Publicness of Goods and Issue Salience: Implications for competition in the provision of public services

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Working Draft: Please do not cite or quote without the author’s consent.

Abstract: This paper extends the theoretical framework of nonprofit activity in three sector economies to include considerations of both the nature of the goods produced by organizations and the salience of issues organizations address within the general population. In so doing, this leads to a more comprehensive theoretical frame than previously offered in the literature, integrating the various strands of theory on the existence of nonprofit organizations into one theoretical lens. Data on internet searches are used to illustrate the temporal variation and relative strength of issue salience in various mission areas in which nonprofits participate relative to goods and services provided by other sectors in the economy. Implications for nonprofit competition for resources, public policy advocacy, and public-private partnerships are discussed.
Introduction

From a general public policy perspective, the implications of competition among organizations in the economy are important for taxpayers, policymakers, and government actors. These concerns include creating and maintaining organizational and industrial structures that promote competition between actors in for-profit activity. In this way, competition in the for-profit sector is generally understood to be viewed favorably. Competition among actors in the public and nonprofit sector are viewed somewhat differently, however – and this perspective is complex. On one hand, public choice and competition to deliver public services is viewed positively, encouraging more efficient production of services. Under this perspective, competition between nonprofit, for-profit and government organizations can benefit taxpayers by maintaining the quality of services in a cost-effective way. A greater diversity of organizational actors competing to provide services can also lead to more diverse audiences being served by public goods than would be under uniform delivery from one government entity. On the other hand, however, introducing greater numbers of organizations that overlap in mission and geographic foci is also seen as potentially wasteful if this expanding group of organizations is competing for the same pool of limited funding.

From a charity perspective, competition for philanthropic funds and the fundraising costs and potential fundraising inefficiencies that accompany increases in the number of organizations vying for funding have been viewed negatively by many philanthropic funders as an unnecessary “duplication of services.” From a government perspective, public charities receive tax exemptions and their donors benefit from tax deductions, and these tax benefits translate to tax subsidies for nonprofit activity. Therefore, the public and government have an interest in the efficient operations of the nonprofit sector. If competition between nonprofits leads to the
dilution of finite amounts of charitable funding and inefficient fundraising, there would be social costs to having duplicative service providers in nonprofit markets. In such cases, federated fundraising campaigns in which nonprofits combine their resources to attract a pool of funding which they then divide could achieve scale economies and be more socially efficient than nonprofits spending more individually to get the same return (Rose-Ackerman, 1982). However, as in for-profit markets, competition among similar organizations could alternatively increase efficiency by forcing competitors to develop innovative service delivery practices and more efficient administration. Additionally, competition could lead to greater efficiency by causing greater service differentiation and market segmentation as individual nonprofits seek particular niches and capture unique funding streams (Barman, 2002; Chektovich and Frumkin, 2003; Rose-Ackerman, 1982).

The complexity of this issue and the divergent implications that these perspectives yield are important to more fully understand. If all are valid perspectives, a better understanding of the particular circumstances under which to apply each viewpoint would inform policy and management decisions. Theory and empirical research on competition in the for-profit sector is robust. The number of empirical studies concerning competition in the nonprofit and public sectors is increasing, but theoretical development and empirical investigation of markets delivering public goods have a long way to go before they advance to a body of knowledge similar to the study of industrial organization in the for-profit context. This paper therefore focuses on advancing theory that may be applied to competition between organizations in the economy that provide varying levels of public goods, specifically focusing on advancing our understanding of both intra- and inter-sector competition for nonprofit organizations. Existing theories that explain nonprofit activity currently contribute to our understanding of organizations
in specific, targeted circumstances. This paper offers a more comprehensive framework that incorporates these diverse perspectives of nonprofit activity in order to facilitate more general evaluation of competition between nonprofits and other organizations across the economy.

**Literature Review**

*Theory on Nonprofit Activity*

The literature holds little consensus on what drives the formation and growth of nonprofit organizations or how competition affects the sector. While a coherent body of economic theory explains why and how for-profit firms operate in market economies, nonprofit studies lack a similarly cogent framework for analyzing nonprofit organizational behavior. Instead, several disparate theories propose explanations on the existence of nonprofit organizations. Each comes from a different perspective of the role of nonprofit organizations in society and contributes differently to how we may better understand the nature of competition and collaboration among nonprofit organizations and between nonprofits and other organizations in the economy.

Public goods theory (Weisbrod, 1975), also known as market failure theory, explains nonprofit activity under circumstances in which for-profit markets and governments do not meet the heterogeneous demand for collective, public, or quasi-public goods. Markets undersupply these goods and services because they are non-excludable or non-rival (Steinberg, 2006), making it difficult or impossible to charge fees at a level that would sustain production. Since individuals cannot be excluded from enjoying the benefits of these goods, they have little incentive to pay and a free-rider problem results, causing private for-profit firms to refrain from providing adequate levels to match demand. If the services are provided, freeriding threatens the ongoing funding of the services over time. While government could overcome the freeriding problem
through a tax, the limited or heterogeneous demands for many collective goods and services does not warrant uniform government provision in all circumstances. Especially if the average or “median” voter does not prefer the provision of a good or service at the quality or quantity demanded by specific groups of individuals, politicians will be unlikely to supply it because government resources and attention will be allocated toward providing goods and services with greater voter demand (Steinberg, 2006; Anheier, 2005). Individuals might be able to arrange and pay for these services on an ad-hoc basis, but it would be inefficient from a transactions cost perspective (Coase, 1937), leading to underprovision in the absence of coordination among associations of individuals or formal organizations supplying the goods and services. This results in the need for collective action (Olson, 1965) to overcome freeriding behavior and supply adequate levels of the goods and services to match demand. Under Weisbrod’s Public Goods Theory, nonprofits step in to supply underprovided collective goods and services through the private contributions and voluntary efforts of individuals who prefer or demand higher levels of those goods. Even though the free-rider problem still exists and nonprofits do not have the power to tax individuals, they can overcome free-riding behavior through various fundraising strategies, creating private incentives for donating to collective causes (Olson, 1965). Nonprofit organizations therefore step in to “meet a diverse demand for collective goods” in democratic societies, from arts, education, and healthcare to environmental protection and community development, providing goods and services that would otherwise be underprovided by the market or government (Weisbrod, 1988, 25).

Under public goods theory, nonprofits exist not to compete with existing organizations but to fill in where collective goods and services are undersupplied. This theory alone does not predict competition between nonprofits and other organizations for clients or market niche.
Instead, nonprofit competition under Public Goods Theory would likely center upon organizational resources, such as human capital, volunteers, and external funding. However, this perspective views individual nonprofits existing because enough people demand the services they provide and are willing to support the organization through donations and time. Therefore, nonprofit density in any market increases as new organizations attract and maintain support from donors and volunteers who have similar preferences for goods and services. Since the mix of demands and preferences in communities changes over time, nonprofits will compete primarily with other nonprofit organizations for philanthropy. However, if demand for collective services increases and the government decides to directly provide the services, nonprofits may begin to compete with government agencies for funding or niche, and nonprofits may begin to compete with for-profit organizations for government contracts if government decides to indirectly supply the services. In this way, an increase in demand for services that nonprofits provide and the provision of those services by government “crowds out” some nonprofit activity (Anheier, 2005, 123). Higher education is an example of a collective good that has evolved in this manner over time. The first academies of higher learning were collective and nonprofit in nature, filling a gap in knowledge production that was otherwise unprovided by the private market or states. As higher education evolved, public institutions became more prominent players, and public funding became centrally important to nonprofit institutions, both through directly through grants and indirectly through student loans. Today, public and private universities compete for students and the resources they bring, and for-profit universities have grown in part through their ability to compete for students that depend on government loan programs.

Weisbrod’s public goods theory itself does not readily explain the ongoing competition between nonprofit organizations and other organizations in the same industries, such as higher
education, because the theory explains that nonprofits act more as gap fillers than competitors. Market failure theory would expect the market to clear over time as heterogeneous demands for collective services are met, and particularly when demands for services increase, causing for-profit and government suppliers to enter the market. Hansmann (1980) introduced a separate trust-related or contract failure theory, however, that provides an alternative perspective to better understand ongoing competition and particularly why nonprofits would continue to exist in service markets where for-profit organizations operate.

Hansmann argues that the free market undersupplies many goods and services because of high levels of information asymmetry between the producers and consumers. Third party payers have difficulty evaluating the quality of these goods and services, such as daycare, hospital or nursing care, and therefore profit-seeking firms are likely to cut service quality to increase profits (Anheier, 2005). Since the non-distribution constraint prohibits nonprofit organizations from distributing residual income as profits to stakeholders, nonprofit managers lack a profit incentive and are trusted to provide higher quality goods and services under scenarios of high information asymmetry between buyers and sellers (Brown, 2010; Anheier, 2005). Under contract failure theory, consumers, donors, and government trust and prefer nonprofits rather than for-profit organizations for services where contracts are difficult to monitor and enforce.

Therefore, trust or contract theory adds to public goods theory by explaining why nonprofits compete with for-profit firms in supplying some goods and services (Anheier, 2005). In addition to nonprofits competing among themselves for general resources, nonprofits directly compete with for-profits for service markets and government funding in some fields. Therefore, we expect nonprofits to push for-profit providers out of particular market niches where high information asymmetry leads clients and government to suspect unscrupulous behavior or when
profit-motivation could outweigh public or client benefit. However, both nonprofits and for-profits will exist in industries and segmented markets where information asymmetries are not as high for clients who pay for the services they directly receive, such as clients paying for elective surgeries in the healthcare industry. Therefore, even with comparative advantages in certain client markets, nonprofits will continue to compete with for-profits in the same industry for human resources and for client markets where information asymmetries are not as great. This theory also helps us better understand why government would choose to collaborate with nonprofit organizations to provide certain services through government grants or contract arrangements because nonprofits would be trusted over for-profits to deliver on their promises that cannot be easily monitored.

Interdependence theory (Salamon 1987) represents another important extension of market failure theory and the interrelation between nonprofit activity and government action in particular. The nature of public goods, demand heterogeneity and market failure remain the basis of interdependence theory, but the theory more explicitly discusses government “failure” to provide many public goods and philanthropic failure to adequately supply public goods as demand increases for them. Interdependence theory argues that nonprofits and government complement each other and that government largely supports the work done in the nonprofit sector through grants, contracts, and public-private partnerships (Anheier, 2005). Based on this theory, nonprofits can only provide a limited amount of services due to voluntary failure, or the insufficiency of philanthropic resources to supply public goods under situations of increasing demand. As public demand for their services grows, nonprofits increasingly rely on government to fund and support their work, leading to competition between nonprofits for valuable government grants and partnerships.
These theories originate from a demand-side perspective to explain how nonprofits form to meet unmet demands. Supply-side theories, such as stakeholder and entrepreneurship theories, focus on the motivation of those who start nonprofits to explain their existence. Like trust theory, stakeholder theory explains that nonprofit organizations overcome information asymmetries where buyers do not trust for-profits to provide goods and services at the quality level demanded (Anheier, 2005; Ben-Ner and Van Hoomissen, 1993). However, stakeholder theory also acknowledges that, in some cases, individuals prefer to provide the good they consume for themselves to ensure the level of quality they want, and in the process they become both the suppliers and demanders. This will be especially true when particular groups demand a very specific level or quality of the good or service. For instance, groups of parents with education preferences for their children that existing schools do not provide may choose to form a cooperative school (Anheier, 2005) or an independent charter school. Adding this supply-side perspective, stakeholder theory improves our understanding of nonprofit competition by explaining certain situations where nonprofits with similar missions will exist in the same community or service market. Extending the supply-side argument, entrepreneurship theories (Young, 1983; Rose-Ackerman, 1996) argue that individuals who start and lead nonprofits derive utility from non-monetary rewards of nonprofit work, either from achieving the mission of the organization or from other motives, such as religious motivation to serve others. Therefore, individuals or groups of individuals with preferences to create their own organizations and approach social missions in unique ways drive the supply of nonprofit organizations. This explains why so many nonprofits with similar services and missions exist. Since these organizations will only differ based on particular stakeholder preferences or ideology, competition between these nonprofits will be high for external funding (such as foundation or
government grants), human services, clients, and market visibility. These supply side theories predict a larger supply of nonprofit organizations and greater competition for funding than would be expected under demand side theories alone.

*Implications of Theory on Nonprofit Competition*

Overall, each of the major theories discussed above provides different insights into the nature of nonprofit competition. As Anheier and Ben-Ner (1997) point out, these theories complement more than contradict each other. Particularly by combining stakeholder and entrepreneur perspectives with public goods and contract failure theory arguments, we may reasonably expect a greater supply of nonprofit organizations than can be supported (i.e., demanded) by charitable donations. Because new and small nonprofits often rely solely or mostly on donated volunteer time, we expect many more organizations than would be demanded by financial resources to exist, especially in subsectors that have low barriers to entry, do not require large physical or capital assets, or have high exit thresholds due to low operating costs.

Meanwhile, others argue that for-profit theory regarding competition and market structure also applies to nonprofit organizations. Tuckman (1998) applies Porter's five competitive forces to nonprofit competition and demonstrates how entry and exit, power of buyers, power of suppliers, the presence of substitutes, and rivalry among competitors similarly impacts nonprofit organizations, even in markets, such as donation or foundation grant markets, where nonprofits compete exclusively against nonprofits. Lakdawalla and Philipson (2006) characterize all nonprofits as for-profits with lower costs due to tax subsidies and the altruistic motivation of their employees. They argue that for-profit theory holds for nonprofits by treating them as for-profits with lower costs. Extending this argument, Harrison and Laincz (2008) show consistency of for-profit models in nonprofit industries.
Harrison and Laincz (2008) find a key difference for nonprofits, however, showing much greater survival rates for nonprofit organizations than for-profits generally. While new nonprofits form at around the same rate as for-profits, only 17 percent of nonprofits fail after 10 years compared to 80 percent of for-profits (Harrison and Laincz, 2008). As Harrison and Laincz explain, this results in much higher net entry rates for nonprofits than found in for-profits. This finding is consistent with Rose-Ackerman’s (1982) argument that low nonprofit entry barriers will allow ideologically driven entrepreneurs to start new organizations even in saturated markets. While new entrants will attract new donors into markets through additional fundraising and marketing, each organization’s share of overall donations will fall as the number of organizations in a market rises (Rose-Ackerman, 1982). Therefore, high net entry rates in the nonprofit sector translate into increased competition for charitable resources over time.

Young’s (2007) Benefits Theory of Nonprofit Finance adds another important consideration for competition in markets in which nonprofits participate. The Benefits Theory, which is elaborated and empirically tested in Fischer, Wilsker and Young (2010) and Wilsker and Young (2010), is useful to explain nonprofit activity and competition for resources on the program level. Nonprofit organizations are understood to be multiproduct firms (James, 1983; Weisbrod, 1998), in which each organization provides multiple goods and services through various programs. Young’s Benefits Theory elucidates the matches between particular benefits that nonprofit programs produce – individual/private goods and services, benefits to specific groups of individuals, organizational resources that can be bartered or traded with other organizations, and public goods – and financial and volunteer resources available to organizations. Organizations with programs that produce private goods and services are expected to use (and compete for) fees for service. Programs that produce group benefits may attract and
compete for donors, foundation or government grants that target those groups, such as low-income single mothers, individuals with AIDS or other diseases, immigrant populations, or groups that prefer high quality arts in their communities. Organizations with program resources, such as extra office space, donor lists or specialized equipment – or a highly respected brand name - are able to trade those resources with other organizations for additional resources to advance their programs. Meanwhile, programs that produce public goods that align with general voter demands and government programs, such as public health, education and services to the elderly, are well positioned to compete for government grants and contracts.

As voluntary organizations grow and professionalize, they capture greater amounts of financial resources in the markets in which they participate. If a nonprofit’s program fills a particular niche providing a public good that aligns with government initiatives, they may secure public funding to expand and meet non-market demand for that good or service, as Interdependence Theory expects (Anheier, 2005). Alternatively, they may fill a niche with a quasi-market good, such as in the arts, and capture a mix of fees for service and private donations to expand their operations. If their mission and services match particular donors’ interests, such as foundations, or general donors’ interests in a community, solicited through annual fundraising drives, these organizations could be sustained through private giving alone. However, foundations and other donors have finite amounts of money to dispense, applications routinely far exceed foundations’ grantmaking capacity and donors experience fatigue when barraged with too many appeals. Therefore, foundation grants and other forms of philanthropy represent an instrumental but limited source of funding. Foundation grants are particularly useful for nonprofit capacity building and growth due to the expertise and accountability that comes with many grants. However, philanthropy alone cannot fund all of the worthy organizations and
causes that saturate nonprofit markets. As greater numbers of nonprofits formalize, seek funding, and enter the marketplace for donations and grants, competition becomes greater for these resources.

*Implications of Competition in the Nonprofit Sector*

Some of the ambiguity over the assessment of positive or negative implications of competition between charitable organizations derives from the relative complexity of nonprofit activity and complex motivations of nonprofit managers. In contrast to for-profit analysis in which the economic theory of the firm assumes profit-maximizing behavior, nonprofits operate in mixed industries with no one model of objective behavior (Hughes and Luksetich, 2010). Nonprofit objectives may be service-maximizing or budget-maximizing (Steinberg, 1989). Service-maximizing managers strive to improve overall program efficiency while maintaining high levels of quality or quantity of goods and services. Budget-maximizing managers, on the other hand may still emphasize providing a high level of quantity and quality, but they increase the total budget to maximize their own salaries and benefits, leading to wasteful management (Hughes and Luksetich, 2010; Steinberg, 1989). Like for-profits, nonprofits suffer from agency problems in which managers may budget-maximize even though directors emphasize service-maximizing (Hughes and Luksetich, 2010). Under monopoly conditions, managers may more easily budget-maximize, potentially wastefully increasing their own budget, whereas competitive environments may constrain managers to service maximize in order to maintain a competitive edge and survive, leading to greater program efficiency (Feigenbaum, 1987; Hughes and Luksetich, 2010).

Other studies point out that increased competition could lead to efficient aggregate outcomes in the sector in addition to administrative efficiency. For example, faced with
competition from similar organizations, nonprofits may opt to differentiate the services they provide, segmenting the market into more socially efficient sections (Chetkowski and Frumkin, 2003; Gronbjerg, 1993; Han, 1994; Hannan and Freeman, 1977 cited in Barman, 2002). Alternatively, organizations may develop relationships with institutional funders or collaborations with other organizations to attract greater funding exposure, which would also produce more socially efficient uses of limited charitable resources (Barman, 2002; Combs & Ketchen, 1999). Part of the uncertainty of these effects derives from the variation in nonprofit markets. In some markets, such as markets for foundation grants and donations, nonprofits only compete against other nonprofits. In other markets, such as health services, nonprofits regularly compete against for-profit and government providers for paying clients. Meanwhile, other markets such as public infrastructure, transportation and utilities are dominated by government and for-profit players. The nature of markets, goods produced, resources competed for and types of organizations competed against all influence organizations’ responses to varying levels of competition, requiring a stronger understanding of variation in these elements across organizations to better explain the effects of competition and implications for policy and practice.

**Toward a More Complete Theory**

*Extending the Theoretical Framework*

Across demand side theories explaining nonprofit activity, there is a common question of what gets provided by nonprofits versus government and for-profit organizations. Common elements of these theories include the varying public nature of goods and services and levels of demand for those services. Even among supply side theories, while entrepreneurs drive nonprofit startups, and apart from organizations that live on healthy endowments, only fee-based demand
or perceived demand from funders or volunteers can sustain the operations. In terms of what
goods and services are provided by government, there are strong links between the common
elements of demand, such as Weisbrod’s demand heterogeneity argument, and theory in the
public policy literature on policy process and agenda setting.

As alluded to above, Weisbrod (1988) describes nonprofit charitable organizations as
deriving from collective action in communities to develop public goods solutions to public
problems that are not demanded of government by the median voter (Anheier 2005). Under
extensions of this market failure argument as discussed in interdependence theory, over time
voluntary groups suffer from “voluntary failure” because they do not receive enough
philanthropic resources, focus too much on particular subgroups and ignore others, are driven by
donor demands rather than client needs, or lack capacity and professionalization to adequately
approach the social issues they address (Anheier 2005). Because of this, nonprofits depend on
government support and coproduction of community solutions. Likewise, government depends
on nonprofits to coproduce legitimate public approaches to the needs of all citizens in the
community, not just those represented by the median voter.

*Issue Salience and Demand*

One element that is lacking in the general theory explaining the existence of nonprofit
organizations and the development of nonprofit organizations in tandem with government
programs is an explanation of how certain issues evolve to be important (or unimportant) to
median voters and government action. Without this piece to the puzzle, each theoretical strand
works well in isolated circumstances but it is more difficult to place each theory within a broader
theoretical framework to explain nonprofit activity and competition in three sector economies,
and how this competition evolves over time. To make this link, the literature on public problem
definition and agenda setting is useful to consider. Because of this, broader theory from public policy research is appropriate to better conceptualize these roles and interactions. The Multiple Streams Framework is one of the most heavily cited theories on public problem definition. In it, Kingdon (1984, 2003) highlights the “importance of problem recognition” to move issues from general social issues to issues that receive public policy attention. As he explains, there are many factors that contribute to problem definition, including interest group actors, prevailing values for bureaucrats, and the salience of the issue at hand. The salience, or general public recognition and interest in a problem, is a key component to moving issues to the public agenda. Problems, even if important, such as Medicaid coverage for the working poor, may not be recognized by public officials as being important unless they receive adequate pressure and the issue reaches adequate saliency (Kingdon 2003, 114).

Cobb and Elder (1983) also explain the importance of general support and multiple actors pressuring the government actors to define public problems. Like Kingdon (2003), they explain that focusing events or “triggering devices” can help push issues into being defined as public problems and onto agendas. Importantly, issues must make it onto the “systemic” agenda, where they become “public” problems, enjoying widespread attention and shared concern by the majority. However, as Wood and Doan (2003) show, public salience depends on a variety of factors beyond focusing events, including general attention and framing of an issue reaching a “threshold” level within the general population. Even then, however, issues may or may not reach the “institutional” or formal governmental agenda (Cobb and Elder 1983). As Jones and Baumgartner (2005; also see Baumgartner and Jones, 1993) discuss and empirically demonstrate, meaningful policy change occurs in not in steady development but in punctuations, which occur when the salience and need for new policies builds to a great enough level to break through
“institutional frictions” that otherwise cause public agendas to adjust incrementally and disproportionately to “moderate” demands in the overall political and societal landscape. Ultimately, the progress of an issue to a public problem that reaches the formal agenda depends on multiple actors, the legitimacy of issues and relative importance of the people they affect, and constraints, such as the public budget (Cobb and Elder 1983).

This concept of issue salience translates well into specific components across theoretical perspectives of nonprofit activity discussed above. Under Public Goods Theory, organizations that work to provide public and collective goods to match heterogeneous preferences in the general population (Weisbrod, 1975) fill market niches that have not gained the public salience to demand government action. When collective goods receive enough public attention, through focusing events or punctuations, they would be expected to have greater chances of moving onto the public policy agenda. If there is adequate pressure and policymaker action to do so, these goods would begin receiving government funding, which would open the door for expansion of those services through nonprofit and government coproduction, as expected under Interdependence Theory (Salamon, 1987). With substantial public attention and widespread provision of these services, for-profit players would also be expected to enter into these markets if contracts could be sufficiently monitored and enforced.

In this way, the concept of issue salience, when related to the concept of demand, also extends current theory and translates well to explain the involvement of for-profit firms in nonprofit and public markets. Under general theory explaining nonprofit activity, when the goods and services provided in these markets are collective or public in nature, or even quasi-public, we would not expect for-profit organizations to be involved in the supply. However, if issues are highly salient and reach a stable demand as demonstrated by making it onto and
remaining on the public agenda, space for for-profit investment opens. This may be especially true in highly technical and/or widespread government services where large, for-profit corporations may capitalize on scope and scale economies, such as seen in for-profit participation in public infrastructure projects, Medicare/Medicaid processing, national defense equipment and contracting, and emerging areas that have gained stability on the public agenda, such as space exploration. The parallel between salience and demand also helps untangle some of the ambiguity of when to apply contract failure theory, which explains that when performance is difficult to assess, information asymmetries between principals and agents are great and contracts are therefore difficult to monitor and enforce, the public and government will prefer nonprofit over for-profit service providers (Hansmann, 1980, 1987; Easley and O’Hara, 1986; Krashinsky, 1986, 1997). This is typically applied in cases of third-party payers of services someone else directly receives, such as child care, elderly nursing care and international assistance. However, the nature of these goods is generally more private than public, representing a special case of nonprofit activity where the centrality of trust predominates in the decisions to prefer organizations that are expected to refrain from profiting off of shirking behavior. Adding to the ambiguity of when to apply contract failure theory, for-profits regularly operate in these fields and they dominate other industries that have high information asymmetries, such as car repair and private medical offices. The question arises of why for-profits successfully penetrate some of markets characterized by information asymmetries and not others. Salience and the level of demand help explain this sorting. If demand is low for a particular good or for a particular quality of a good, it will be less attractive for for-profit actors and more likely for individuals and government to prefer a nonprofit provider because there are
not competitive market pressures to encourage for-profit organizations to maximize service quality.

Without adequate levels of substitute providers, the threat of sanction and oversight mechanisms is lower, and the transaction costs of consumer monitoring and principal-agent oversight within the firm would be greater than would be worthwhile. Businesses such as car shops regularly deal with these costs and they are sanctioned by customers leaving to their competitors when they are caught shirking. Doctors in private medical and dentistry offices also need to meet certain patient numbers to be profitable and experience competitive pressures to deliver quality services. Due to the technical nature of the services in these fields, agents can shirk, but general and widespread demand for their services has encouraged outside monitoring and enforcement through licensing bodies and oversight groups such as the Better Business Bureau and Angie’s List.

This same pattern can be applied to club goods, as well. Membership groups, such as consumer clubs and broad social clubs with high general demand, such as Sam’s club, music/movie buying clubs, Facebook and other large-scale social media are for-profit, whereas more localized or specialized clubs with lower demand for the specific level of quality provided are generally nonprofit, such as Community Supported Agriculture (CSA) groups, golf clubs, social and recreation associations. As discussed in the literature on clubs (Buchanan, 1965; Hansmann, 1996; Gugerty and Prakash, 2010), this is in part because the quality of the club depends on the quality of the members so a profit motivation is suspect since it can exploit individual members’ status.
Combining Perspectives: the Publicness of the Good and Issue Salience

By pairing theoretical lenses derived from theory on the demand for nonprofit organizations and the importance of issue salience for public agenda setting, a more general theoretical framework can be developed to explain nonprofit activity across the special circumstances described in current theories discussed above. When viewing issue salience as synonymous with the true or perceived demand for goods or services in the general population, this combined framework explicitly includes interorganizational competition as a central force affecting the development of public, private and profit organizations in various service markets.

Figure 1 illustrates a graphical representation of the combined theoretical frame. As shown in figure 1, the “Publicness” of a good or service varies across the y axis from private goods to public goods. As shown along the right hand side of the graph, the nature of resources organizations compete for (ranging from private fees to public/donations) is expected to vary with the nature of the good, as Young’s Benefit Theory expects. “Issue Salience,” or the perceived or actual demand of a good or service varies across the x axis from low, or limited demand shared by small groups, to high, or widespread demand in the general population. As shown along the bottom of the graph, interorganizational competition is expected to co-vary with Issue Salience. As shown, in general, just because a good is classified as public, it is not necessarily expected to be provided by government, following Weisbrod’s Public Goods Theory. Likewise, just because goods may be private in nature, they are not necessarily provided by for-profit firms. The interaction between Issue Salience and the Publicness of the good is expected to influence the public or private, profit or nonprofit nature of the organization providing the good.

As shown in the figure, current theories explaining nonprofit activity fit among this framework as special cases of specific levels of Publicness and Issue Salience. For instance, club goods
demonstrate low Publicness (they primarily provide private or experience goods to individuals) and low Issue Salience because they appeal to relatively small groups of the population characterized by heterogeneous preferences. Because of their low demand, for-profit actors prefer not to provide these goods, and as discussed above, individuals may prefer nonprofit rather than for-profit motivations for the organization providing the service. Along this band of private and consumer goods, Stakeholder Theory and Contract Failure Theory fit to explain the use of nonprofits to provide goods that have high information asymmetries, depend on trust to assess the quality of the service and lack levels of supply and demand that would produce competitive pressures to prevent shirking by profit-seeking firms.

Moving up the Publicness scale, toll goods that are excludable but not rival (up to a point of congestion) include goods and services such as the arts, museums, performing arts, as well as public infrastructure projects, roads and bridges. Many of these goods, such as the arts, are commonly found in the nonprofit sector. Others, such as paid parking lots or cable television are almost exclusively for-profit, and public infrastructure projects are supplied by a mix of public and private, for-profit actors. Applying the view of Issue Salience, this variation can be explained by the general demand for these services. There is a general demand for cable television and the demand for parking is widespread across urban environments, creating effective space for profit-seeking firms and entrepreneurs to operate. On the other end of the spectrum, many museums appeal to relatively small audiences, making it difficult for ticket prices to cover the costs of producing the quality of these goods that are preferred by those who demand them. Because of this, congruent with Public Goods Theory, this heterogeneous demand for these quasi-public services is met by private donors and nonprofit action. Meanwhile, public infrastructure projects such as roads and bridges have widespread demand and are reasonably
technical, requiring specialized knowledge and equipment. These factors lead to potential for profitable activity with the proper investments. Since these goods have a stable place on the public agenda, there is a stable demand from government to contract these services, making them appealing to for-profit activity.

In the middle band of the graph are goods that have a mix of public and private qualities, such as healthcare, education, and human services. Because of the widespread positive externalities (public goods) produced when these goods are provided to the general population and general demand for these services from the population, government has long included these services on the public agenda. Because these goods and services are primarily private in nature, serving individuals, fees can be assessed, either covered by individuals themselves or through third-party payers, such as insurance or the government through consumer-side subsidies. These factors create the potential for effective public-private partnerships to develop. Services that appeal to groups of people willing to pay for them, such as foundations and donors who are willing to pay for free medical clinics for undocumented immigrants, the uninsured and the working poor would have relatively low demand and operate as nonprofits, as explained by Public Goods Theory, with organizations competing for group resources as expected by the Benefits Theory. Other goods and services that have more general appeal would be more likely to be provided by a mix of public, nonprofit, and for-profit actors depending on the salience or demand, the publicness of the services, and if government includes them on the public agenda. As issues in this public-private partnership band develop to attract greater public salience, government is more likely to move them to the public agenda and provide avenues for funding, as Interdependence Theory discusses. This trajectory can be seen with many types of organizations, such as battered women’s shelters that developed from grassroots nonprofit
organizations to government funded services in the 1970s and 1980s (Sandfort, 2005a, 2005b, 2005c).

Figure 1: Illustration of Combined Framework

Quasi-public goods that are rival but non-excludable, known as common pool resources, depend on their general salience and demand to be identified as important for public policy to address. Common irrigation channels, the maintenance of neighborhood parks and other
resources with low or isolated demand may be effectively managed by horizontal voluntary
groups (Ostrom, 1990). Similar goods, such as public water supplies and water treatment plants,
however, are sufficiently public in nature and have sufficient salience and widespread demand to
place them firmly on the public agenda, and they are generally provided by government. Other
public goods with high salience or general importance, such as national defense are also
provided by government, with potential during periods of particularly high salience, such as
wars, to encourage for-profit involvement in many goods and services to sustain large militaries.
Meanwhile, other public goods and services, such as response to natural disasters, experience
sporadic and unpredictable periods of extremely high salience and demand (i.e., during and
immediately following natural disaster events). In general, these services have a mix of
government and nonprofit actors, with key challenges for raising funds on an ongoing basis
given the short-lived issue salience following events. During such times of intense salience,
many organizations compete for funding from donations and government to respond to the
crises, but private donations in particular quickly subside as issue salience and public attention is
supplanted by other current events.

Illustration of Temporal Shifts in Issue Salience using Internet Search Data

Data on internet searches from Google Trends (www.google.com/trends) illustrates
temporal shifts in issue salience for goods across the Publicness spectrum. As explained by
Google, these data are derived from Google user internet searches and are catalogued weekly by
search theme from 2004 to the present. More specifically,

Google Trends analyzes a portion of Google web searches to compute
how many searches have been done for the terms you've entered, relative
to the total number of searches done on Google over time. This analysis
indicates the likelihood of a random user to search for a particular search
term from a certain location at a certain time. Keep in mind that Trends designates a certain threshold of traffic for search terms, so that those with low volume won't appear. Our system also eliminates repeated queries from a single user over a short period of time, so that the level of interest isn't artificially impacted by these type of queries. https://support.google.com/trends/answer/92768?hl=en&ref_topic=13975

For illustration, the relative internet search volume in the U.S. for five goods or services are shown below, including searches for “nursing care,” “doctor,” “iPod,” “symphony” and “hurricane.” As shown, the general issue salience varies across these goods and across time. Goods that are characterized by greater private benefits, such as the iPod and doctors receive the highest average search traffic over time with peaks when new versions of popular consumer products such as iPods are released or during high demand periods, such as winter flu seasons for doctors.

Figure 2: Salience of Selected Issues in U.S. Internet Searches from 2004 to 2013
Meanwhile nursing homes experience much lower issue salience than “doctors.” Since the nursing home industry is a mixed industry with many nonprofit organizations operating in the same markets as for-profit and government players, lower issue salience is congruent with the general expectations that nonprofits will provide greater amounts of services in markets with lower issue salience or general demand, controlling for the general nature of the good or service produced. Symphonies, a generally nonprofit category of services in which nonprofits exclusively exist in many markets, receive the lowest issue salience of the five issues shown. This is also in keeping with the framework presented and with the general expectations of Public Goods Theory since symphonies are preferred by relatively small groups of people within the general population. “Hurricane” presents an interesting case of natural disasters that receive immediate and widespread attention, as well as the greatest isolated magnitudes of issue salience, following events (Frances, Katrina, Irene and Sandy for the major hurricanes shown from left to right). However, issue salience and public attention very quickly drop, leading to challenges for organizations to rapidly develop funding while the public’s attention is captured.

**Discussion and Implications for Policy and Practice**

This framework combining the Publicness of goods and Issue Salience advances a more general theory on nonprofit activity than currently provided in the literature. As discussed above, the major theories explaining nonprofit activity are consistent with this framework as special cases of nonprofit activity within the general theoretical frame. This framework also more explicitly addresses issues of competition in the nonprofit sector and between nonprofit organizations and other organizational forms in a three sector economy. Several implications
emerge from this framework when applied to organizations in varying markets characterized by the nature of the good produced and the salience of the issues organizations address. In markets with low issue salience and mostly private goods, nonprofits are expected to compete with other nonprofits on a limited basis for volunteers, members, and philanthropic funding. In general, due to the limited or isolated nature of demand for these services, such as clubs and organizations explained by stakeholder theory, these markets are expected to be generally noncompetitive and funded by the individuals that both demand and supply the services. For more salient goods that are characterized by high levels of information asymmetry between buyers and sellers, nonprofits are expected to be preferred over for-profits in markets with low to moderate levels of salience and demand, as explained by contract failure theory. As private goods become more salient in the general population, however, greater competition for fees and market share emerge, with for-profit actors dominating most consumer markets, regardless of information asymmetries, which can be overcome with sufficient pressures from competitive markets.

For goods that are more public in nature but that have low levels of issue salience and demand, Public Goods Theory holds under which nonprofits generally supply collective goods that are otherwise undersupplied by for-profit markets and government. In these markets, nonprofits primarily compete against other nonprofits for charitable funding, limited government grants and fees. Greater fundraising efforts, marketing of these goods and policy advocacy for greater public attention on these issues may attract greater philanthropic investment or potentially push these issues into greater salience, creating potential for greater general demand and possibly government involvement if these issues make it onto the public agenda. This would in turn open up potential for for-profit involvement as the services receive greater demand and government seeks partnerships to implement its policies. This could result in greater levels of
competition between nonprofits and for-profits in these markets, but it would also introduce
greater government support of nonprofit organizations, increasing their capacity to deliver public
goods and services, as explained by Interdependence Theory. As empirically demonstrated by
Lecy and Van Slyke (2012), this could also lead to greater nonprofit entry into these markets
over time. In general across levels of publicness, greater inter-organizational competition is
expected with greater issue salience.

As discussed above, the key contribution of this theoretical framework is the inclusion of
issue salience as a central component to competition in nonprofit markets. Varying issue salience
also has important implications for the effects of competition on management in the sector and
helps sort some of the previously discussed complexities on when to apply various perspectives
to discern implications of competition on efficiencies or inefficiencies in the sector. For instance,
Rose-Ackerman (1982) argues that greater density of nonprofit organizations competing for the
same pool of funding is inefficient. Because charitable funding is essentially a common pool
resource, more numerous actors tapping into the funding pool presents a problem of the
commons that diminishes the utility of these funds over time. This argument, however, depends
on stable or static levels of funding for nonprofits to share as their market grows. Applying the
issue salience perspective, it becomes easier to sort out when this problem might exist or not.
Under the framework presented above, when nonprofits enter markets, they largely do so in
response to increased issue salience and greater general preferences for funding the issues new
nonprofits seek to address. With their entry and fundraising efforts, new nonprofits further
increase issue salience by appealing to broader populations to support the cause. Existing
organizations also respond to incentives of additional funding sources by more heavily marketing
their programs to potential funders, which in turn provides market pressures on institutional
funders, such as foundations, to strategically respond to these demands (or perceived demands) and direct additional funding to those areas. In this way, increases in competition or density of organizations can produce increases in funding pools. Greater competition for these funds would also encourage greater efficiencies from organizations appealing to donors and funders and trying to maximize comparative advantages, such as the quality of their programs, quantity of services provided, and measures of financial and organizational efficiency (Castaneda et al, 2008; Feigenbaum, 1987; Thornton, 2006; Tuckman, 1998).

Conversely however, if salience wanes and issues fall off or get pushed off the public agenda and out of donors’ and foundations’ priority foci, the general pool of funding in particular nonprofit markets could decline over time. Because exit rates are low in the sector (Harrison and Laincz, 2008), the density of organizations and competition for funds would not be expected to decrease as issue salience falls. Because of this, Rose-Ackerman’s (1982) problem of the commons would be more applicable in these scenarios, such as seen in declines in funding to the arts and shifting donor preferences toward human service organizations in the economic recessions following September 11, 2001 and that intensified in the subsequent recessionary period of that decade. During such scenarios of declining issue salience but stable or growing market density, the encouragement of collaboration and common funds instead of competitive fundraising may be appropriate to incentivize from policy and funder perspectives. These coordinated efforts may have greater efficiency than diffuse fundraising appeals from individual organizations as Rose-Ackerman suggests. Furthermore, the existence of these funds, such as The Metropolitan Atlanta Arts Fund (Pousner, 2011), could be the deciding factor for the survival of some organizations during periodic drops in issue salience.
An interesting challenge emerges for organizations that regularly experience volatile issue salience in the general population for their goods and services, such as disaster response. As implied by the Multiple Streams Framework and the random, limited opportunities for action within windows presented by focusing events, nonprofit and government actors must act quickly to secure resources and political support before attention on the issue wanes. The question emerges of whether competition for funding, and the widespread and diverse funding appeals from new and existing organizations in these fields following focusing events is efficient or inefficient over the long term and over multiple iterations of similar events. Instead, coordinated and centralized rather than competitive and diffuse efforts in these scenarios may yield greater efficiency in immediately combining and tracking funding to be later dispersed when public attention and donations diminish.
Resources


