CHAPTER ONE

The Age of Nonprofits

America loves nonprofits. They represent what is best about our country: generosity, compassion, vision, and the eternal optimism that we can resolve our most serious problems. Unlike the for-profit sector that employs most Americans, nonprofits have a higher calling, a more noble purpose. Each week millions of people volunteer their time to nonprofits, reading to the blind, raising money for the Cancer Society, mentoring adolescents from troubled backgrounds, or doing countless other good deeds. Nonprofits show loving kindness to the most vulnerable and the most wretched in society. Nonprofits keep homeless alcoholics from freezing to death on cold winter nights and make sure that people dying of AIDS can spend their last days in the familiar surroundings of their home. We love nonprofits because they embody the caring, charitable side of us.

Everyday we come across nonprofits that we admire, like New York's City Harvest, which donates food to pantries and shelters; or Chicago's Bottomless Closet, which provides professional clothing and interview training for women trying to escape welfare; or the Codman Square Health Center in the Dorchester section of Boston, which not only provides health care to the poor but also offers free computers to parents and their children who take a ten-week training course together; or the Genesis Women's Shelter in Dallas, where women and their children arrive in the middle of the night with just the clothes on their back; or Beyond Shelter in Los Angeles, which finds housing for the homeless and provides the social services that, it is hoped, will keep its clients from becoming homeless again; or the Transitional Work Corporation in Philadelphia, which takes the hard-core unemployed and gives them part-time work and support from a mentor while training them for something better; or Newark's New Community Corporation, which operates 3,000 units of low-income housing as well as day care centers, a nursing home, and a supermarket; or Movers, a faith-based nonprofit trying to combat AIDS in the poor Liberty City section of Miami; or Somerville-Cambridge Elder Services, which provides Meals-on-Wheels, homemaker assistance, personal care, and other services that enable frail elderly to remain in their apartments and out of nursing homes. These organizations are a mere handful of the hundreds of thousands of nonprofits that do similar work.

Besides these kinds of health care and social service providers are the nonprofits that enrich our lives with beauty and art. The Seattle Symphony, the San Francisco Ballet, and the Lyric Opera of Kansas City add to the vitality and appeal of those cities. The Friends of the Mill Valley Public Library, a tiny organization in a small California town, earns our gratitude too. Even in this day and age of the Internet, libraries are nothing less than the repositories of our civilization, and members are passionate about their town library. Many nonprofits, like the Friends of the Mill Valley Public Library, are rather small, run out of people's homes, and depend entirely on volunteers. Neighborhood-based nonprofits like parent-teacher associations (PTAs) build community within our communities. At the other end of the spectrum are nonprofit behemoths like the United Way, the Salvation Army, Catholic Charities, and the Red Cross. If these organizations did not exist, would the government step in and provide the same services? Maybe. Or perhaps the government would offer those services but not perform them as well. It is hard to answer the question because it is hard to imagine America without these public charities.

Americans' devotion to nonprofits is reflected in their generosity. In 1998, 109 million Americans volunteered for nonprofits, approximately 56 percent of the adult population. On average they volunteered 3.5 hours per week, representing an annual aggregate of $226 billion in donated time.[1] In actual dollars contributed, Americans' commitment to nonprofits is equally impressive. Total giving from all sources in 2001 was $212 billion. Approximately 75 percent of the donated money came from individuals.[2] Giving to nonprofits rose sharply through the 1990s, though the subsequent downturn in the stock market tempered the rate of increases.[3]

As essential as nonprofits are today, current trends suggest that they are going to grow even more significant in the years to come. Increasingly, scholars and pundits have drawn our attention to the importance of civil society, community, and civic engagement in American life.[4] When discussion turns to improvements, to ways of enhancing a sense of community, nonprofits are inevitably at the heart of visions of what the good society should look like. Building a better society means working together to solve problems. When we work with others in the community, we usually do so in organizations—nonprofit organizations. Whatever the problem, nonprofits seem to be part of the solution.

Government: Tough Love

America's love affair with nonprofits includes the affections of its government. Although not all nonprofits carry out functions of critical importance to government, a surprising number of them deliver services that ordinary Americans depend on. Indeed, the modern welfare state has largely been subcontracted to nonprofits. Appropriately, scholars emphasize the partnership between the agencies of government and nonprofits.[5] In many ways it is an ideal relationship. Government provides a significant portion of the financial resources but by subcontracting the actual administration of programs to nonprofits, it is able to take advantage of the dedication, imagination, and private fund-raising capacity of these public-spirited organizations.

Consider, for example, the Idaho Youth Ranch. Begun in 1952 with a lease of four square miles of government land from President Harry Truman, the nonprofit has grown over time and now runs several residential facilities in the state. The initial site, located in southern Idaho, is a working ranch, and the troubled youth who are sent there not only go to school but also work with the staff raising thoroughbred horses. The young men and women at the Youth Ranch take part in all aspects of the horse program, including foaling, imprinting, and halter breaking. They take classes on breeding and horse care, show horses to prospective customers, and attend sales. Those youth sent by either corrections or welfare bureaucracies are paid for under a contract with the state.[6]

Alternatively, the state of Idaho could run its own home for troubled youth. It is a virtual certainty that the state would not build and run a horse farm as a residential facility for children with serious behavioral problems. Most likely, the state government would construct something modest, in deference to taxpayers' concerns about the cost of government. The nonprofit Idaho Youth Ranch, with its tax-deductible status, raises a significant amount of private money to supplement the contractual payments it gets from government. Donors to the Youth Ranch give with the certain knowledge that they will get part of their charitable contributions back from the federal government when they file their tax returns. In contrast, a state facility for troubled youth would receive no private support, and taxpayers would have to fund 100 percent of its budget.

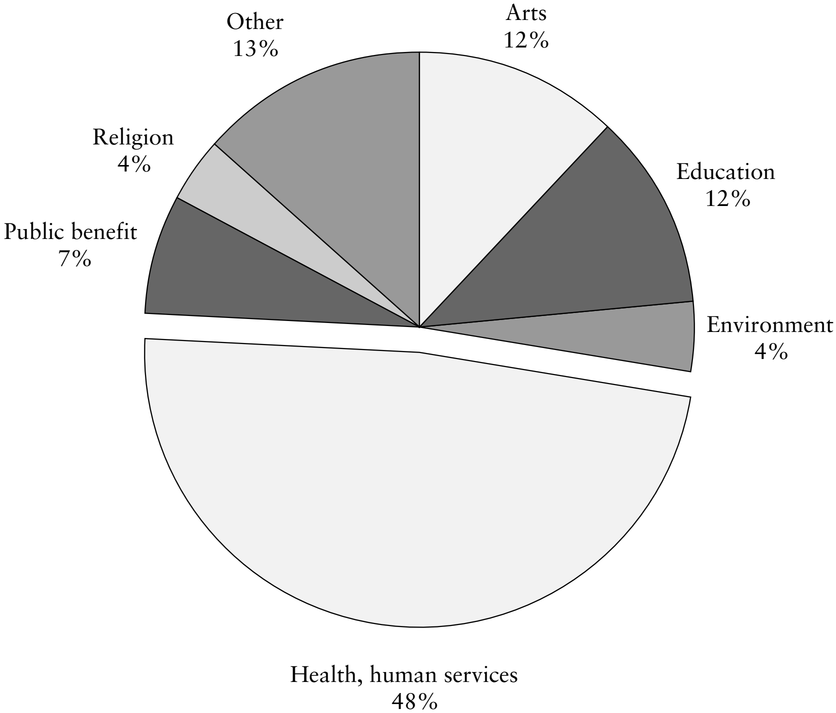
The financial incentive for contributions to nonprofits comes at a price to those organizations. In exchange for tax deductibility, nonprofits must accept a serious restriction on their right to lobby legislative bodies at the federal, state, and local levels. Under the tax law governing nonprofits, lobbying is considered an unsavory and suspect activity. Although legislative advocacy is not forbidden, almost all tax-deductible nonprofits fall under a regulatory standard that restricts them from doing any "substantial" amount of lobbying. The government may love nonprofits, but when it comes to political activity it is a case of tough love.[7] Nonprofits must comply with government's restriction or risk losing the crown jewel of fund-raising: tax deductibility.

In the chapters that follow we argue that the consequence of this regulation is that it deters nonprofits' participation in public policymaking. This, in turn, harms the most vulnerable populations, who are denied effective representation in the political system. Although nonprofits serve a cross-section of all Americans, they are crucial elements in serving the hungry, sick, disabled, and frail. What nonprofits are not supposed to do is to represent their clients before legislators. Feed them, just don't lobby for better antihunger programs. Heal them, just don't try to lobby for changing the health care system. This is the essence of American law on nonprofits.

To measure the impact of tax law on political participation, a mail survey was conducted of a random sample of nonprofits from all over the United States. The survey was supplemented by interviews with the executive directors from nonprofits from around the country and by focus groups with executive directors and board members of nonprofit organizations. All the interviews and focus groups were done on a not-for-attribution basis and were conducted between the fall of 2000 and the spring of 2001. More detail on the survey and interview methods is offered in chapter 2, and the appendix offers a more complete review of the study's methodology.

This study's emphasis on nonprofits offering social services reflects their predominance in the population of all nonprofits. As figure 1-1 shows, approximately half of all nonprofits are involved in either health care

Figure 1-1. *America's Nonprofits*



Source: Authors' survey; see appendix.

Note: $N = 583$. "Religion" is religion-related nonprofits and excludes individual congregations.

(11 percent) or human services (37 percent). More accurately, these organizations are half of all charitable nonprofits, eligible to receive tax-deductible donations.[8] "Nonprofit" is an inherently ambiguous term.[9] Indeed, it is rather a misnomer because it is perfectly legal for a nonprofit to make a profit. There are restrictions on what a nonprofit can do with a profit, principally that it cannot distribute the profit to shareholders or employees, but profits are not prohibited.[10]

"Nonprofit" is also a relatively elastic term as it covers an enormous range of organizations in America.[11] Under section 501(c) of the IRS code, there are twenty-six different types of nonprofits.[12] They include nonprofit cemetery companies [section 501(c)(13)]; labor unions [sec. 501(c)(5)]; and employee-funded pension trusts [sec. 501(c)(18)]. These diverse organizations have only one thing in common: they are tax exempt. That is, they pay no taxes on income related to their exempt purposes. But when we think of nonprofits we usually do not have in mind nonprofits like the AFL-CIO (a c5) or the American Petroleum Institute (a c6). Only one type of the 501(c) nonprofits can offer donors a tax deduction for their contributions. Section 501(c)(3) encompasses those nonprofits considered to be public charities, such as religious organizations and educational institutions. It is these organizations, the c3s, that we are usually referring to when we talk about nonprofits. The same is true of this study: unless otherwise indicated, a reference to nonprofits is a reference to only those that qualify under 501c3 and thus offer donors tax deductibility for contributions.[13]

Distinguishing nonprofits is more than a bit of methodological housecleaning. The tax-deductible nonprofits, the 501c3s, have a different story to tell because their legal status as public charities gives them a unique financial structure. When in 1917 the federal government created the tax incentive for people to donate money to charities, there was little controversy because everyone is in favor of charity. Over time, however, the vast majority of organizations applying for 501c3 status from the Internal Revenue Service have not been charities in the colloquial sense of the term. They are public-spirited organizations to be sure and do work broadly supported by Americans. But the fact that half of tax-deductible nonprofits are now health or human service providers creates a public policy dilemma. The nonprofits envisioned in the original legislation creating the tax deduction—churches, charities, and educational institutions—were not seen as having much stake in public policy. That is not true of today's community health centers, multiservice centers, Community Development Corporations, job training facilities, housing collaboratives, and the like. They have an enormous stake in what government does and therein lies the problem.

Growth Sector

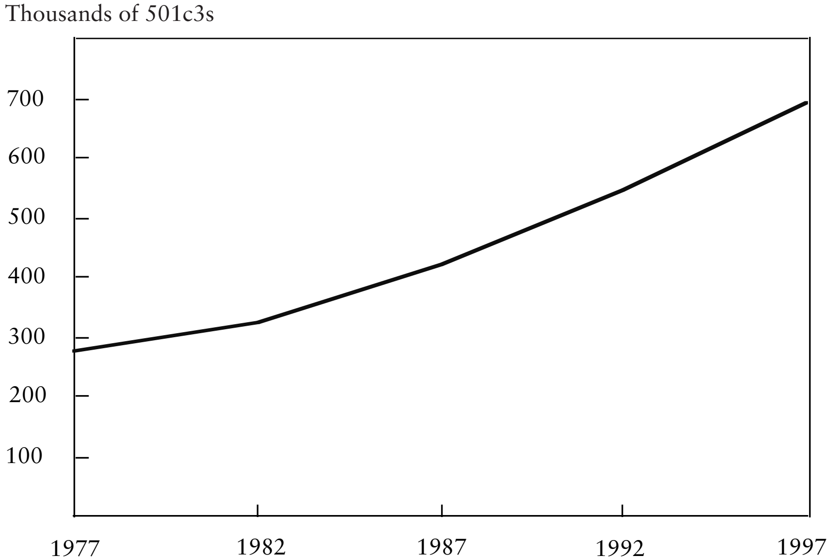
Economists offer a straightforward explanation of the rise of nonprofits in areas in which government itself directly offers services, such as health care, social services, and education. In their view, when government offers services it will aim to satisfy the demand of the median voter. (In plain English: government will offer what the typical consumer wants but nothing more extensive than that.) Economists also say that nonprofits will emerge in areas served by for-profit organizations when consumers have difficulty evaluating the quality of service and are worried that the for-profits will pursue greater earnings at the expense of quality service. For example, when a family must place a loved one in a nursing home and cannot monitor that nursing home closely because it is far away, the family might feel more comfortable utilizing a nonprofit facility. A 501c3 does not have the same profit incentive as a private sector nursing home and, presumably, there is little pressure on its managers to cut corners or keep services to a minimum.[14] Finally, of course, economists point out that nonprofits are a response to market failure, where neither government nor business steps in to provide necessary services.

Political scientists offer a different perspective for examining the growth of nonprofits. They focus on the political process that leads to agenda change. In some cases, new social problems emerge and government feels a responsibility to address them. When AIDS became an issue Congress enacted the Ryan White Act and federal agencies responded with new initiatives too.[15] For the most part, though, the nonprofit sector has grown because of increased attention to problems that have long existed, such as malnutrition, inadequate job skills, or family violence. Consequently, political scientists also look at the events and trends that raise our awareness of problems. In this vein they will emphasize the role that advocacy groups play in drawing our attention to various social problems and in lobbying legislatures, agencies, and executives to address them.[16]

These differing perspectives are not mutually exclusive. Political advocacy can cause government to begin funding a service, but then support it only to the degree it satisfies the median voter. Given that the nonprofit sector has expanded by hundreds of thousands of organizations in recent years, surely many cogent explanations could explain all or part of this population explosion. Documenting the growth, however, is relatively straightforward since the Internal Revenue Service provides population figures for 501c3s and all other types of nonprofits. Whatever the underlying reasons, the proximate cause of the rising number of nonprofits is the expansion of government's commitment to social services. The sharp rise of 501c3s is evident in figure 1-2. Between 1977 and 1997, a period of just twenty years, the number of public charities shot upward from 276,000 to 693,000. In 1998 (the last year for which figures are available), the number of 501c3s increased by another 41,000, or 5.9 percent, above the previous year. This is even more robust than the already high (5.1 percent) annual growth for the previous decade.[17]

The phenomenal growth of public charities is further evidenced by comparisons with other types of nonprofits and with all organizations in general. All major types of organizations have been growing in number—

Figure 1-2. *The Nonprofit Surge*

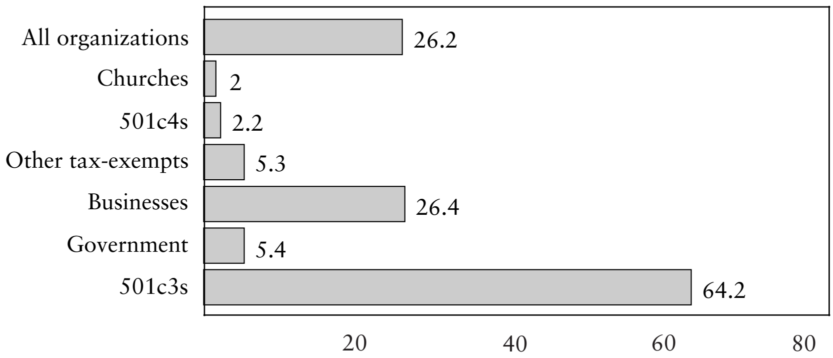


Source: Murray S. Weitzman, Nadine T. Jalandoni, Linda M. Lampkin, and Thomas H. Pollak, *The New Nonprofit Almanac and Desk Reference* (Jossey-Bass, 2002), pp. 4–5.

hardly surprising since the American population is growing, and the nation's collective wealth continues to expand. Conceivably, nonprofits could simply be growing at the general rate of growth for all organizations. Figure 1-3 shows that this is not the case. Between 1987 and 1997, all other types of nonprofits have grown only incrementally while 501c3s grew by 64 percent. Even more striking is that 501c3s have grown at about two and one-half times the rate of new businesses. Clearly, the 501c3s are not simply riding the crest of a wave of growth of all kinds of organizations.

The financial resources fueling the growth of 501c3s are imposing. Excluding health care nonprofits, total revenue for all other public charities in 1997 was $338.5 billion.[18] The nonprofit sector share of GDP is close to 7 percent, and it employs 10 percent of the work force in the United States.[19] Government is a significant source of funding and constitutes just over 20 percent of all revenues for non-health-related public charities. As a proportion of revenue, government funds have dropped slightly from 21.6 percent of 501c3s' revenues in 1977 to 20.7 in 1997.[20] When we look at human service providers, government support is far more important. As figure 1-4 demonstrates, these nonprofits depend more heavily on govern-

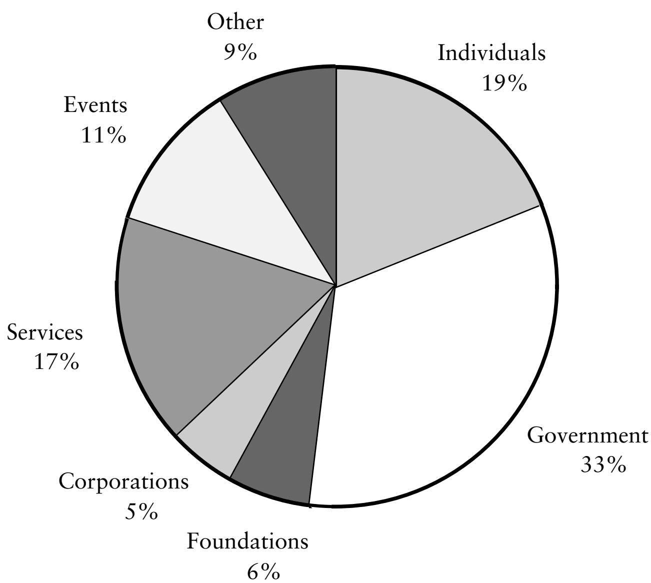
Figure 1-3. *America's Growth Sector*



Percentage change, number of organizations 1987–97

Source: Weitzman and others, *The New Nonprofit Almanac and Desk Reference*, pp. 4–12. "Other tax-exempts" are all nonprofits except 501c3s, 501c4s, and church congregations. Although churches are tax deductible, they do not file the same tax return as 501c3s and are counted separately by the Internal Revenue Service. The 501c4s are social welfare organizations but lack tax deductibility.

Figure 1-4. *Sources of Income for Human Service Providers*



Source: Authors' survey.
Note: N = 539.

ment, receiving 50 percent more than other non-health-care-related public charities. The 33 percent figure for government support for human service providers underestimates the true level of assistance since some of the income that nonprofits count under services are fees paid through government programs.

The nonprofit sector has clearly developed substantial sources of support beyond government. The 501c3 population expanded sharply during a period when there were federal budget cuts in many social service programs. The Reagan-Bush years (1981–92) were characterized by a philosophy calling for more reliance on private charity. Nonprofits were aggressive in seeking out additional private sources of revenue, and they even found ways of getting one part of government to make up for the funds cut by other parts. As Lester Salamon notes, nonprofits profited from "repackaging traditional social services as behavioral health services [to] secure government support through the rapidly expanding health programs."[21] After adjusting for inflation, revenues for nonprofits grew by 144 percent between 1977 and 1997 while the nation's economy grew at just 81.[22]

The growth of nonprofits did not just happen because funds were available and needs became more evident. This growth reflects an intellectual ferment about the substance of domestic policy and the process by which it is made. Two enormously important ideas that took hold in the second half of twentieth century America had a profound impact on the nonprofit sector. The first is the belief that welfare should be directed at fighting dependency. The government's basic approach to welfare, born in the New Deal, was to provide income maintenance to the needy. Social Security, unemployment compensation, and Aid to Dependent Children (ADC) were the cornerstones of this approach. As ADC (later AFDC, Aid to Families with Dependent Children) became a general welfare program for the poor, criticism began to mount that it did little to resolve the underlying problems that kept people impoverished. There was also growing recognition that macroeconomic policy, after years of Keynesian fine-tuning, was not enough to cure poverty either. Beginning in 1962, the federal government moved toward the rehabilitation of the poor through social services. It was a philosophy of helping people by giving them skills and (noncash) support to supplement their welfare payments.

Second, American federalism was fundamentally changed by a devolution of responsibility for domestic programs from the national to the state and local levels. Presidents Richard M. Nixon and Ronald Reagan each called for a "new federalism," and money and authority were transferred out of Washington. The primary structural change was the replacement of numerous categorical programs with block grants. The accent was on creativity. Each local government could fund programs it saw as uniquely well suited to solve the problems of the community. What wasn't attached to these grants was administrative capacity. Consequently state and local governments needed to develop a means of carrying out their new mandates. They quickly came up with a solution.

The Revolution in Welfare

There is nothing new about nonprofits providing assistance to the poor in this country. Before there was government-sponsored welfare, there were nonprofits offering assistance—charity—to the dispossessed. But change in the American welfare system changed the nonprofit sector. The transformation of welfare from a system oriented around income maintenance to a system relying on social services is at the heart of the transformation of the nonprofit sector from being largely a source of private charity to being an arm of the government.

A Turn toward Services

President John F. Kennedy was encouraged to move welfare toward a social services approach by his transition Task Force on Health and Social Security and by its chair, Wilbur Cohen, who continued to shape policy as the assistant secretary for legislation at the Department of Health, Education, and Welfare (HEW). Cohen's views reflected the current thinking of many academics and social work professionals.[23] The administration proposed legislation that was designed in the words of Abraham Ribicoff, secretary of HEW, "to wage war on dependency." In testimony before Congress he declared, "The byword of our new program is prevention—and where it is too late—rehabilitation."[24] Ribicoff then asked rhetorically, "Now how, you may ask, is this accomplished? The answer is through professional, skilled services. We believe that services represent the key to our efforts to help people become self-sufficient so that they no longer need assistance."[25]

Social services were certainly not an entirely new approach to welfare as the federal government was already providing a small amount of funding for various programs, especially in child welfare.[26] Yet the 1962 amendments initiated a sea change in the American welfare system. Surprisingly, "services" was not defined in the legislation, and HEW did not offer a specific definition in the initial regulations either. Martha Derthick writes, "Ultimately [services] could mean anything that would help troubled, handicapped, and dependent people."[27] The new program was attractive to the states because the federal government committed itself to paying 75 percent of the cost of services states provided to its welfare population. For states already providing services, it was found money since they could just turn around and bill HEW for programs they were already offering.[28] The three-for-one matching formula thus provided a strong incentive for states to support a continuation of the services program, which would become known as Title XX.

The social services approach was spurred on by the mounting criticism of AFDC. Conservatives complained that dependency was being passed on from welfare mothers to their children and that something must be done to break the cycle of poverty.[29] As pressure grew to do something to get people off AFDC, "self-help" became the guiding philosophy. Those who were just receiving a check became the unworthy poor, while those who were actively trying to escape welfare deserved job training, day care, and other government-sponsored services.[30] As the War on Poverty was being designed inside the White House, Lyndon B. Johnson summed up his philosophy succinctly when he gave an aide instructions for a meeting with antipoverty czar Sargent Shriver: "You tell Shriver no doles."[31]

When the 1962 amendments came up for renewal in 1967, social services were strongly endorsed despite the lack of any concrete evidence that the approach was working. As the nation's economy picked up steam, escaping from the terrible recession of the late 1950s, unemployment dropped to a record low. Perversely, AFDC enrollment continued to climb.[32] It is certainly conceivable that AFDC rolls might have been even larger without the new money sent to the states, but it seems unlikely that services had any real effect on dependency since actual spending was still modest. Five years after the program was begun, the federal government forwarded just $281 million in matching funds to the states.[33] The real problem, of course, is that dependency and all its assorted ills are not easily ameliorated. Even so, the 1960s was a time when social scientists thought they knew the solutions to social ills and the federal government demonstrated its strongest activist bent since the darkest days of the Great Depression.

The program was not only renewed but, remarkably, no budget ceiling was prescribed. Also, in what seemed like an innocent oversight, the language from the 1962 statute stating that the HEW secretary could determine what qualified as reimbursable services, was somehow dropped. What followed was an open-ended appropriation for services that HEW could not define. The result was an explosion in spending on social services, jumping from $354 million in 1969 to $1.7 billion in 1972. The agency's inability to control the costs of its matching grants led those in the agency to joke that the agency's operating philosophy was "You hatch it, we match it."[34]

Another feature of the 1967 amendments was the removal of restrictions on subcontracting services to nonprofits. States were no longer required to use a circuitous funding route to use nonprofit service providers. With a mandate in the 1967 law for child care and family planning services for those enrolled in job training programs, lawmakers acknowledged that greater utilization of nonprofits was critical to any expansion of social services. The government was actually having trouble filling social worker positions as salaries for comparable positions in the private sector were higher.[35] Whereas earlier administrators were cautious about contracting to private vendors instead of state agencies, a new regime in HEW "made a wholesale commitment" to using nonprofits to deliver services.[36] A particularly interesting incentive to encourage nonprofits to approach state agencies was that they could donate the money that the state had to put up as its match in the one-for-three formula. If, for example, a nonprofit gave the state $25,000, the state would receive $75,000 from Washington, which it would then send to the nonprofit for the services it was offering. Nonprofits would make in-kind donations in the form of the services they were already offering and would designate private contributions or a United Way allocation as the funding source for the donated services. In effect this meant that a nonprofit "could receive a contract essentially at no cost."[37]

Services Dominant

The loophole leading to the uncontrollable spending was corrected in 1972, and a fixed appropriation was set for the social services match. The spending debacle did little to diminish the enthusiasm of policymakers for finding ways to end dependency. As the reach of Title XX expanded, nonprofits took on increasing responsibilities for administration of social programs. In 1971 subcontracting accounted for 25 percent of all state spending on social services. Five years later it had risen to 49 percent. The true figure was surely higher since some state agencies technically contracted with another state agency, but that second agency then turned around and subcontracted its grant to an array of nonprofits.[38]

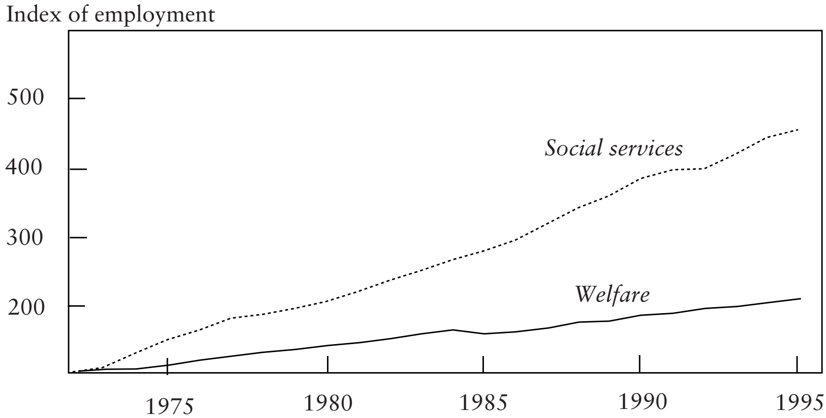
Social services continued to expand beyond those programs first funded by Title XX. Over the years besides core areas like job training, day care, and child welfare, the government came to fund programs for the homeless, runaways, battered women, shut-ins, and many other constituencies. Health and nutrition services are funded from other budget lines, and appropriations for these areas have risen exponentially. Government funds had a compounding effect: nonprofits attracting significant federal money gained in stature and used this credibility to expand their private fund-raising. Through individual donations, foundation grants, corporate gifts, United Way contributions, fees for services, and money garnered from fund-raising events, nonprofits multiplied government's investment. Whatever the mix of funding sources, each year more multiservice centers, more mental health centers, more mental retardation centers, and more of just about every kind of nonprofit, open their doors for business and begin offering services to the needy.

The range of services currently offered by nonprofits is so broad and the level of services so vast that there is no way to offer a summary assessment of their effectiveness. Even evaluating an individual service is difficult. Highly qualified analysts can look at the same program, like Head Start, and come to different conclusions about whether it works. And when programs do not work terribly well, the instinct usually is to find new ways of providing that service rather than giving up on the basic approach. Should the government stop funding teen pregnancy programs because progress has been limited? Assessments of the social services approach to fighting poverty and family dissolution often criticize the shallowness of programs and call for more comprehensive services. In this vein Lisbeth Schorr writes, "Programs that are successful in reaching and helping the most disadvantaged children and families typically offer a *broad spectrum of services*."[39]

Although services may not be as effective as hoped, the social services approach has now succeeded income maintenance as the basic means for providing assistance to people in poverty. In 1996, with the passage of the Personal Responsibility and Work Opportunity Reconciliation Act, AFDC was replaced with Temporary Assistance for Needy Families (TANF).[40] Those on welfare are now restricted in the time they may receive cash benefits and face a stiff work requirement. In President Bill Clinton's words, TANF did "end welfare as we know it"—at least for cash assistance. Social services, particularly job training and child care, remain "as we know them" and may become more important in the wake of TANF and its time limits for cash assistance.

No matter what the future holds for TANF, the bull market for nonprofits providing human services should continue. Unlike the income maintenance approach to welfare, social services are highly labor intensive. They typically require a professional staff trained in counseling, social work,

Figure 1-5. *The Transformation of Welfare: State and Local Government Employment in Public Welfare vs. Private Organizations, 1972–95*[a]



Source: Richard P. Nathan, with the assistance of Elizabeth I. Davis, Mark J. McGrath, and William C. O'Heaney, "The 'Nonprofitization Movement' as a Form of Devolution," in Dwight F. Burlingame, William A. Diaz, Warren F. Ilchman, and associates, *Capacity for Change? The Nonprofit World in the Age of Devolution* (Indianapolis: Indiana University Center on Philanthropy, 1996), p. 33 (reprinted with permission).

a. Private organizations include profit and nonprofit.

substance abuse, special education, or other such field. Quality in services is largely tied to the time that professionals spend with their clients, and thus economies of scale are particularly difficult to achieve. Not surprisingly, the growth in employment for social service nonprofits has far outpaced that of government welfare offices, a large proportion of which are involved with income maintenance programs (figure 1-5).[41]

Changing the approach to welfare not only structurally changed American government by spawning a huge class of government subcontractors, but it also changed the relationship between government and its poorest and most vulnerable citizens. In the United States, when people need help beyond cash assistance they go to nonprofits and do not interact directly with government. Although many receiving services are not unaware that some of the funding for the nonprofit comes from government, the face of compassion, care, and concern they see is the face of private caregivers and community organizations, not bureaucrats and government agencies.[42]

Devolution

Instead of recreating a welfare state built around subcontractors, the federal government could have improved salaries and established multiservice and specialized local offices around the country. This would have provided uniformity in services and alleviated the problem of monitoring the vast number of nonprofits that it now contracts with. During the period of transition to social services, however, the federal government moved toward devolution. There was a growing belief, especially among Republicans, that government would work better if authority as well as revenues were turned over to the states, counties, and cities. Beyond this desire to reinvigorate American federalism, pressure grew on Washington to downsize and to become more efficient—to become in the jargon of the business world, "lean and mean."[43]

The New Federalism and the New Federalism

It is easy to identify reasons why Washington should be shrunk and many of its tasks turned over to local government. The national government is popularly seen as an inflexible leviathan, prone to establishing policies that do as much harm as good. One of the most common criticisms is that Washington prescribes policy on a "one size fits all" basis. Local governments, however, are perceived as more sensitive to the true preferences of citizens and able to tailor policies to fit the unique needs of their constituencies. The imagination and inventiveness of the local citizenry is viewed as an elixir for all that ails the governmental process. As Philip Howard argues, "Whenever the rules are eased, our energy and good sense pour in like sunlight through open blinds."[44]

There is, of course, a simple and compelling reason *not* to ease federal rules in favor of local authority and discretion. Statutes and regulations are drafted in a one-size-fits-all manner to ensure that people are treated equally before the law. If there is a federal program to provide mental health services to those who have no means of paying for them, shouldn't everyone, regardless of where they live, be subject to the same eligibility requirements and receive the same level of services? If federal dollars are paying for those services, shouldn't recipients in Tennessee obtain the same level of counseling and medical care as those residing in California? This is the liberals' concern. But in the face of continuing criticism of the national government, the liberals' rhetoric has not been as convincing and their voices have not been as loud. Liberal legislators in Congress sympathetic to this point of view have also been compromised by Democratic mayors and governors who want greater freedom to spend federal dollars in the way they see fit. They want that freedom as long as those budgets are not cut in the process of devolving programs onto the states and cities.

Within this context of conservative preference for smaller government on the federal level and liberal concerns for protecting funding for social programs, President Richard M. Nixon put forward his "New Federalism." Soon after taking office, Nixon proposed a fundamental alteration in American federalism, offering revenue sharing to state and local governments. Nixon said his proposals "represent the first major reversal of the trend toward ever more centralization of government in Washington."[45] The revenue sharing concept was enormously popular with governors and mayors since such funds could provide badly needed fiscal relief. This step back from categorical grants with their specific mandates gave state and local governments flexibility and additional money. Despite the enthusiasm from state and local officials, Democratic leaders in Congress were wary, and revenue sharing was not enacted until a few weeks before the 1972 election.[46]

Nixon's new federalism did not stop there. He subsequently put forward specialized revenue sharing proposals in broad policy areas. Resistance from Congress resulted instead in new block grant programs, like CDBG (the Community Development Block Grant program). This combined seven different housing and community development programs into just one but still required applications from local municipalities, and the law contained extensive guidelines on the use of the CDBG money.[47] Nevertheless, it was an important step as it gave communities significant flexibility and clearly redefined the role of the federal government in the housing field. Increasingly the Department of Housing and Urban development's responsibility was to evaluate the different approaches each city took with its federal dollars, which typically involved subcontracts with nonprofits. But as Richard Nathan points out, "Nonprofit groups . . . were not explicitly considered in framing Nixon's new federalism."[48] The focus was on the changes in fiscal relations between Washington and the states and cities, and the greater flexibility offered to local government officials. The implications for nonprofits were not yet fully recognized by policymakers at the national level.

When Ronald Reagan took office in 1981 he, too, emphasized block grants as an instrument of change. His similarly labeled "new federalism" was primarily oriented around reducing the size of the national government. Advocating a replacement of AFDC and Food Stamps with a block grant to the states, Reagan said, "In a single stroke, we will be accomplishing a realignment that will end cumbersome administration and spiraling costs at the federal level while we insure these programs will be more responsive to both the people they are meant to help and the people who pay for them."[49] Reagan's true goal was to reduce the size and scope of government rather than to sort out the functions of government among the federal, state, and local levels. Still, in Reagan's mind, cutting the federal budget was the "first step toward returning power to states and communities."[50]

Buoyed by supportive Republicans in Congress, Reagan's initial efforts to implement his new federalism were highly successful. In the momentous 1981 budget act, nine new block grants were created through the merger of seventy-seven categorical programs. In addition sixty categorical programs were abolished.[51] (The proposal to combine AFDC and Food Stamps was not enacted.) The discretion offered to local governments through these block grants ranged considerably, and some programs eventually went through "recategorization." As liberals feared, overall federal spending for the block grants was much less than the combined spending for all the programs they replaced. Between 1980 and 1990, domestic spending for all nonentitlement programs dropped 10 percent in constant dollar terms.[52]

The contrast to Richard Nixon's new federalism was striking. In Nathan's words, "Nixon was a big spender."[53] His goal was to provide money to state and local governments with a minimum of restrictions. He wanted to share the federal largesse in the belief that local control and federal dollars would produce the most effective social policy. For Reagan block grants were a means to reduce federal funding of the same kinds of services and programs that Nixon wanted to support. Reagan's supporters argued that if state and local governments wanted to spend more than the reduced funds Washington was willing to provide, they could raise their own revenues to do it. Reagan also saw a greater role for private charity. He called on individuals and corporations to do more, linking his appeal to a revival of community. In Reagan's mind, America needed to embrace small town values, replacing government paternalism with private voluntarism.[54]

Even though the goals were vastly different, Nixon's and Reagan's versions of the new federalism reshaped intergovernmental relations in America. The expanding discretion deriving from block grants gave state and local government agencies more and more opportunity to experiment and to create competition among potential vendors.[55] Different 501c3 organizations would vie by offering their own program designs for addressing the needs of the community. This was an important change in American government: broad outlines of policy would be developed in Washington, but more detailed program design would, in a sense, be put out for bid. Nonprofits would compete on the basis of their proposals and, over time, on the basis of their performance as well. As in the private sector, competition would presumably produce the optimum outcome: the "best practices" for treating social ills. This competition among nonprofits would be unleashed across the country, in every major city, in every state of the union. The culmination of the two new federalisms was the application of market logic to social services.

False Downsizing

Ultimately Reagan's most enduring accomplishment on domestic policy may have been to make "government" a dirty word. Since he took office in 1981 there has been relentless pressure to keep government small. Democrats and Republicans have been loath to let the size of government expand. Since even in bad times budgets grow inexorably, the coin of the realm in political discussions has been headcounts of government workers. For presidents as well as members of Congress, being able to point to even a small reduction in the number of federal government workers is good enough for the campaign trail.

Head counts may make for good campaign rhetoric but they are a terribly misleading measure of the size of government. Even though its tasks have grown, the federal government has been able to keep its official work force small by subcontracting with the nonprofit and private sectors. The result is what political scientist Paul Light calls the "shadow government." In 1996, the head count of the federal civilian work force was 1.9 million individuals. But that year the federal government indirectly employed 12.7 million full-time equivalent jobs through grants, contracts, and mandates to state and local government.[56] Although there has been a modest decline in the overall federal work force (civil servants plus shadow employees) during the past few decades, there has been a significant rise in employment in the policy areas where nonprofits are most prevalent. For both Health and Human Services and Housing and Urban Development, grant and contract employment has risen sharply.[57]

Subcontracting has been the perfect answer for an electorate that wants services without bureaucrats. More than a government version of Three Card Monte, subcontracting is built on the belief in private sector efficiency. Backed by research demonstrating that the private sector can often deliver services for less money, privatization became another foundation of the Reagan revolution.[58] A variant in the privatization movement is public-private partnership, where corporations and nonprofits form a new nonprofit to coordinate their collaboration with government. The public-private model is undeniably attractive, though the enthusiasm for the concept has always outrun the willingness of businesses to work on social issues.

The dominant trend has been delegation to nonprofits rather than to private sector vendors, although in the past few years more private sector firms like Lockheed Martin and Maximus have become competitors to nonprofits.[59] The role of private sector vendors in human services does not represent a belief that the ideology of efficiency has been compromised by the increasing subcontracting of government services to nonprofits. Rather, the growing competition is more an indication of the money now available to government social service subcontractors.

Although there is no one broad measure of efficiency to use in comparing direct government service providers or private sector vendors to comparable nonprofit organizations, nonprofits' heavy reliance on volunteers and their employees' low salaries are, by themselves, significant sources of efficiency. When fiscal problems squeeze government, demands on nonprofits grow and their ability to offer services in an environment of shrinking resources has enhanced their image of efficiency.[60] The poster child for nonprofit efficiency could be Louisville Housing Services, which the city created to give itself flexibility. At one time Louisville Housing Services had no full-time employees and was run by a half-time consultant.[61] That office contracts with nonprofits to manage all its housing projects.

For all the reasons highlighted, subcontracting became the principal form of social service delivery in the United States.[62] State and local agencies, reluctant to add bureaucrats for the same reason the federal government avoids head count creep, have utilized nonprofits to do what they cannot realistically do themselves. But the government does not merely delegate policies to nonprofits to implement. As chapter 5 details, nonprofits are collaborators with local agencies at every stage of the administrative process.

Operating through grants and contracts, nonprofits adapt and grow and learn how to anticipate government's needs. Large, successful nonprofits can offer a rather substantial range of services to clients. As table 1-1 shows, a single nonprofit can administer numerous government programs, each with its own separate demands for specialized staff skills and organizational capacities. In 2001–02, the "Front Street Health Center" in Massachusetts operated thirty-five programs funded by various government agencies.[63] For simplicity's sake the table lumps together different grants falling under the same general program, but the reality is much more complicated. For example, Front Street runs three separate Ryan White programs, each dependent on a separate grant and each necessitating a different administrative relationship with agency overseers.

Table 1-1. *One Nonprofit, Thirty-Five Government Programs*[a]

Program	*Funding/implementing agencies*
ACT Now[b]	Massachusetts Department of Public Health (DPH)
AIDS Transportation Grant	Boston Public Health Commission
Breast and Cervical Cancer Initiative	Centers for Disease Control/(DPH)
Campaign for Excellence[b]	Mass. Dept. of Medical Assistance
Center Care	DPH
Children's Medical Security Program	DPH
Chronic Disease Prevention	CDC/DPH
Community Health Centers (#330)	Bureau of Primary Health Care, Health Resources Srvc Adm (HRSA)
Community Access Program[b]	Bureau Of Primary Health Care, HRSA
Community Health Center Enhancement	DPH
Dental Services	Bureau of Primary Health Care, HRSA
Enrollment and Outreach	Mass. Dept. of Medical Assistance
Free Care Pharmacy Demonstration Project	Mass. Division of Health Care Finance and Policy
Hardship Grant	Mass. Division of Health Care Finance and Policy
Health Access Program	DPH and Mass. Division of Mental Health
Healthy Schools, Healthy Communities	Bureau of Primary Health Care, HRSA
Healthy Start	Health Care Financing Agency/DPH
Home Intervention Program	Mass. Dept. of Mental Retardation
Immunization Program	DPH, Division of Food and Drugs
Mass. Loan Repayment Program	DPH
Medicaid	Mass. Dept. of Medical Assistance
Medicare	Centers for Medicare and Medicaid
New Access Point	Bureau of Primary Health Care, HRSA
New Start Dental Program	DPH, Division of Oral Health
NS AIDS Collaborative	DPH
PACE (all-inclusive elderly care)	Medicaid and Medicare
Perinatal and Pediatric Program	DPH
Proyecto Encuentros[b]	HRSA, Substance Abuse Mental Health Services Administration
Refugee and Immigration Health Program	DPH
Representative Payee Program	Mass. Dept. of Mental Retardation
Ryan White Act	DPH/HRSA
School Based Health Centers	DPH
Tobacco Control Smoking Cessation	DPH
Uncompensated Care Pool	Mass. Division of Health Care Finance and Policy
Women, Infants, and Children	U.S. Dept. of Agriculture/DPH

a. Federal, Massachusetts, and city-funded programs at the Front Street Health Center.
b. Grant is to another nonprofit, and Front Street is a subcontractor.

Devolution has come in different ways to different nonprofits. In an interview a Native American leader described the gradual process by which the tribe's nonprofit came to take over programs previously operated by the Bureau of Indian Affairs and other government agencies:

> For the Bureau, we provide the whole range of their services under federal regulations: realty, social services, 15 programs in all we control. The biggest one is social services, part of which is under the TANF program. We do credit finance, loans. . . . We also do job creation and opportunity for our clients. For the state we deliver medical programs, mental health programs [and so on]. We do forestry work. We have an agent on staff who does the cooperative extension work for the system.

The demand by government for nonprofit services continues to grow. The replacement of AFDC with TANF was another huge step in the devolution of government services to the nonprofit sector. In interviews for this study, TANF contracts were repeatedly cited by respondents as representative of the partnerships they had developed with government agencies. But TANF is but one step along a long road. For both political parties, for policymakers at the federal, state, and local levels, and for officials in the legislative and executive branches, the logic of devolution is incontrovertible. Devolution is a means of pretending that government is lean while at the same time maintaining necessary services. Nonprofits are flexible, efficient, and willing to operate in a competitive environment characterized by tight resources. For the 501c3s, devolution is also a path to growth since agencies' constant search for new approaches and more effective ways of providing services creates ongoing opportunities for entrepreneurial nonprofits. When an individual nonprofit grows, the additional revenue allows the organization to address more problems, serve more clients, and come a little closer to fulfilling its mission. For all concerned, devolution is the ultimate win-win situation.

Conclusion

The sharp rise in the number of nonprofits seems to be a classic case of supply and demand. Since the 1960s demand for nonprofits has soared, and the nonprofit sector has demonstrated little trouble in generating enough 501c3s to meet the growing needs of American society. The source of these needs was the transformation of the nation's welfare system. Social services are labor intensive, and nonprofits provide the lion's share of the counselors, employment specialists, social workers, and others who deliver those services. The devolution of social programs, fueled by the movement toward block grants and the political pressure to keep government bureaucracies small, has pulled nonprofits closer into the web of government.

Underlying these changes were two powerful ideas. As the debate over welfare and devolution developed within academe and government, sharp partisan and ideological divisions were never far from the surface. Yet significant resolution was achieved because liberals and conservatives found some common ground. In the case of welfare, conservatives wanted to find ways of cutting back on the welfare state by reducing people's dependency. Liberals did not focus on dependency, but they liked the idea of providing support beyond income maintenance. Social services offered both sides a means of addressing the welfare problem as they saw it. Devolution also represented a neat meld of conservative and liberal preferences. Conservatives wanted a small national government, believing that the scope of government at the state and local levels would accurately correspond to the preferences of their citizens once these governments were given discretion over social programs. Nixon was a bit of an aberration among conservatives who were also looking for ways to cut the budget. Liberals did not share the cost-cutting goals of the conservatives, but the civil rights movement prompted them to look for ways of giving people in urban centers more control over their lives. In politics ideas have power, and these two ideas led to an unprecedented role for nonprofits in America.[64]

Ironically, the debates surrounding these ideas focused little on nonprofits. Even as government's dependency on nonprofits became clear to policymakers over the years, the capacity of nonprofits to administer the welfare state has not been seriously questioned.[65] Nor has our trust in nonprofits been shaken by the occasional scandal like those involving the United Way and the American Red Cross. And that trust is enormous. Nonprofits are given responsibility for our most vulnerable populations, for people who may not have the sophistication to understand their options in services or treatments. Although nonprofits administer government programs, they are not government agencies and are not accountable in the same way as government officials are.[66] This deep reservoir of trust extends to almost all realms of nonprofits' activity, except for involvement in public policy. In the case of advocacy, the federal government has a policy of restrictive regulation. One thing that has not devolved down to nonprofits is the right to represent those that they serve.