
Backgrounder

The Emerging Sector: In Search of a Framework

Bookshelves are loaded with studies of the public sector and the market sector. The time has come to pay some attention to the nonprofit sector, for several reasons:

- Governments are shifting the delivery of programs to charitable organizations.
- Social needs are rising in response to dramatic changes in the world of work, in family structure and in the role of government.
- Political analysts are beginning to focus attention on the importance of civil society.

What are the defining characteristics of this emerging sector? How do nonprofits differ from for-profit and public sector organizations? How large is Canada's nonprofit sector? Do the major government policies directed at the sector foster healthy nonprofits? These are among the major questions addressed at a CPRN Roundtable held in January 1997.

This study reports on the discussions at that Roundtable, where 35 people who know the sector gathered to review the findings of three research papers commissioned by CPRN on the size and scope of the nonprofit sector, organizational and supervisory law and the tax treatment of nonprofits. The study also includes three essays: two on the definition of the sector, and a third, which positions the Roundtable deliberations in the context of recent public policy discussions and the growing academic literature on the nonprofit sector.

What Are Nonprofits?

On the definition of the sector, Paul Reed pointed to the absence of self-serving behaviour by participants in nonprofit activities as the sector's distinguishing characteristic. Arthur Drache, by contrast, emphasized the tax definition: that, unlike for-profit enterprises, nonprofits never distribute their surplus. Jacquelyn Thayer Scott described how different labels (i.e., nonprofit, not-for-profit, voluntary, third, independent sector) have their roots in different academic approaches to this sector.

The discussion also made it clear, however, that there is no universally correct way to impose order on the diversity that exists within the sector. The boundaries of the nonprofit sector are likely to vary depending on the issues under discussion. Much research remains to be done to identify

common characteristics, to develop a framework for assembling data on the sector, and to take account of the evolution of these organizations over time.

What Is the Role of Nonprofits?

Ron Hirshhorn, in his lead essay, says that while existing theories are incomplete, the literature shows that nonprofits may have a comparative advantage over for-profits in certain situations where clients want the assurance of trustworthy behaviour. Nonprofits may also help address certain needs that are not adequately addressed by governments. In addition, nonprofits often foster individual and group activities that have important value in their own right they promote giving, voluntarism, association and citizen engagement, for example. These activities are now recognized as providing the foundation for the social capital that is essential to the healthy functioning of both society and economy.

The Dimensions of the Nonprofit Sector and the Nature and Extent of Civic Activity

Kathleen Day and Rose Anne Devlin summarize the findings from their extensive review of available data sources, and provide a useful list of suggestions for ways to improve the quality of the data and thus to improve our understanding of the sector. The findings include the following:

- In 1994, 67,606 charities received revenues somewhat in excess of \$60 billion.
- The total size of the sector, including nonprofits that are not registered as charities, is much larger, but there are no comprehensive counts of their size or number.
- The number of charitable organizations has been increasing at a significant pace.

Charitable nonprofits come in a range of sizes, with different organizational and legal structures, and provide a wide variety of services to different groups of individuals. Roughly speaking, the sector can be divided into three segments, as shown in Figure 1:

- Hospitals and teaching institutions account for a small number of all charitable organizations, but a major share of total remuneration paid to employees in the charitable sector. Most of their revenue comes from governments.
- Religious organizations account for a large proportion of all organizations, but are far smaller on average than other charities. Religious organizations depend heavily on donations and volunteer support.
- Other charities include a diverse array of social service and community service organizations. These 34,700 organizations had a payroll of almost \$8 billion in 1994. This includes some large, national organizations, and many very small units. Almost half of their revenue comes from governments, while 13 percent of their receipts are from individual and corporate donations.

Table 1**Three Categories of Nonprofits, 1994 Snapshot**

	Hospitals and teaching institutions	Organized religion	Other charities	Total
Number of organizations	3,613	29,308	34,685	67,606
Percent share	5.3	43.4	51.3	100.0
Worker remuneration (millions of dollars)	19,678	1,528	7,814	29,020
Percent share	67.8	5.3	26.9	100.0
Remuneration per organization (thousands of dollars)	5,446	52.1	225.3	
Percent of revenue from government	72.0	5.0	47.1	
Percent of revenue from donations ¹	1.9	57.4	12.7	
Volunteer hours, percent share of total reported ²	4.1	44.7	51.2	100.0

1 Includes gifts for which receipts were not issued. Excludes gifts from other charities.

2 Reporting of volunteer hours is not compulsory. These data are based on the 37 percent of filers that reported volunteer hours.

Source: Based on data in Kathleen M. Day and Rose Anne Devlin, *The Canadian Nonprofit Sector*, CPRN, 1997.

Government is the most important stakeholder in charities, accounting for 60 percent of all revenues. While donations account for a modest share of all revenues, individuals also make an important contribution through their volunteer labor, and corporations provide in-kind gifts of time and supplies. Indeed, the research points both to the dynamism of the nonprofit sector and the vibrancy of the volunteer community in Canada. And the European Values Study, which surveyed voluntary involvement during 1991 in 16 countries, found that the volunteer rate in Canada is robust just slightly below the 47 percent rate recorded for the United States, and above that of all other surveyed countries. Studies show that the rate of volunteering by Canadians varies with age, education and religious practice. Higher levels of activity occur among older, better educated people who attend church or synagogue.

While the data available on voluntary activity and on the sector are weak, there is no question that nonprofits are an important dimension of Canadian society. The next two papers commissioned by

CPRN suggest that governments need to strengthen the framework laws in order to promote a strong and responsive sector.

Organizational and Supervisory Law

Organizational laws attempt to set out a framework for the organization and conduct of nonprofit activities. Their general purpose is to make it easier and less costly for individuals to work out the agreements that are needed to establish a formal charity or nonprofit. Hirshhorn and Stevens find that:

- There are some unnecessary and undesirable restrictions in current legislation (e.g., borrowing and investment restrictions) that are at odds with this general purpose;
- The enabling function of the law could also be enhanced by creating draft bylaws and other optional provisions that offer guidance to nonprofits; and
- The law should be amended to incorporate codified standards that would clarify the “duty of care” and the “duty of loyalty” of directors of charitable organizations.

Participants at the Roundtable recognized the critical role of public trust to the effective operation of nonprofits, but they had different perspectives on how this can best be achieved. While some saw the answer partly in the reform of existing federal and provincial supervisory laws, others believed that the sector itself should develop codes of conduct and/or other forms of self-regulation.

The Tax Treatment of Charities

The study of the tax treatment of charities by Scharf et al. finds that Canada’s approach is in line with the best practice in other developed countries. The recent budget addressed one significant anomaly in the system by eliminating differences in the treatment of charitable donations to Crown foundations and other charities. However, there are some issues that merit closer review. For example, monetary gifts are treated differently from gifts of appreciated property in the form of publicly traded securities (which benefited from provisions in the last budget). Also, GST rebates for charities are less generous than those for universities and hospitals.

Some participants also expressed concern that Revenue Canada may be applying an overly restrictive definition of charitable purposes in determining an organization’s eligibility for registration. It was argued that the current definition, based on case law, excludes important minority communities and cultures.

Conclusions

At the moment, Canadians have barely enough information to create an X-ray of the bare bones of the nonprofit sector. What is needed for the future is an MRI, which will portray the soft tissues that tie the bones together and give the sector muscle. To gain that in-depth understanding of the sector, all the main stakeholders will have to invest:

- Governments need to invest in reforms to organizational law, the collection of better data, and research on the definition and classification of the sector.
- Corporate donors (and foundations) need to be more demanding with respect to the accountability of the sector. They should develop best practices for partnership with the

sector and standards of disclosure to ensure that the sector is accountable for the resources it uses.

- The sector itself needs to take on more responsibility for its own future, whether that is regulation, standard setting, governance or disclosure.
- Social science researchers should devote more energy to data development, classification, and the many unexplored facets of this dynamic emerging sector.

While the Roundtable was not aimed at developing a consensus, participants agreed that Canadians need to develop a framework for understanding the kind of nonprofit sector that can best contribute to making Canada a more just, prosperous, and caring society.

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