subsidiary of the larger organization. Smaller percentages have created for-profit subsidiaries (32%)	A division or department within the organization (42%) or a nonprofit subsidiary (23%)
Revenues earned	More than one-third (34 %) had earned-income revenues of over \$1 million, while one out of four (25 %) were earning less than \$100,000 per year.	Less than \$25,000 (23%)
Startup capital	Foundation funding	Corporation or private funding
Major challenges	Finding funding to start the new venture (more than two thirds), sales and marketing	Financing the Start up 58%, Securing Partners or Collaborators 27%,

	(27%), financial issues (23%) and human resources (14%)	identifying a feasible business 23%, Potential conflict with mission 23%, Lack of knowledge of concept or best practices 19% or expertise to develop the business plan 19%
Technical assistance needs	Business plan development ; introductory training on social enterprise ; market research and analysis; and accessing capital.	Business planning and financing, Finances , human resources including the board of directors and sales & marketing

CONCLUSIONS

Rethinking nonprofits with a focus on how to make achieving the common good financially sustainable seems a major topic of concern and interest of scholars, policy makers, public policy and practitioners at the global and local level.

Many similarities exist between the local nonprofits corporations and those in the US and Canada beginning with an increasing interest in launching social enterprises as a division of the parent entity and the corresponding adoption of management practices consistent with the marketization of at least part of their operations. Major motivations in both jurisdiction are the prospects of revenues and mission impact. The types of social enterprises launched are very similar as well as the technical assistance needs of the parent organizations. In PR, nevertheless, the trend is more recent and less widespread among nonprofits and the social enterprises established are much smaller. Other minor differences include the prevalence of corporate funding as a source of startup capital, the focus of the parent so far on one enterprise and that of child and elderly care as potential types of services to produce earned income.

Also, while marketization practices are viewed by some academics as a threat that may lead to mission breach, from the perspective of local practitioners it seems quite the opposite.

Practitioners view the adoption of market practices as an opportunity to garner the resources to assure the continuity of operations and achievement of the social mission. On the other hand, human resources related issues such as staff recruitment and retention, volunteer engagement in the social enterprise and board of director's familiarity with the concept seem to pose important challenges for nonprofit administrators in their process of rethinking themselves for achieving financial sustainability.

LIMITATIONS

The absence of a sampling frame with a list of the universe of nonprofits corporations in PR may have influenced the results obtained. Also, the empirical survey data gathering was limited to the items in the questionnaire used in the National Field Study. As a result, responses in the data set are limited to the aspects examined by the study.

IMPLICATIONS & FUTURE RESEARCH

Public policy should continue to be updated to reflect the evolving nature of nonprofits and social enterprises. Academia must update curriculum to address the need for qualified human resources to lead and operate the diverse typologies of social enterprises emerging as organizations rethink themselves.

Future research could entail a more in depth examination on the survey findings beyond descriptive statistics. Also, the authors will like to continue to engage in case analysis of social enterprises identified to further study their business models. This aspiration is also consistent with the methodology in the original study by CASE and Community Wealth Ventures.

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