7

Money for mission or moral minefield? The opportunities and risks of not-for-profit business venturing[1]

Bronwen Dalton and John Casey

Introduction

Increasing numbers of Australian not-for-profits have come to embrace the idea of participating in the market to maximise their revenue. In the academic literature assessments of not-for-profit business venturing are mixed, with some scholars highlighting the benefits of commercialisation (Dees 1998, 2001; Boschee 2001; Borgaza & Defourny 2001; Simons 2000; Thompson 2002) and others noting commercialisation's tendency to create tensions between not-for-profits' mission and market and to adversely affect community relations and public image (Chetkovich & Frumkin 2003; Ryan 1999; James 2003; Gunn 2004). In business circles the response has been less than enthusiastic, with many arguing that not-for-profit run businesses are a source of unfair competition (Bennett & Dilorenzo 1989). In Australia, these arguments have been aired in government inquiries (investigations into the tax status of charities have been conducted by the Department of the Treasury in 2001, and by the Industry Commission in 1995), in courts (such as in *Commissioner of Taxation v Word Investments Ltd* [2006] FCA 1414) and in a wave of media reports, particularly in the Australian business media. If not-for-profits are to undertake business venturing, it is important for them to understand the meanings and contestation that surround it. In particular, not-for-profits need to be aware of the risks of being seen by the public as more of a business than a social agency and to develop ways to effectively and coherently align mission, strategy and revenue streams.

This chapter begins by defining not-for-profit business venturing and then discusses various interpretations of business venturing in the academic literature. It then traces the rise of not-for-profit commercial activity in Australia and in comparable countries, notably the United Kingdom and the United States. Responses to business venturing from the business community are then discussed and the findings of a review of recent media reports which focus on the commercial activities of not-for-profit organisations are presented. The chapter concludes by discussing some measures that may improve not-for-profits' capacity to capitalise on the benefits, while minimising the risks, of commercialisation.

What is not-for-profit business venturing?

Not-for-profit associations draw their revenue from a wide range of sources. These include government grants and contracts, fees paid by members and other users of their services, and fundraising activities. In recent times, however, one of the fastest growing sources of revenue has been the returns made from commercial activities (see for example Zappalà and Lyons' chapter in this book on the spread of community–business partnerships).

The kind of entrepreneurial activity not-for-profits engage in as a means of raising revenue is generally referred to as business venturing. Business venturing can be defined as regularly conducted commercial activities that increase the reliance of not-for-profit organisations on sales revenue rather than on donations or government grants (James 1998: 271).

Academic perspectives

For many not-for-profits and those that study them, business venturing has become the new orthodoxy – accepted as the most logical response to a situation that calls for them to stretch limited resources. This has occurred within a broader context that is characterised by the legitimisation of the business model within the not-for-profit sector (Kenny 2002; Frumkin 2003); this business orientation is evident in much of the academic literature. Morales (1997), for example, emphasises the increased autonomy and flexibility gained by earned-income strategies:

> Earned income can provide funds that [community service organisations (CSOs)] can allocate without any conditions or constraints: it helps groups overcome the pitfalls of becoming a donor-driven organisation or a mere implementer of donors' pre-determined programs. CSOs will be free to design and implement programs that are more responsive to the needs of their members or beneficiaries. They will also be free from the reporting and accounting requirements of donors. (Morales 1997: 23)

Positive assessments of business venturing are especially prominent in the social entrepreneurship literature, which refers to a broad set of entrepreneurial strategies to address social goals (Boschee 2001; Borgaza & Defourny 2001; Simons 2000; Thompson 2002). Business venturing is supported in work that focuses particularly on the not-for-profit sector in the United States and Canada and looks at earned-income strategies as elements of social enterprise in not-for-profits (Dees 1998, 2001). Social enterprises are often characterised as having two major organisational goals: to generate earned income and to expand the organisation's efficiency and impact through adoption of entrepreneurial modes of operation (Emerson & Twersky 1996; Boschee 2001; Borgaza & Defourny 2001;

Simons 2000; Thompson 2002). This kind of research and analysis is related to arguments about how public enterprises can become more efficient by taking a dose of 'market medicine' (Deakin & Walsh 1996). For example, the well-known social enterprise advocates Dees and Anderson note that:

> Increasingly we are turning to business methods and structures in our efforts to find more cost-effective and sustainable ways to address social problems and deliver socially important goods. (2003: 16)

In a similar vein, much of the fundraising and resource development literature is focused on resource mobilisation targeting the market sector rather than donors or the state, activities often described as 'venture philanthropy' (see, for example, recent editions of the journal *New Directions for Philanthropic Fundraising*, including articles such as Reis & Clohesy 2001; Frumkin 2003).

In much of the social enterprise and fundraising literature the ability to simultaneously fulfil charitable and commercial roles is not generally problematised and, in the case of the social enterprise literature, 'going commercial' is often treated as a tenet of the social entrepreneurial approach. A consequence of this interpretation is that activities such as developing partnerships with business, or establishing social enterprises, are seen within the sector as good practice. Many not-for-profit executives feel that their organisations must appear more businesslike in order to be considered disciplined and effective (Frumkin 2003). In a 2003 survey of US not-for-profit executives by the Bridgespan Group, over 50 per cent of respondents said they believed earned income would play an important or extremely important role in bolstering their organisations' revenue in the future (Bridgespan Group 2005).

Not everyone, however, has welcomed moves by not-for-profits to embrace a business framework and there is a significant literature about mission/market tensions in not-for-profits. Various authors have described how business venturing can have negative consequences in terms of not-for-profits' mission, capability, financial capacity, legal situation, community relations and public image (Chetkovich & Frumkin 2003; Ryan 1999; James 2003; Gunn 2004). Gunn, for example, warns about potential 'mission drift', and that:

> [any] assessment of whether or not to take the road of for-profit ventures must include attention to where the internal resources will come from to build a new venture, how the potentially different culture of the two parts of the organisations will fit together, and whether the incentive and compensation structures of the organizations might clash, among other issues. (Gunn 2004: 169)

James (2003: 35) identifies what she describes as the 'potential dangers' of commercialisation, in particular how a focus on earning profits could impact on managerial values, create conflicts of interest and lead to public funds being diverted for private gain. In *The State of Nonprofit America* (2002), Salamon highlights growing mission/market tensions in the not-for-profit sector of the early 21st century. The relevant trends include growing reliance on – and pervasiveness of – fee revenues, an increasingly entrepreneurial culture within the not-for-profit sector, growing involvement of not-for-profits with corporate partners, and intensifying competition with for-profit service providers. With these forces in play, Salamon observes: 'The move to the market may thus be posing a far greater threat to the nonprofit sector's historic social justice and civic mission than the growth of government support before it' (2002: 47).

The rise and rise of not-for-profit business venturing

Not-for-profits have been involved in commercial businesses for a long time. It was a key feature of the poorhouse system in Victorian England, in particular of the institutions known as workhouses, and was also characteristic of the early history of welfare in the United States (Digby 1978; May 1997). However, for most of the 20th century, Australian, UK and US not-for-profits, often affiliated with Christian denominations, relied on raising donations from the public and on government grants rather than on engaging in commercial businesses. Those few not-for-profits that did operate businesses usually were involved in low-risk, small-scale activities such as operating second-hand clothing outlets (charity shops) and were often directly mission-serving, such as the few specialist not-for-profits that operated businesses to employ people with disabilities (Lyons 2001; Kendall 2003; Steinberg 1987). In Australia, one well-known exception was the non-woven textiles manufacturing business run by The Smith Family. Another significant source of revenue has been that generated from the gambling and hospitality income of clubs, including those affiliated with the Returned and Services League of Australia (war veterans) (Lyons 2002). In the United States, well-known examples are the business activities associated with Goodwill Industries and the Scouts movement, such as Girl Scout cookies, as well as museum stores (James 1998; Weisbrod 2000). In the United Kingdom, the most visible entry of not-for-profits has been in the retail sector, with the rapid growth in the number of charity shops: in 1992 there were around 3480 charity shops in the United Kingdom, with sales of £183.3 million; by 2002 there were 6220 shops, with total sales of £426.5 million; by 2006 there were over 6500 charity shops throughout the country (Charity Finance 2002; Parsons 2002).

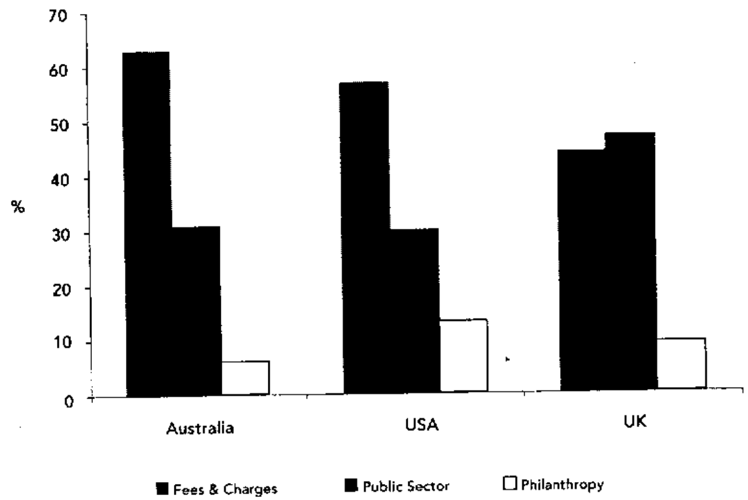
More recently, both interest among not-for-profits in commercial practices and the breadth of not-for-profits' commercial operations have grown significantly (see, for example, Capling and Marjoribank's chapter in this volume). According to Australia's St Vincent de Paul Society (cited in Commonwealth Department of the Treasury 2001: Ch. 27):

> There is a wide acceptance within the Australian community that charities and related organisations conduct commercial activities to support their core services ... What differentiates this type of 'commercial' activity from that undertaken by for-profit organisations is that the profits are used directly for the core purpose of the organisation, that is, the relief of poverty, destitution, suffering or misfortune, rather than distribution to shareholders.

The Johns Hopkins Comparative Nonprofit Sector Project, which analyses the scope, structure, financing and role of the not-for-profit sector and now covers 39 countries, highlights the significance of revenue from sales of goods and services in financing not-for-profits throughout the world (Salamon et al. 1999). As Scott (2003) has observed, there are various issues affecting direct comparisons between countries – for example, Australian figures do not include revenue from self-funded or self-governed universities and not-for-profit hospitals – but the findings provide another indicator of the growth of earned-income strategies. In the Johns Hopkins project the category 'fees and charges for services' was used, and it covered revenue generated from a range of activities, including sales of goods, hospitality income of clubs, business sponsorships and membership dues. For Australian data the project relied on the Australian Bureau of Statistics' (ABS) *Non-Profit Institutions Satellite Account 1999–2000* (ABS 2002). However, it should be noted that most of the revenue recorded by the ABS is from the sale of goods and services related to the primary purpose of the not-for-profit, such as fees received for child care and schooling, and membership payments. One grey area is the significant amount of revenue generated by registered clubs through their provision of gambling services, principally their operation of poker machines. The status of this income stream – that is, whether it is earned as part of the primary activity or purpose of a hospitality club, or is rather an incidental money-making activity – has not been legally tested. Figure 7.1 shows the major sources of revenue for not-for-profits in Australia in comparison with those in the United States and the United Kingdom.

Figure 7.1 shows that in 1995, revenue from fees and charges received by Australian not-for-profits accounted for almost two-thirds (62.5 per cent) of total not-for-profit income. In the United States, the dominant source of income was fees and charges (57 per cent), followed by government funding (30 per cent) and private donations

Figure 7.1 Three country comparison of source of not-for-profit revenue (1995)



SOURCE Kendall & Almond 1999; Sokolowski & Salamon 1999; Lyons 1999; in Salamon 1999.

(13 per cent). In the United Kingdom, government funding was the dominant source of income (47 per cent), followed by fees and charges (44 per cent) and private donations (9 per cent).

In the United States, another indicator of the increased amount of not-for-profit business venturing is the rise in the number of not-for-profits paying unrelated business income tax (UBIT).[2] The proportion of not-for-profits reporting taxable activities increased from less than 5 per cent in 1975 to over 14 per cent in 1999 (US Department of the Treasury, Internal Revenue Service 2000). Not-for-profit taxable revenues have also grown significantly, from $56 million in 1986 to $277.5 million in 1995 (Riley 1997). However, the reliance on self-reporting and the improbability of tax audits together mean that these figures do not fully reflect the extent of not-for-profit commercial activity (Brody & Cordes 1999; Hines

(2000). In this vein, Brody and Cordes argue that 'the UBIT has, in effect, become a voluntary tax and has served, at most, as an "intermediate sanction" short of the loss of tax exemption for charities earning "too much" commercial income' (Brody & Cordes 1999: 3).

This development has occurred in a context where the not-for-profit sector has assumed many welfare service provision functions; where demand for services continues to outstrip supply; and where discretionary funding has been increasingly limited under government contracting and project-based models (Lyons 1997; Nowland-Foreman 1998). In this situation, income generated from business activities has become valued as 'unallocated' funds that can be used in any area of charitable work. As stated by one of Australia's largest charities, The Smith Family, business venturing 'supports our work in the community by generating untied funds and offsetting the costs of running the organisation' (Smith Family 2005).

Perspectives from business: Funding good works or unfair competition?

Not-for-profits compete with for-profits in a number of key industries, most recently in areas such as child care, education and nursing homes. In Australia, there is fierce competition between the two breakfast cereal makers: Kelloggs Pty Ltd and the Seventh Day Adventist Church-owned Sanitarium Health Food Company. In the United Kingdom, charity shops compete with major clothing stores. In the United States, local YMCAs compete with for-profit health clubs; the American Association for Retired People competes for market share with for-profit insurance product providers; and National Geographic is pitted against Discovery Channel in the cable television market.

Accompanying the expansion of not-for-profits into the market have been complaints from for-profit businesses that not-for-profits are unfair competition. In the United States, in August 1986, delegates to the White House Conference on Small Business called for government to give preference to private enterprises when awarding government contracts (Gomes & Owens 1988). More recently, the International Health, Racquet and Sportsclub Association (IHRSA) has run an ongoing campaign against operators of not-for-profit health and racquet clubs such as the YMCA and the Jewish Community Centre (IHRSA 2003).

In the United Kingdom, the Federation of Small Businesses has repeatedly complained about the introduction of bought-in goods in charity shops; combined with those shops' preferable tax and rates concessions, they argue, this has given them an unfair advantage. The essence of their argument is that charity shops' presence on the high street represents a serious threat to other local small traders (Federation of Small Businesses 1994). Evidence from different parts of the United Kingdom has indicated that Chambers of Commerce have sought to exert pressure on local authorities to limit the number of new charity operators (Paddison 2000). The UK-based Forum of Private Business – which, interestingly, is registered as a charity – has devoted a section of its website to advocating a change in the tax arrangements for charity shops, declaring: 'We believe that the new breed of professional charity shops selling new goods are undercutting small businesses and should no longer benefit from tax breaks' (Forum of Private Business 2006).

In Australia, Kelloggs Pty Ltd and a consortium of for-profit, healthcare-related companies commissioned reports submitted to the Inquiry into the Definition of Charities and Related Organisations established by Prime Minister Howard in September 2000. The submissions argued that charitable groups had an unfair advantage when competing with for-profit organisations due to their taxation concessions extending to their commercial operations. In another submission to the inquiry, relating to the health industry and commissioned by a group of private healthcare companies, the estimated value of the income tax exemption to not-for-profit hospitals is between 2.1 and 3.0 per cent of operating costs and, taken with other tax concessions, is equivalent to at least 5 per cent of total costs (Allen Consulting Group 2001). The submission prepared by Access Economics on behalf of Kelloggs Pty Ltd argued that the

tax exemption of Sanitarium Health Foods allowed it to significantly undercut competitors. The report argued that:

> The market share scale of Sanitarium's operations in Australia is virtually unprecedented internationally ... This speaks volumes for the distorting effects – and tax revenue losses – incurred as a result of the Australian type concessions. (Access Economics 2001: 20)

More recently, in an interesting test case, in November 2006 the Australian Commissioner of Taxation took a case to the Australian Administrative Appeals Tribunal arguing that a commercial funeral director operating as Word Investments – set up primarily to raise funds for the charity Wycliffe Bible Translators – was carrying on a commercial activity and not entitled to endorsement as a charity, nor to income tax exemption. A cross-appeal by Word Investments was later upheld by the Federal Court: an organisation that raises funds exclusively for a charitable purpose through a commercial enterprise is not precluded from being a tax-exempt charity. The Australian Taxation Office is currently appealing this decision (ATO 2006a, 2006b). A finding against the not-for-profit could prompt many other for-profit competitors to launch similar cases. Alternatively, if the appeal fails, not-for-profit run businesses will be able to cite the judgement as a basis for maintaining their tax-exempt status.

These arguments have also been expressed by academics. One of the best known examples is the book *Unfair Competition: The profits of nonprofits,* by Bennett and Dilorenzo, which argues that not-for-profits enjoy a whole host of advantages – chief among them being tax-free status and reduced postal rates – that give them an unfair advantage in the marketplace:

> The effect of these special privileges is that governmental policy not only reduces the costs of nonprofit organizations, but it also raises the costs of doing business for their for-profit competitors. Profit-seeking firms must pay higher taxes and postal rates to offset the subsidies accorded non-profits. Thus, because of this

> preferential treatment, competition between nonprofits and for-profits is inherently unfair. (Bennett & Dilorenzo 1989: 21)

Such arguments raise an important question: is the business view of not-for-profit business venturing shared by the wider public?

Review of media coverage of not-for-profit business venturing

Ascertaining public opinion throws up major methodological challenges. One approach has been to examine how an issue is dealt with by the mass media. Gamson argues that the mass media plays a central role in modern societies because it is the most generally available forum for debates on meaning and it is the major site in which contests over meaning must succeed. This latter point is a tacit acknowledgement of the fact that the mass media not only describes, but also influences, cultural change (Gamson 1988). Media analysis has also been used in the not-for-profit literature (see the extensive survey of media reports on incidents of fraud in the sector by Fremont-Smith and Kosaras [2003]). It is important for Australian not-for-profits to be aware of media constructions of an issue: it is a way of understanding wider discourse and how the media or other groups may distort this discourse in ways that serve their, or their readership's, interests.

The review of media treatment of not-for-profit commercial venturing is based on reports in major news and business publications in the United Kingdom, the United States and Australia over an 18-month period (1 September 2003 to 30 March 2005) as identified by the media search engine *Factiva*™. The search terms, designed to cover a whole range of topics relating to business venturing, were: 'nonprofits', 'not-for-profits', 'charities', 'NGOs', 'business venturing', 'social enterprise', 'social entrepreneurship', 'community', 'economy', 'development' and 'finance'. A total of 11 articles were found to significantly focus on not-for-profit organisations' involvement in commercial activities, although we

readily acknowledge that these articles are indicative, rather than definitive, of recent media coverage. The coverage can be separated almost equally into positive (five) and negative (six) assessments of the practice of business venturing (see Table 7.1).

As the positive articles in Table 7.1 show, some media reports adopt a position similar to that expressed in much of the social entrepreneurship literature; five articles advocate that current not-for-profit management deficiencies can be remedied through involvement with the market, because of both the additional income generated and the market orientation and business methods it engenders. For example, one report described how:

> The burgeoning field of social enterprise – trading for social purposes – now aims to replicate business successes through franchising, while looking on failures as means to innovation and reinvigoration. (*The Times*, 29 June 2004)

The negative articles are of course less enthusiastic about not-for-profits' burgeoning corporate orientation. In particular, business activity that does not appear to be directly tied to the realisation of a not-for-profit's mission – that is, activities not employing the disadvantaged nor selling mission-driven products and services – has been the subject of criticism. The three themes that strongly emerge from the articles are unfair competition, the greater risks of exposing not-for-profits to fraud and scandal, and the blurring of the distinction between profit and not-for-profit. One article goes on to say:

> Without adequate supervision or transparency, the not-for-profit sector is a ticking time bomb. It would take just two or three scandals to harm all the good that the other charities are doing. (*Business Review Weekly*, 24 March 2005)

The review also highlights the fact that a significant part of the negative press appears in business media. This is a reflection of the concerns of some in the business community that the profitability of their own businesses will be damaged with the entry of not-for-profit

Table 7.1 Media articles relating to not-for-profit business venturing as reported in all major news and business publications in the United Kingdom, the United States and Australia, accessed via *Factiva* from 1/9/2003 to 30/3/2005, by theme

Theme: negative assessments	
Country	Sample headline/quote
Aust	THE $70 BILLION SACRED COW Are you sick of paying tax? Is your entrepreneurial drive being held back by over regulation? Would you like regular government assistance in expanding your business? Sizable corporate and private donations – no questions asked? Would you like to see your competition operate at a disadvantage? If you answer yes to any of these questions and see yourself as compassionate and charitable, send your application to the Australian Taxation Office (ATO) to start your own charity or religion. You will be joining more than 700,000 other like-minded organisations in a sector that turns over more than $70 billion a year (almost 10% of the country's GDP) in tax-free dollars and is the last bastion of the economy that is left largely to its own devices. *Business Review Weekly*, 24 March 2005.
USA	CHARITY, D.C. STYLE: ARE SOME NONPROFITS REALLY IN THE LOBBYING BUSINESS? For some tax-exempt organizations, the question is whether their charitable works are an end in themselves – or a means to one. KORUSEC's stated goals included working for peace on the Korean peninsula and building stronger ties between U.S. and Korean leaders. But KORUSEC strengthened Kim's own ties in Washington as well. *Time*, U.S. Edition, 28 March 2005.
USA	CHARITIES FEAR NEW LAWS WILL BE COSTLY Congress weighs tighter controls Nonprofits worry that the cost of compliance could divert money from the people they try to help. Congress is considering more stringent regulatory controls over the nonprofit sector after reported abuses by some charities, including excessive compensation for executives, inappropriate expenditures and inadequate disclosure of financial information. *Denver Post*, 25 March 2005.

Theme: negative assessments	
Country	Sample headline/quote
UK	CHARITY SHOPS THREAT TO UK BOOKSELLERS British independent booksellers are facing competition from charity shops. Many UK charities have opened specialist second-hand bookshops. Oxfam has over 70 shops in the UK and claims to be the largest retailer of second-hand books in Europe. The charity shops feel that they are providing a useful service. However, traditional booksellers feel that they are providing unfair competition as they do not pay for stock, have volunteers as staff, and pay lower business taxes. *Inside Retailing*, 21 March 2005,
UK	DO CHARITY SHOPS HAVE AN UNFAIR ADVANTAGE OVER SMALL TRADERS? The Federation of Small Businesses complained last week that regulators take a soft approach to the UK's 6,500 charity shops, which get relief on business rates. Does this amount to unfair competition on the high street? *Third Sector*, 20 April 2005.
UK	SAVE US FROM THE CHARITY SHOPS, SAY FIRMS; NEW BREED 'TOO AGGRESSIVE' Charity shops are gaining an unfair advantage over small retailers and should lose their preferential tax breaks, a business pressure group said yesterday. The Forum of Private Business (FPB) claimed that its members faced heightened competition from charities, which ran their shops as professional businesses rather than volunteer-led organisations. *The Herald*, 8 March 2006.
Theme: positive assessments	
Country	Sample headline/quote
UK	CHARITIES NEED TO STAY IN BUSINESS The past decade has seen dramatic changes in the way charities operate. Without losing their essential philanthropic purpose, working practices now closely parallel and sometimes even lead the commercial sector. *Daily Mail*, 29 March 2004.
USA	"BUSINESS PLAN" COMPETITION FOR CHARITIES The Pittsburgh Social Venture Accelerator ... will launch a "business plan" competition in August for charities that want to augment traditional sources of funding ... with their own money-making ventures. *Pittsburgh Post-Gazette*, 10 July 2003.

Theme: positive assessments	
Country	Sample headline/quote
UK	CHARITIES NEED TO BECOME MORE BUSINESS-LIKE Major charities, including the RNID and National Trust, are now streamlining their boards to achieve better, faster decisions through business-like models, while ensuring broader representation and responsibility to service users and beneficiaries through democratic accountability. The burgeoning field of social enterprise – trading for social purposes – now aims to replicate business successes through franchising, while looking on failures as means to innovation and reinvigoration. *The Times*, 29 June 2004.
UK	RNID MOST INNOVATIVE NOT-FOR-PROFIT The Royal National Institute for the Deaf was last night named most innovative charity by the top voluntary organisations, in a poll promoting the growing role of not-for profit organisations in Britain. The RNID's £125m contract to modernise hospital audiology services ... puts it at the forefront of charities delivering public services. *Financial Times*, 23 November 2004.
Aust	CHARITY BUSINESS CASES Philanthropy brokers are linking donors with charities – and insisting on better accounting of where the dollars go and what they achieve. Old-style, hand-out philanthropy is dying. A new generation of donors is demanding accountability, performance measurement, analysis of social returns on their investments, formal business plans and sustainable business models. In response, many charities are becoming more business-like but some are reluctant to change their old ways. *Business Review Weekly*, 20 May 2004.

SOURCE The authors

business ventures – ventures they perceive to be operating at an advantage due to their eligibility for some government subsidies and their tax-exempt status. Despite being principally confined to the business media, these attitudes have the potential to inflate negative

sentiment towards not-for-profits that engage in business activity more generally and, if ignored, could become a source of increased pressure on policy makers to revisit tax exemption arrangements. For this reason, we would argue, it is important that not-for-profits develop strategies to effectively respond to (and refute) such negative press.

Managing the risks of business venturing

The promise of increased revenue and the potential benefits to management practice will continue to entice not-for-profits into the market. However, in embarking on commercial activity, not-for-profits need to tread carefully. Externally, not-for-profits need to defend their position by becoming active interlocutors in debates about not-for-profit business venturing, in particular by making an informed case for its benefits. Internally, not-for-profits must be attuned to certain risks associated with commercialisation, in particular mission drift and the potential for a backlash from donors and the wider community.

A significant body of research has found that not-for-profit market participation does not inevitably tilt the playing field. Rose-Ackerman (1990) argues that as industry is competitive, and investors in for-profit enterprises anticipate the possible entry of exempt organisations into the market, those investors will earn the market return despite the presence of tax-exempt competitors. According to analysis by Weisbrod (1988), a not-for-profit organisation is unlikely to underprice its for-profit competitor in a bid to gain market share – that in effect non-profits are price takers not price makers. Australia's Industry Commission report supported this finding, saying:

> the income tax exemption does not compromise competitive neutrality between organisations. All organisations which, regardless of their taxation status, aim to maximise their surplus (profit) are unaffected in their business decisions by their tax or tax exempt status. (Industry Commission 1995: K5)

Finally, both Liu and Weinberg (2003) and Steuerle (1988) argue that an income tax exemption is not an input subsidy and is thus no more 'unfair' to a taxed competitor than are the progressive income tax rates on individuals who conduct business activities in sole proprietorships or through partnerships or limited liability companies.

Some of the measures that can assuage public concerns as well as manage risk are outlined below:

- *Conduct tailored risk assessment analysis.* Commercial activity undertaken by not-for-profits will not engender the same reaction from all stakeholders. Research into how different categories of stakeholders might respond to entrepreneurial activity would allow not-for-profits to respond in a more targeted and situation-specific way. Methodologies available include surveys and focus groups with key stakeholders.
- *Manage the brand (and the brand life cycle).* This is principally a marketing and communication exercise that seeks to manage the image and identity of an organisation in ways that align with stakeholders, especially donors, who desire the maintenance of the not-for-profit's humanitarian focus. Strategic use of the media will be crucial in this area.
- *Know your business partner.* In terms of developing partnerships with business, not-for-profits must increase their capacity to accurately assess risk through 'due diligence' so as to avoid associating with business corporations that could damage the not-for-profit's reputation.
- *Use funds for what they are intended for.* Some organisational resources must be protected from high-risk investments – a variation of the Chinese Walls principle. It will be important for not-for-profits to manage access to some assets and funds to avoid exploitation of special resources such as charitable funds and volunteer effort.
- *Financial performance is not the sole criterion of success.* Not-for-profits should equip themselves to manage cultural conflicts that may arise between profit-oriented and mission-oriented groups within the organisation. The lack of common practice around social impact assessment and reporting means that many commercial ventures are judged purely in financial terms, even if social goals are their primary motivation. It will be crucial for not-for-profits to develop ways to ensure that social outcomes (not just profitability) become the key measure of performance.
- *Strike a balance.* It will be particularly important to strike a strategic balance between profitable and mission-contributing ventures and activities. The not-for-profit organisation must properly manage its portfolio within acceptable bounds of risk tolerance.
- *Aim for transparency and accountability.* Transparency and accountability will be crucial to engendering trust among multiple stakeholders. Unlike businesses, these include stockholders and customers, as well as donors, board members, regulators, paying and non-paying customers, institutional funders, volunteers and others involved in the particular venture or the organisation at large.

These measures need to be integrated in not-for-profits' overall risk management strategy – a strategy Bryce defines as the assessment of 'contingent costs or liabilities that are due to the probability that an event that could be costly could occur, with profound consequences to the organisation' (1992: 3). With a clear focus on mission, and a well thought out strategy of how to manage the risks of commercialisation, not-for-profits are in a much stronger position to simultaneously reap the rewards associated with business venturing and maintain organisational integrity, values and reputation within the community. The ultimate outcome will be an increase in their effectiveness as agents of social benefit.

Conclusion

Business venturing has created new opportunities and new challenges for the not-for-profit sector. It has the potential to bring innovation to not-for-profit management and operations, and to provide an opportunity for not-for-profits to augment scarce resources. This latter benefit is particularly attractive at a time when demand for not-for-profit services far outstrips resources.

It is important, however, that not-for-profits understand the meaning of and contestation surrounding business venturing, if they are to apply it critically and reflectively and participate in debates about its place in not-for-profit management. For example, not-for-profits need to be aware of the risks of being seen as more of a business than a social agency, and as a threat to private operations competing in the same markets.

To explore the new possibilities of commercialisation, and to avoid its perils, not-for-profits need to craft their strategies carefully. In considering business ventures, not-for-profits should pay attention to the organisation's mission, its capability, the financial impact, the legal and taxation situation, the implications for community relations, and professional and ethical considerations. If public expectations are not managed, social enterprise ventures risk discrediting the whole sector.

References

ABS – *see* Australian Bureau of Statistics.

Access Economics (2001) The Strong Case for a Clearer, Activities-Based, Definition of Charities and Related Organisations, Submission to The Inquiry into the Definition of Charities and Related Organisations Commissioned by Kellogg (AUST) Pty Ltd and prepared by Access Economics, Canberra, January.

The Allen Consulting Group (2001) Issues in the Definition of Charities and Related Organisations in the Health Care Sector, Submission to the Inquiry into the Definition of Charities and Related Organisations, <http://www.allenconsult.com.au/publications/view.php?id=4>.

ATO – *see* Australian Taxation Office.

Australian Bureau of Statistics (2002) *Australian National Accounts: Non-Profit Institutions Satellite Account, 1999–2000*, Cat. no. 5256.0, ABS, Canberra.

Australian Taxation Office (2005a) *Endorsement as an Income Tax Exempt Charity – Income Tax Guide for Non-Profit Organisations*, ATO, Canberra, <http://www.ato.gov.au/print.asp?doc=/content/34308.htm&page=1>.

—— (2005b) *Taxation Ruling TR 2005/21 Income Tax and Fringe Benefits Tax: Charities*, ATO, Canberra, <http://law.ato.gov.au/pdf/tr05-021.pdf>.

—— (2006a) *Non-Profit News Service No. 0157 – Federal Court Decision in Word Investments Ltd*, ATO, Canberra, <http://ato.gov.au/nonprofit/content.asp?doc=/content/81165.htm>.

—— (2006b) *Non-Profit News Service No. 0158 – Tax Office is Appealing the Decision in Word Investments*, ATO, Canberra, <http://www.ato.gov.au/nonprofit/content.asp?doc=/content/81517.htm&pc=001/004/020/008&mnu=36157&mfp=001/004&st=&cy=1>.

Bennett, J & Dilorenzo, J (1989) *Unfair Competition: The Profits of Nonprofits*, Hamilton Press, Lanham MD.

Boschee, J (2001) Eight basic principles for nonprofit entrepreneurs, *Nonprofit World*, 19(4): 15–18.

Borgaza, C & Defourny, J (eds.) (2001) *The Emergence of Social Enterprise*, Routledge, London.

Brody, E & Cordes, J (1999) *The Unrelated Business Income Tax: All bark and no bite?*, Emerging issues in philanthropy seminar series, Urban Institute Center on Nonprofits and Philanthropy, Washington DC, in association with the Harvard University Hauser Center for Nonprofit Organizations, Cambridge MA, <http://www.urban.org/publications/310257.html>.

Bridgespan Group (2005) Knowledge letter, *Strategies for Social Impact*, Winter 2005, Bridgespan Group, introduction by Nan Stone, <http://knowledge.bridgespangroup.org/knowledgeletters/winter2005/#perspective1>.

Bryce, H (1992) *Financial and Strategic Management for Nonprofit Organizations*, 2nd edition, Prentice Hall, Englewood Cliffs NJ.

Charity Commission for England and Wales (2007) CC35 – Trustees, trading and tax: How charities may lawfully trade (April 2007), <http://www.charity-commission.gov.uk/publications/cc35.asp>.

Charity Finance (2002) *Charity Shops Survey*, Plaza Publishing, London.

Commissioner of Taxation v Word Investments Ltd [2006] FCA 1414 (3 November 2006), <http://www.austlii.edu.au/au/cases/cth/federal_ct/2006/1414.html>.

Department of the Treasury (2001) *Report of the Inquiry into the Definition of Charities and Related Organisations: June 2001*, Charities Definition Inquiry, Department of the Treasury, Canberra, <http://www.cdi.gov.au/html/report.htm>.

Chetkovich, C & Frumkin, P (2003) Balancing margin and mission: Nonprofit competition in charitable versus fee-based programs, *Administration and Society*, 35(5): 564–96.

Dalton, B & Casey, J (2006) Innovation or ill-gotten gains? Interpretations of nonprofit business venturing in Australia, the United Kingdom and the United States, Paper presented at the Australia and New Zealand Third Sector Research Eighth Biennial Conference, *Navigating New Waters*, 26–28 November, Adelaide.

Deakin, N & Walsh, K (1996) The enabling state: The role of markets and contracts, *Public Administration*, 74(1): 33–48.

Dees, JG (1998) Enterprising non-profits: What do you do when traditional sources of funding fall short?, *Harvard Business Review*, January/February: 5–15.

—— (2001) *The Meaning of "Social Entrepreneurship"*, Center for the Advancement of Social Entrepreneurship website, Fuqua School of Business, Duke University, Durhum NC, <http://www.fuqua.duke.edu/centers/case/documents/dees_SE.pdf>.

Dees, JG & Anderson, B (2003) Sector-bending: Blurring lines between nonprofit and for-profit, *Society*, 40(4): 16–27.

Digby, A (1978) *Pauper Palaces*, Routledge & Kegan Paul Ltd, London.

Emerson, J & Twersky, F (1996) *New Social Entrepreneurs: The success, challenge and lessons of nonprofit, enterprise creation*, Roberts Foundation, San Francisco.
Federation of Small Businesses (1994) *Trading in a Jungle of Unfair Competition – Policy Report*, Federation of Small Businesses, London.
Forum of Private Business (2006) Charity shops gaining unfair advantage over small businesses, *FPB News*, 7 March, Forum of Private Business, Cheshire, <http://www.fpb.org/news/1124>.
Foster, W & Bradach, J (2005) Should nonprofits seek profits?, *Harvard Business Review*, February: 92–100.
Fremont-Smith, MR & Kosaras, A (2003) *Wrongdoing by Officers and Directors of Charities: A survey of press reports 1995–2002*, Hauser Centre for Nonprofit Organizations, Working Paper No. 20, Kennedy School of Government, Harvard University, Cambridge MA.
Frumkin, P (2003) Inside venture philanthropy, *Society*, 40(4): 7–15.
Gamson, W (1988) Political discourse and collective action, in B Klandermans, H Kriesei, and S Tarrow (eds) *From Structure to Action: Comparing movement participation across cultures*, International Social Movement Research, Volume 1, JAI Press, Greenwich CT.
Gomes, GM & Owens, JM (1988) Commercial nonprofits, untaxed entrepreneurialism, and 'unfair competition', *Journal of Small Business Management*, 26(2): 8–16.
Grønbjerg, K & Paarlberg, L (2002) Extent and nature of overlap between listings of IRS tax-exempt registration and nonprofit incorporation – the case of Indiana, *Nonprofit and Voluntary Sector Quarterly*, 31(4): 565–94.
Gunn, C (2004) *Third-Sector Development: Making up for the market*, ILR Press, London, and Cornell University Press, Ithaca NY.
Hines, J (2000) *Nonprofit Business Activity and the Unrelated Business Income Tax*, National Bureau of Economic Research Working Paper 6820 (November), Cambridge MA.
IHRSA – *see* International Health, Racquet and Sportsclub Association.
Industry Commission (1995) *Charitable Organisations in Australia*, Inquiry Report No. 45, 16 June, Australian Government Publishing Service, Melbourne.
International Health, Racquet and Sportsclub Association (2003) *Fair Competition Annual Report 2003*, IHRSA, Boston MA, <http://download.ihrsa.org/gr/faircomp.pdf>.
James, E (1998) Commercialism among nonprofits: Objectives, opportunities, and constraints, in B Weisbrod (ed.) *To Profit or Not To Profit: The commercial transformation of the nonprofit sector*, Cambridge University Press, New York.
James, E (2003) Commercialism and the mission of nonprofits, *Society* 40(4): 29–35.
Katz, M (1986) *In the Shadow of the Poorhouse: A social history of welfare in America*, Basic Books, New York.
Kendall, J (2003) *The Voluntary Sector: Comparative perspectives in the UK*, Routledge, London.
Kendall, J & Almond, S (1999) Chapter 9: United Kingdom, in L Salamon, HK Anheier, R List, S Toepler, SW Sokolowski & Associates (eds) *Global Civil Society: Dimensions of the nonprofit sector*, Johns Hopkins Center for Civil Society Studies, Baltimore MD, 179–99.
Kenny, S (2002) Tensions and dilemmas in community development: New discourses, new Trojans?, *Community Development Journal*, 37(4): 316–26.
Liu, Y & Weinberg, CB (2004) Are nonprofits unfair competitors for business: An analytical approach, *Journal of Public Policy & Marketing* 23(1): 65–79.

Lyons, M (ed.) (1997) Contracting for Care, *Third Sector Review Special Issue*, vol. 3.
Lyons, M (2001) *Third Sector: The contribution of nonprofit and cooperative enterprises in Australia*, Allen & Unwin, Sydney.
—— (2002) What's new about social enterprise?, Paper presented at *Doing Well*, the Australia and New Zealand Third Sector Research Sixth Biennial Conference, 27–29 November, Auckland.
Lyons, M, Hocking, S, Hems, L, & Salamon, LM (1999) Chapter 10: Australia, in L Salamon, HK Anheier, R List, S Toepler, SW Sokolowski & Associates (eds) *Global Civil Society: Dimensions of the nonprofit sector*, Johns Hopkins Center for Civil Society Studies, Baltimore MD, 203–17.
May, T (1997) *The Victorian Workhouse*, Shire Publications Ltd, Buckinghamshire.
Morales, Jr HR (1997) Earning income through trade and exchange, in LM Fox and SB Schearer (eds) *Sustaining Civil Society: Strategies for resource mobilization*, CIVICUS, Washington DC, 21–44.
Nowland-Foreman, G (1998) Purchase-of-service contracting, voluntary organizations and civil society: Dissecting the goose that lays the golden eggs?, *American Behavioral Scientist*, 42(1): 108–23.
Paddison, A (2000) Charity shops on the high street: Complementarity or unwanted neighbour?, *International Journal of Nonprofit and Voluntary Sector Marketing*, 5(2): 161–72.
Parsons, E (2002) Charity retail: Past, present and future, *International Journal of Retail and Distribution Management*, 30(12): 586–94.
Reis, T & Clohesy, S (2001) Unleashing new resources and entrepreneurship for the common good: A philanthropic renaissance, *New Directions for Philanthropic Fundraising*, 32: 109–44.
Riley, Margaret (1997) Exempt organization business income tax returns: Highlights and an analysis of exempt and nonexempt finances, 1993, *IRS Statistics of Income Bulletin* 16 (spring): 75–98.
Rose-Ackerman, S (1990) Competition between non-profits and for-profits: Entry and growth, *Voluntas*, 1(1): 13–25.
Ryan, WP (1999) The new landscape for non-profits, *Harvard Business Review*, January–February, 77(1): 127–36.
Salamon, L (ed.) (2002) *The State of Nonprofit America*, The Brookings Institution Press, Washington DC.
Salamon, LM, Anheier, HK, List, R, Toepler, S, Sokolowski, SW & Associates (1999) *Global Civil Society: Dimensions of the nonprofit sector*, Johns Hopkins Center for Civil Society Studies, Baltimore MD.
Sansing, R (1998) The unrelated business income tax, cost allocation, and productive efficiency, *National Tax Journal*, 51(2): 291–302.
Scott, S (2003) Investigation and comparison of the taxation treatment of income derived from commercial activities carried on by non-profit organisations in Australia, United States and United Kingdom, Honours Dissertation, Queensland University of Technology, Brisbane.
Simons, R (2000) *Social Enterprise: An opportunity to harness capacities*, Briefing Paper No. 7, The Smith Family, Sydney.
Smith Family (2005) *The Smith Family Commercial Enterprise*, The Smith Family, Sydney, <http://www.smithfamily.com.au/index.cfm?pid=2540&pageid=2540>.
Sokolowski, SW & Salamon, LM (1999) Chapter 13: United States, in L Salamon,

HK Anheier, R List, S Toepler, SW Sokolowski & Associates (eds) *Global Civil Society: Dimensions of the nonprofit sector*, Johns Hopkins Center for Civil Society Studies, Baltimore MD, 261–81.
Steinberg, R (1987) Nonprofit organizations and the market, in WW Powell (ed.) *The Nonprofit Sector: A research handbook*, Yale University Press, New Haven CT, 118–38.
Steuerle, CE (1988) The issue of unfair competition, Working Paper, Center for the Study of Philanthropy and Voluntarism, Institute of Policy Sciences and Public Affairs, Duke University (February), Durham NC.
Thompson, J (2002) The world of the social entrepreneur, *International Journal of Public Sector Management*, 15(5): 412–31.
The Prime Minister's Strategy Unit (2002) *Private Action, Public Benefit: A review of charities and the wider not-for-profit sector*, Strategy Unit Report (September), <http://www.cabinetoffice.gov.uk/upload/assets/www.cabinetoffice.gov.uk/strategy/strat-data.pdf>.
US Department of the Treasury, Internal Revenue Service (2000) Selected returns and forms filed or to be filed by type during specified calendar years 1975–2000, *Statistics of Income Bulletin*, Summer.
Weisbrod, B (1988) *The Nonprofit Economy*, Harvard University Press, Cambridge MA.

Notes

1 The authors would like to thank the editor for her valuable comments. An earlier version of this chapter was presented at the Australia and New Zealand Third Sector Research Eighth Biennial Conference, *Navigating New Waters*, in November 2006 in Adelaide (Dalton & Casey 2006).
2 In Australia not-for-profits are not required to pay tax on the profits made from engaging in commercial activity, a situation that is in stark contrast to international practice. In the United States, for example, the unrelated business income tax (UBIT) taxes profits of unrelated business activities carried on by not-for-profits and denies exemption to 'feeder organisations' operated for the primary purpose of carrying on a trade or business to pass profits to a not-for-profit (Sansing 1998). United Kingdom charity law only permits not-for-profits to trade through separate non-charitable (that is, taxable) entities (Charity Commission for England and Wales 2007). However, a combination of under-reporting and provisions for donating business profits to not-for-profit activities mean that, in effect, not-for-profits in the United States and the United Kingdom pay negligible business taxes.

SECTION 3

STRATEGIC ISSUES FOR THE not-for-profit SECTOR

EDITED BY JO BARRAKET

UNSW PRESS