

Challenges of Building Nonprofit Capacity for Cross-Sector Collaborations, Including Minority-Led Nonprofits

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Abstract

Local governments in the United States depend on intergovernmental transfers of money to help finance social services. The national debt of the United States is now approaching \$28 trillion and annual interest payments on the debt are approaching \$400 billion a year, in part because of economic needs driven by the Covid-19 pandemic. The pandemic has, in turn, increased the need for effective social services. This paper offers suggestions for enhancing the capacity of nonprofit organizations (including minority-led nonprofits) to help local governments become more effective in delivering social services through effective cross-sector collaborations.

Keywords: nonprofit organizations, city government, cross-sector collaboration, Black-led enterprises, church-related nonprofits

1. Challenges of Building Nonprofit Capacity for Cross-Sector Collaborations

Local governments in the United States are under severe financial strain to provide needed social services, especially in the wake of the Covid-19 pandemic and related events. The consequences of the pandemic will affect state and local governments in the United States for years to come. Current events have increased service needs and intergovernmental revenues will likely be constrained once the funding associated with the CARES Act and American Rescue Plan are long gone. Many employers will not reopen and a housing crisis could ensue, causing continuing loss of local tax revenues. The recent dramatic increases in the national debt will likely constrain the amount of money that state and local governments would have received from the national government. The states will also have fewer resources to share with local governments. A rise in interest rates could dramatically decrease discretionary spending at the national level of government, triggering rounds of "fend for yourself federalism." Possible civil unrest fueled by social protests and armed militias could push the capacity of many state and local governments beyond their fiscal limits. Like flood victims trapped in their attics, local governments may find themselves trapped between rising fiscal needs and ceilings imposed on them by restrictions on their ability to increase tax revenues.

There is a long history of relationships between local governments and nonprofit organizations. "Different strands of economic theory support alternative notions of the nonprofit sector as supplementary, complementary, or adversarial to government." (Boris, 2017, p. 39). The most common form of "partnership" between a local government and a nonprofit organization is a one-to-one relationship in which the nonprofit provides local social services under contract with the local government (Feiock & Jang, 2009). This kind of working relationship allows the local government to provide social services to residents without increasing the government payroll, which includes salary, benefits and pension obligations (Denhardt & Denhardt, 2015). A common theme in this pattern is that the nonprofit is a junior player and may be dependent upon the government contract to survive financially. This is especially true if the nonprofit is a small local organization without substantial name-recognition and supportive donors within or beyond the local political jurisdiction. While this kind of relationship may serve the interests of the local government, it may limit the nonprofit's capacity to obtain the resources needed to substantially supplement local government funding in the present political and economic environment. Ultimately, local governments will need not only more oars in the water, but additional partners to share the burdens of public governance. To the degree that nonprofit organizations can provide social services for reasonable costs, the more likely local governments will be able to fulfill their responsibilities in the face of declining intergovernmental revenues. This dilemma is rapidly becoming an existential crisis for local governments and the nonprofits in their orbit.

2. Overview of Nonprofit Sector Service Delivery Models

Registered 501c3 organizations in the United States are a form of corporation approved by the Internal Revenue Service as a tax-exempt, charitable organization. Unlike for-profit organizations, they have no owners.

Unlike governments, they have no powers of taxation. If they produce any profits, those funds must be channeled into their charitable missions. If they dissolve, they must distribute their assets to other charitable organizations. Nonprofit social service organizations commonly receive donations from individuals, grants from Foundations (which are also nonprofit organizations), and they may enter into contracts with local government jurisdictions to provide social services.

Generally speaking, these government contracts do not confer the power of government on nonprofit contractors, nor do they constrain them with the many Constitutional and legal restrictions government must operate under. As Kettl (2020) explains, government can only do what the Constitution and related laws allow, while business and nonprofits can do anything not expressly forbidden by those documents. Thus, nonprofits working at arms-length under government contracts have some leeway in delivering social services, so long as they are reasonably transparent, effective and accountable. Nonprofits operating in this local market niche may not face much competition from other nonprofits or private sector firms because, as one nonprofit manager put it, “the work is difficult, and no one wants our jobs.”

While their revenues primarily come from donations, grants and contracts, their delivery of services is substantially derived from the work of volunteers. There are, of course, some paid employees in many nonprofit organizations, but they are often underpaid and overworked. Likewise, most board members and many direct service providers are unpaid volunteers. For governing boards and managers, this heightens concerns about maintaining the quality, consistency, and continuity of services, especially with increased pressure to collaborate with others and to meet stringent accountability standards. The board’s ability to exercise its strategic planning and oversight functions is critical given scarce and competitive funding, and the greater fragmentation and differentiation of services that characterizes the contemporary landscape (Smith & Phillips 2016). This has implications for the capacity of small and midsize nonprofit organizations, as discussed below.

3. Literature Review

Shortly after the 2007-2008 economic recession, Boris et al. (2010) conducted a national survey of government contracting and grants with nonprofits. The authors found that many nonprofits were experiencing serious problems in their relationships with government. An estimated 33,000 human services nonprofits held government contracts at that time. Seventy-five percent of those surveyed said that applying for contracts and grants was too complex and time consuming, while seventy-six percent said that the complexity and time required for reporting on contracts and grants was excessive. Sixty-eight percent felt they were not being paid the full cost of contracted services, while fifty-three percent said late payments by government were a problem. Fifty-eight percent also reported that government changes to contracts and grants were troublesome. This nationwide survey revealed that both governments and nonprofits are struggling to manage their contractual relationships and deliver essential social services, particularly during economic downturns when counter cyclic forces increase the demand for social services (Moffitt 2013).

Another study of 22 health and human services organizations performing cross-sector work in Oregon documented some relevant insights (Petchel, Gelmon & Goldberg 2020). The authors found that leaders from both sectors perceived collaboration risks related to reputation, sustainability, and compliance with regulatory or funder requirements. Risk perceptions differed across the public and nonprofit sectors, and the leaders noted having difficulty in judging the reliability of potential partners, some of whom were perceived as competitive or coercive.

Kim and Peng (2018) reported that while many small nonprofit organizations do engage in collaboration with cities and other entities, such collaborations require human capital. Small nonprofit organizations are constrained because they have few employees and tend to depend heavily on volunteers. While volunteers may have substantial knowledge and skills, and share strong commitment to the nonprofit’s mission, they may not be able to devote themselves fully to the work of the organization. Board members may become so involved in fund-raising activities that their potential contributions to other boundary-spanning activities become compromised. This situation could jeopardize their ability to maintain effective collaborative relationships with local governments and other service organizations. Financial constraints limit access to intellectual, social, and human capital. These limitations further constrain the kinds of collaborations needed to substantially enhance the capacity of local governments via contracts and other forms of collaboration. Having too few paid professional employees prevents small nonprofit organizations from being able to acquire and maintain the kinds of collaborative contracts needed to partner with local governments, especially given the need to maintain extensive documentation for accountability purposes. Small nonprofit organizations must deploy their full-time professional workforces to meet government standards and become effective partners with local governments. The costs of doing so are often very high, which helps to explain their usual dependence on part-time employees and volunteers.

Governments are required to maintain documentation showing that they are accountable for the expenditure of taxes and other revenues.

Nonprofit organizations also need to be accountable, but often in different and less strenuous ways. Many nonprofits need to formalize and strengthen their systems of accountability to build greater capacity and win additional contracts with local governments. Faith-based nonprofit organizations, in particular, may need to demonstrate and document that their religious value systems do not limit or compromise their ability to respond to political directives that may not align with their own organizational values. Poister, Aristigueta and Hall (2015, p. 428) identify factors that tend to constrain the capacity of nonprofit organizations to create and apply the kinds of accountability systems required by local government agencies. One priority need is to implement an effective performance management and measurement system. Nonprofit managers may think this is unnecessary, and some volunteers may be leery of attempts to evaluate their performance. Like government itself, nonprofit organizations often pursue missions that are vague and aspirational, which makes performance measurement difficult.

Local chapters of nonprofit organizations may have high degrees of autonomy, which makes coordination and control more difficult. Nonprofits are often dependent on a changing mixture of grants, which can create a more fluid flow of services. Funders may provide nonprofits with unique sets of performance indicators, requiring them to implement systems that capture and report data required by different performance measurement systems. Many local nonprofits do not have the managerial and analytical resources to support complex performance management and measurement systems.

Poister, Aristigueta & Hall (2015) recommend implementing performance evaluation systems incrementally so as not to overwhelm those responsible for collecting data, creating documentation, and making it align with the needs of various stakeholders, which includes donors, congregants, foundations, and government entities. While performance management systems are often mandated by elected chief executives, legislatures or governing boards, many public and nonprofit managers have become advocates for using them (page 440).

Thirdly, the capacity of nonprofits to supplement the activities of local government depends upon their ability to supplement government contracts with money from other sources, including donations and grants. Few people voluntarily give money or personal services to government agencies. The compulsory nature of taxation and political rhetoric describing bureaucratic systems as overgrown and wasteful tends to discourage such contributions. When programs administered by nonprofits can attract funding from charitable donations, foundations and gifts, government departments who contract with the nonprofit can benefit from such resources indirectly. It is in part this mixture of revenues that makes the accountability mentioned above so important. Bray (2018) describes a variety of common fundraising activities of nonprofit organizations, including communications, solicitations, and special events. Dan Pallotta (2013) has challenged the way we think about fund-raising for charity. One of the most widely used metrics regarding fundraising by nonprofits is the percent of donations that goes directly to the mission. The idea is that a nonprofit that uses a large percentage of its donations for additional fundraising is not effective. Pallotta argues that it is the amount of money available to be spent on the mission that matters – not the percentage of donations used for the mission.

Another important feature of accountability that can discourage local government contracts with nonprofit organizations is their conflicting accountability structures. Local government authority largely resides in elected officials and their appointees. One common feature of democratic government is multiple principals – that is, various elected and appointed officials – who vie for control and seek a mandate to govern. Most nonprofit organizations have fewer principals that are politically weaker. These nonprofits can be weakly constituted or have governing boards and directors who exert control with varying degrees of effectiveness. Some nonprofits are run by charismatic leaders who are quite powerful internally and have a strong hand in the organization's management. The result is that a kaleidoscope of conflicting accountability structures is created when government contracts social services to nonprofits. Efforts to integrate these different command and control systems can be difficult and may result in a loss of accountability.

4. Concerns of Local Government Administrators

Three city administrators in small municipalities in the Midwest responded to questions about their experiences contracting with nonprofit social services organizations. We asked the following questions.

- In your experiences in city administration, have you generally found nonprofit social services organizations to be constructive partners with city government; not constructive partners; or a mixed bag?
- Generally speaking, do you see social services nonprofit organizations as having any substantial fiscal capacity (via their other sources of revenues) to supplement or replace intergovernmental transfers that may decrease in the future?

- In your experiences or opinion, do small to midsize social services nonprofits usually have the performance monitoring systems in place to provide the kinds of accountability required to be reliable partners with city departments in providing vital social services?
- Would it be better for the city to partner with a nonprofit social services provider; a for-profit provider; or no-difference?

A town administrator in Ohio (with prior experience in Midwestern cities) reported having never had any such experiences. A retired city administrator in Nebraska reported that his experiences have been very positive. He reported that the NGOs he worked with had solid private financial resources. His NGOs had performance monitoring systems and his cities required audits of them. He and his city officials worked with two for-profit local economic development groups that were well-funded and very successful with subdivision development and multi-million-dollar commercial developments.

A third administrator of a small city in Nebraska reported that his city, "gets along with the nonprofits." He reported, for example, that the city looks to them to step in and help with utility bills when customers cannot pay. "The Police Department also works with them on life safety issues and cases of domestic abuse." He reported that the kinds of nonprofits he is familiar with do not have enough revenue to help make up for intergovernmental transfers that may decrease in the future. He offered that he does not think it matters whether the city contracts with a nonprofit service provider or a for-profit service provider. "Both will likely be getting grant funds from the government and are required to follow the same set of guidelines. He did not use the word "partner" to describe relationships with local nonprofits.

A deputy county administrator of a large suburban county in the Midwest has found nonprofit social services organizations to be critical and essential for providing services to the community, especially in the areas of criminal justice and general welfare services. Many such nonprofits rely on state and federal grant funding, which may not always be there. Some have been successful in obtaining funding from foundations, private donors, and businesses, which helps them become and remain more fiscally sound. Some of the smaller local nonprofits have recruited board members who can help develop good accounting and strong accountability systems. Because the nonprofits they work with also receive state and federal funds, the county knows that these nonprofits are accountable for use of grant revenues. Nonprofit firms tend to be comprised of employees and volunteers with a strong "public service ethic," which makes them very committed and devoted to their work.

5. Discussion: Strategies to Increase the Capacity of Nonprofit Organizations, Including Minority-led Enterprises

Nonprofit organizations can be complex to govern and run. While they may not rise to the levels of accountability expected of government organizations, they are held to standards of accountability by the IRS through Form 990, Return of Organization Exempt from Income Tax, and through other means such as board governance and stakeholder oversight. Their reports are made available through online websites like Guidestar and Charity Navigator (see respective websites). While they are not required to have a website, many nonprofits do. Foundations (and many potential donors) study the information on websites very carefully. While a local nonprofit that helps people pay their utility bills may want to stay "under the radar" of intense scrutiny; all nonprofits that hope to grow and thrive must increase their professional capacities in multiple key areas. Without key competencies (not just monetary capacity), nonprofit organizations are unlikely to become effective partners with local governments in times of fiscal distress. The expertise needed to develop such competencies may not be available from the organization's existing pool of managers and staff volunteers. The pool of prospective board members and service-delivery volunteers is likely limited as well.

So, a "chicken or egg" situation may develop. To grow into a professional organization, a nonprofit may not be able to employ the variety of professional employees necessary to meet the accountability standards of government authorities or major foundations. A heart-wrenching mission and pictures of distraught children or animals on a website may create a flow of small donations from donors. But a professional nonprofit able to partner with local governments in the midst of growing social needs and declining intergovernmental revenues needs a more professional business model. The fact that both the city and the nonprofit may face declining revenues from the national government is likely to increase the need for professionalism and accountability.

At least three major types of professional capacity are needed. One is professional fundraising, beyond the level of newsletters, annual reports and special events. Two is professional management skills regarding the recruitment, training, and supervision of both paid and volunteer workers. And three involves acquiring the skills needed to manage financial records and performance reports needed by government auditors and other oversight bodies.

Foundations and federal grant administrators have made fund raising far more difficult than in the past when the source of revenues was likely to be individual donors making relatively small donations; or the local public radio station offering a t-shirt for a donor's continuing annual support.

Modern foundations now have standardized application packages and many detailed forms requiring submission of formal documents and statements. It is difficult for the founder of a nonprofit organization and his or her several friends or family members to make the transformation to the threshold level for nonprofit operations without having accountants, lawyers and other professionals on staff or on retainer.

The recruitment, training and supervision of volunteer workers differs from the skills of traditional personnel administration. It is not possible to "lean on" volunteers in the same way that employees are often motivated and managed. And yet, nonprofit organizations with government contracts (and/or major grants from foundations) must extract the dedication and professionalism from volunteers that would be sought from regular paid employees.

Finally, serving a government entity becomes part of the work of the government entity itself. The documentation and performance of the work done by the nonprofit must rise to the standards required by the government entity itself. Evidence of having charitable values is not enough to excuse glaring mistakes. The nonprofit organization must document their performance and effectiveness, requiring hard numbers on administrative activities and services delivered. Specialists in government who are experts in contract administration must have counterparts in nonprofit organizations with similar skills. Documentation must reflect the requirements of the contract rather than the mission statement and aspirations of the nonprofit organization. This may create challenges for nonprofit organizations (such as those with strong religious affiliations) who describe their activities in different ways for donors and for government entities who contract with the nonprofit organization to perform services.

Black and other minority-led nonprofit organizations face the same challenges related to capacity building as other nonprofits (Kapucu, Augustin & Krause, 2007). It is common for local ministers to become founders of local nonprofit organizations that are separate from their churches and congregations. Black-led nonprofits associated with church congregations are common in many local communities. We are not suggesting that all Black-led nonprofits are religious organizations; or that all church-related nonprofits are minority sponsored. We also do not mean to suggest that minority-owned nonprofits are more challenged than other nonprofits of similar size and type. Kapucu and colleagues (2007) studied nine small minority nonprofits working with HIV/AIDS issues in Central Florida and identified one important capacity challenge as recruiting and maintaining volunteer services. They observed: "Minority volunteers proffered lack of personal time due to health and economic hardship as a detractor to volunteer availability" (Kapucu, Augustin & Krause, 2007, p 14). While many potential volunteers were likely concerned about their health and safety, it is possible that concerns are greater for other minority-led nonprofits. Also, we have observed that the boards of many church-related nonprofits tend to be comprised of ministers and other religious leaders rather than people with the professional backgrounds that are needed to run a modern nonprofit organization.

6. Suggestions for Enhancing the Capacity of Nonprofit Organizations

Nonprofit organizations, like other types of organizations, tend to either die young or evolve through a lifecycle (Connolly, 2006). The typical stages of this life cycle are inception, growth, maturity, and either reinvention or organizational death. Transitions between stages of the life cycle are referred to as "passages." Almost anyone can identify a charitable need and complete the paperwork to create a new nonprofit organization, with the help of an attorney or a commercial service. The person who does so is identified as the founder of the organization. That person may assume the formal role of executive director or chair of the board of directors. In any case, the founder is likely to shape the mission and culture of the new organization.

There is an organizational pathology known as "founder's syndrome." An organization grows when the passion of the founder attracts others (volunteers, donors, etc.) and transforms the entity's processes and structures into those of a professional organization. Board members with relevant professional experiences are recruited when possible, and they may employ a qualified executive director. Professional staff are also retained. Ideally, the founder entrusts his or her "baby" to others, and it grows in strength and stature over time.

At some point, the organization enters a mature stage. This means it has a clear mission, sufficient resources including a stream of revenue, an accounting system, the ability to manage employees and volunteers, and a capacity to maintain records and produce the kinds of reports necessary to qualify for government contracts. In order to grow and become mature, the founder should not insist on doing everything, even if he or she is a very talented person. Rather, the founder should become more of a "spiritual leader" and less of a governor or administrator. Recall that Steve Jobs, a co-founder of Apple Corporation, was fired from the company because of his tendency to micro-manage.

7. Conclusions

While nonprofit organizations have the ability to tap revenue sources separate from the usual revenues of local governments, those nonprofit revenue sources are not adequate to make up for the likely losses of intergovernmental transfers from the national government.

The sum of monetary contributions to charitable organizations in the United States was \$410.02 billion (2.1% of GDP) in 2017 (Charity Navigator, n.d.). This is substantial and likely to increase in future years. But \$500 billion in philanthropy pales in contrast to the recent \$1.9 trillion Covid relief bill, some of which was earmarked for local governments and social services.

The capacity of nonprofit organizations (including minority-led ones) to supplement revenue flows into local government programs to provide needed social services cannot fully replace intergovernmental transfers of monies to local governments. The monies may be used to enhance the capacity of small to medium-sized nonprofits themselves. The idea that charitable organizations should be poor is unreasonable. They need adequate revenue to develop needed professional capacities to become effective partners with others, including local governments.

Even though philanthropy is large in the United States, it is not large enough to save local governments from likely future losses of intergovernmental revenues. These governments are struggling with other problems as well, including unfunded pension liabilities, shifting demographics, and natural disasters stemming from climate change. Mature nonprofit organizations can provide social services by contracting with local governments through competitive negotiated agreements. Competitive contracts can be cost effective for local governments when they have the skill and will to manage the contracts. But the additional revenues nonprofits may receive from donations and grants should be channeled into building and maintaining the nonprofit's capacity to administer government contracts and maintain the necessary documentation for accountability purposes. Increasing fiscal stress and gaps in performance and effectiveness when delivering government social services are likely to increase the demands for accountability – not decrease them. Small community-based nonprofit organizations are one potential solution to these problems, if they can develop adequate capacity.

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