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## **Diffusion of Nonprofit Organizations from an Internal and an External Perspective**

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### **Abstract**

Nonprofit organizations are generally considered to be employed in order to achieve goals as they relate to the needs and desires of the local community. Diffusion of nonprofit organizations, on the other hand, can depend on various government conditions, such as the availability of resources. This is because most nonprofit organizations rely on grants from the government. Thus, this study attempts to examine whether nonprofit organizations are more commonly established under favorable government conditions or any other conditions, such as emulation of neighboring counties and other socioeconomic factors. Using a panel data set from 24 counties in Maryland between 2007 and 2012, our analysis demonstrates that nonprofit organizations are more commonly established when social conditions have deteriorated in a county rather than when financial conditions of government are good. This implies that nonprofit organizations have voluntary characteristics.

**Keywords:** nonprofit organizations, organizational diffusion, social conditions

### **Introduction**

As society has become more democratized and decentralized, citizens have been more willing to participate not only in issues in their community, but also in government work. They are also interested in the improvement of public service delivery to address social problems. Recently, the pattern of public service delivery has changed from a hierarchical system to a governance model, in which public service is provided through a complex form of network building with other nongovernmental entities. This is because government programs and regulatory activities directly affect citizens, and government is well supported by citizens only when it performs its activities and carries out its responsibilities well. Public service can be provided through various

systems and devices with the private sector, especially when the nonprofit sector's interest in and criticism of public service is rapidly increasing. That is, collaboration with different participants is one of the critical factors that ought to be considered in planning and processes for government policy making that results in positive outcomes and also addresses social problems in the community.

Currently, various nonprofit organizations are immersed in the context of governance and are considered a type of collaborator. This is because a nonprofit organization in the community commits to advancing its social responsibility by managing social business, and the forms of collaboration is through the provision of empowerment to community residents. Citizens in the community take over vital services for the greater benefit of their community. Nonprofit organizations in the community have an autonomous and democratic nature. Additionally, profits from their commercial activities are reinvested into the community, and these activities of nonprofit organizations can serve as strong policy tools for addressing community problems with voluntary cooperation from citizens.

While the number of nonprofit organizations in the community has increased, there is no previous empirical study which examines why nonprofit organizations are established more in some local governments than others, although several studies have examined the impact of nonprofit organizations on community conditions. This nonprofit organization's diffusion is meaningful to study because: 1) it leads to competition with other public sector services or businesses, and as a result, service quality can be improved; 2) nonprofit organizations bring positive social impacts to the community and local government through the revitalization of communities and the support of disadvantaged groups; and 3) it improves the community through innovations in the form of service.

Nonprofit organizations are more likely to appear when severe community conditions are present, such as high unemployment and poverty rates, because nonprofits are often one of the best alternative solutions for a community. Additionally, they might be varied based on financial conditions in local government because nonprofit organizations rely on governmental grants. This is because nonprofits have suffered from revenue shortages as grant money decreases when governments face economic crises. Alternatively, they are initiated by emulating behavior of other neighborhoods and communities as they learn how they work. Thus, this study attempts to examine why nonprofit organizations are more commonly established based upon the financial condition of county governments. The study not only includes variables such as socioeconomic attributes within a county but also considers emulating behavior from neighboring counties.

### **Literature Review**

*Collaboration with Nonprofit Organizations:* The necessity for changes to the form of public services leads to changes in the way policy is delivered. The form and direction of public service delivery to citizens has stressed increased cooperation and partnerships among various actors such as the government, the private sector, nonprofit organizations, and even citizens

themselves. The form of service delivery and policy development has been transformed into collaboration (Adshead & Quinn, 1998).

Collaboration plays such an important role in public-private partnerships that each benefits the other (Gazley & Brudney, 2007). Under the condition that organizations cannot solve the problem and find appropriate solutions by themselves, collaboration comes in the form of increased voluntary relationships as well as minimized contractual associations. Thus, all participants in the collaborative process can have mutual power and articulate their opinions or ideas without pressure from any influence or power when they make suggestions. Through collaboration, participants in such partnerships can mutually increase the benefits to all parties by sharing resources and knowledge with each other (Wood & Gray, 1991).

*Participation of Nonprofit Organizations:* Citizen participation is defined as a process of citizen involvement in providing services and making decisions (Wang, 2001). Traditionally, citizen participation is implemented in a passive form, such as public hearings and community meetings, as an important method of participation (Raudla & Krenjova, 2013). Moreover, active participation in solving community problems can be realized when the citizens manage their own social business by improving communities as well as making profits for investment in communities. It involves playing a role as “real” owners in their community and co-producers of public services with the government (King, Feltey, & Susel, 1998). This type of participation is related to how public values can be realized (Lane, 1998).

Currently, nonprofit organizations have characteristics of enterprise and run social businesses. A community business, as a form of a nonprofit organization, is established, owned and controlled by the local community in order to develop communities and improve community conditions, so it is based on geographic attributes and definitions with a focus on issues in specific local areas. Citizens themselves run the business in the particular communities, and they make money through selling products or services. However, nonprofit organizations don't settle just for profit seekers. They improve community conditions through investing their profits into community development.

*Diffusion Theory in Nonprofit Organizations:* There are two primary forms to explain the initiation of a new program: internal determinants and regional diffusion models (Berry & Berry, 1990). Internal determinant models assume that factors for innovation include political, economic or social characteristics of the state and are not influenced by any external actions. On the other hand, diffusion models are intergovernmental and believe that policy adoption in a state is affected by emulation processes in neighboring states. Most of these models assume that states are influenced entirely by states with which they share a border (neighbor models) (Berry & Berry 1990; Mintrom 1997; Bella 2001). Berry and Berry (1990) introduced a model of state lottery adoptions reflecting the simultaneous effects of both internal determinants and policy diffusion on state adoption behavior and employed event history analysis to test their model. First, decision makers adopt a policy directly by making certain of the necessity for the policy, and indirectly by stimulating demand for the policy by societal groups (Berry & Berry, 2007). Second, in terms of resources, innovation theories have emphasized the importance of

financial resources, which means the ability of the potential adopter to innovate. This is because new government programs often require high expenditures. Organizations of a larger size with higher levels of “slack resources” are expected to be more innovative than smaller organizations and those with lower levels of slack (Cyert & March, 1963; Rogers, 1995).

Applying the Berry and Berry model, this study assumes that both internal determinants and regional influences help explain the variations in the establishment of nonprofit organizations. However, our research uses a different model from the previous ones: 1) previous diffusion research has focused primarily on the state level (Berry & Berry, 1990, 1992; Mintrom, 1997; Mintrom & Vergari, 1998), but this study deals with local governments as a unit of analysis; 2) prior studies have used as a dependent variable the adoption of a policy (Berry & Berry, 1990, 1992), while this paper focuses on the number of nonprofits (non-governmental area and organization itself rather than policy) in each county over time; and 3) this research begins to focus on the financial condition as well as emulation behavior of the organization.

### **Hypotheses**

*Financial Conditions:* All nonprofit organizations require start-up funds. Additionally, in order to maintain their businesses, they must rely on government grants as one of main revenue sources. However, if nonprofit organizations have suffered from financial instability and decreased availability of grants, they have difficulty in operating the organization. Thus, when government does not have a strong fiscal condition, it might lower its grants to nonprofit organizations. In addition, organizations of larger size or with higher levels of “slack resources” are assumed to be more innovative than smaller organizations with fewer resources (Cyert & March, 1963; Rogers, 1995). Walker (1969) similarly concluded that larger, wealthier, and more economically developed organizations are more innovative, because these organizations have greater adaptive abilities and tolerance for change. Thus, some studies hypothesize that the fiscal health of a state’s government has a positive effect on the propensity of a state to adopt a new policy (Allard, 2004; Lowry, 2005). Daley and Garand (2005) insist that the capacity of a state’s economy to finance extensive public services is the ultimate determinant of the state’s propensity to innovate. Thus, local governments will not attempt innovative methods of public service delivery if they do not have sufficient resources. Local governments expend money when they support nonprofit organizations. According to Zhang and Yang (2008), the new policy adoption is also related to the financial condition of local government. Nonprofit organizations are susceptible to financial problems because they face high start-up costs and require resources to operate the business.

*Hypothesis 1: Counties with a higher level of financial resources are more likely to have a higher level of nonprofit organizations.*

*Institutional Conditions:* Legislative party and executive offices significantly influence policy adoption and support for implementation of such policies (DiConti, 1996; Jacobs & Carmichael, 2002). The ideological tendency of policy makers affects the probability of policy adoption. The reason political dominance is critical for policy adoption is that “party dominance reflects a more general understanding of liberal/conservative ideals and values that are present in the legislature and state as a whole.”

(Renzulli & Roscigno, 2005, p349) Spending on nonprofit organizations or other collaborations with community activities are dependent on the preference of the decision makers.

Thus, this study assumes that Democrats support nonprofit organizations more, and that there are more nonprofit organizations in a county which is dominated by the Democratic Party. In addition, because decision makers usually behave rationally toward reelection, their decisions should consider voters' demands in the jurisdiction. Some studies (Renzulli & Roscigno, 2005; Zhang & Yang, 2008) suggest that citizens' ideologies might reflect the predictability of new policy adoption.

*Hypothesis 2.1: Democratic counties are more likely to have a higher level of nonprofit organizations.*

Previous studies found that governments tend to adopt a policy if their neighboring governments have already adopted the new policy (Walker, 1969; Light, 1978; Berry & Berry, 1990; Mooney, Christopher, & Lee, 1995). Three factors explicate the regional influence of adoption: learning, competition, and public pressure (Berry & Berry, 2007). In terms of regional diffusion, most of the models assume that each level of government is influenced entirely by the governments with which they share a border (neighbor models). These models hypothesize that the probability that each level of government will adopt a policy is positively related to the number of governments bordering it that have already adopted it (Berry & Berry, 1990; Mintrom, 1997; Bella, 2001). Specifically, the models emphasize the emulation of nearby governments. Policy diffusion happens most commonly when a local government competes with other local governments which share its border (Berry & Berry, 2007). Due to concerns that residents can move to other areas, each local government must compete with other neighboring governments. Relevant to this, nonprofit organizations may also learn how to start a business or other components of running a business from neighboring communities.

*Hypothesis 2.2: The number of nonprofit organizations is positively related to the number of nonprofit organizations in neighboring counties.*

*Socioeconomic Conditions:* Citizens in a community have different policy preferences and needs, as well as different socioeconomic backgrounds (Teske, Schneider, Buckley, & Clark, 2000; Weiher & Tedin, 2001). Substantial racial variances and different household income levels lead to variations in preferences about nonprofit organizations in local areas. A community with a high level of minority or low-income residents most often requires more nonprofit organizations. Based on empirical research, districts with lower income and a greater number of minorities prefer to create new policies (Mintrom, 2000; Nathan, 1996). Additionally, social conditions such as the unemployment rate and the poverty rate might call for new policy forms or collaboration with non-governmental sectors.

*Hypothesis 3.1: Counties with large minority populations have more nonprofit organizations.*

*Hypothesis 3.2: Counties with high unemployment rates have more nonprofit organizations.*

### Data and Methodology

*Data:* In our analysis, we empirically investigate the impact of various factors, and in particular financial resources, on the diffusion of nonprofit organizations in local government by using a longitudinal analysis from 2007 to 2012. To estimate the effect of financial resources on nonprofit organizations' diffusion in local government, this study uses fiscal, political, economic, and demographic data for 24 counties from 2007 to 2012.

*Dependent Variable:* This study is interested in the degree of expansion of nonprofit organizations. Accordingly, the dependent variable is the number of operating nonprofit organizations per county year. In order to account for the overall size of the different counties, each is measured as a nonprofit organization per population in the local government.

*Independent Variable:* For financial capacity, this study will consider financial resources as a financial condition in a county year. To measure financial resources, this study will use revenue per capita, which is the total general revenue from local government's own sources and grants divided by the total number of people per county year. Neighboring nonprofit organizations are measured by the total number of nonprofit organizations in neighboring counties (Berry & Berry, 1990, 1992; Rinke, 2004, 2007; Renzulli, 2005; Zhang & Yang, 2008). In terms of political ideology in the counties, citizens' political ideology may serve as a proxy for the political ideology in the county, and this is measured by the percentage of voters registered with the Democratic Party.

To measure socioeconomic factors, this study will measure the number of minorities in the population and the low-income population in a county year. The composition of the minority population is measured by the percentage of the African-American and the Hispanic population in the county year. The unemployment rate and personal income changes are also used in the analysis as indicators of economic conditions. They are related to the level of income in a county's population and are an appropriate indicator of it.

*Model Specification:* In our analysis, the total number of nonprofit organizations is used as a dependent variable. The Ordinary Least Squares (OLS) model with a panel data set in Maryland from 2007 to 2012 offered for our analysis measures how governmental, social, and economic factors affect the total number of nonprofit organizations. In this model, the dependent variable is estimated as shown in equation (1):

$$Nonprofit_{i,t} = \alpha + \sum(Governmental\ Variables_{i,t}) + \sum(Institutional\ Variables_{i,t}) + \sum(Socioeconomic\ Variables_{i,t}) + \varepsilon_{i,t} \quad (1)$$

Where governmental variables include revenue per capita, institutional variables consist of the total number of neighboring nonprofit organizations and the total number of Democratic voters out of the total population, and socioeconomic variables include land size, unemployment rate, personal income change of people, and the proportion of minorities, such as African-Americans and Hispanics, in each county.

### Results

Table 3 provides the regression results for the total number of nonprofit organizations as a

dependent variable. The model indicates that the number of nonprofit organizations has a positive impact on the total number of nonprofit organizations in neighboring counties. It supports the evidence that the number of nonprofit organizations in neighboring counties influences the number of nonprofits in the county and proves the model of Berry and Berry (2007). Political ideology is statistically significant as well. Counties with a high level of Democratic voters are more likely to have nonprofit organizations compared to those with a lower Democratic voter rate. Democratic voters are more likely to support new programs. In addition, the unemployment rate has a positive impact on the number of nonprofit organizations at the 1 percent level of significance. This indicates that severe social conditions attract new programs or new forms of service delivery. The minority group also has a positive relationship with the total number of nonprofit organizations. Counties with large minority populations have more nonprofit organizations, and this indicates that disadvantaged groups might prefer non-traditional governmental service delivery and new types of organizations. However, the personal income level of the region is not significant in terms of nonprofit organizational expansion.

(Table 3 here)

### **Conclusion**

This study concludes that the total number of nonprofit organizations is likely to increase as the number of nonprofit organizations in neighboring counties, the percentage of Democratic voters, the unemployment rate, and the percentage of Hispanics and African-Americans increases. However, revenue per capita does not prove statistically significant in our analysis. Thus, the number of nonprofit organizations in the county is proved to be determined by emulation among counties, and not by 'financial slack,' in local government. Moreover, deteriorating social conditions induce more nonprofit organizations in order to improve the community.

Nonprofit organizations can substitute for roles that governments normally play in the delivery of public services. According to the results of our analysis, the number of nonprofit organizations increases in poor economic conditions. High unemployment rates and negative personal income changes (even though they are not statistically significant) have positive effects on the number of nonprofit organizations. Thus, citizens' preferences or needs for nonprofit organizations in local government increase when they experience severe economic conditions in their regions. This indicates that nonprofit organizations have voluntary characteristics.

However, our research also has some limitations. First of all, the definition of nonprofit organizations is sometimes ambiguous, and the only reliable data set for nonprofit organizations is the nonprofit organizations from 501 (c) (3) of the IRS revenue code. Second, some counties serve as outliers in our analysis, because the State of Maryland has extremely varied counties in terms of their overall structure and other characteristics. Thus, it is difficult to reflect all of the differences in the counties included in our analysis.

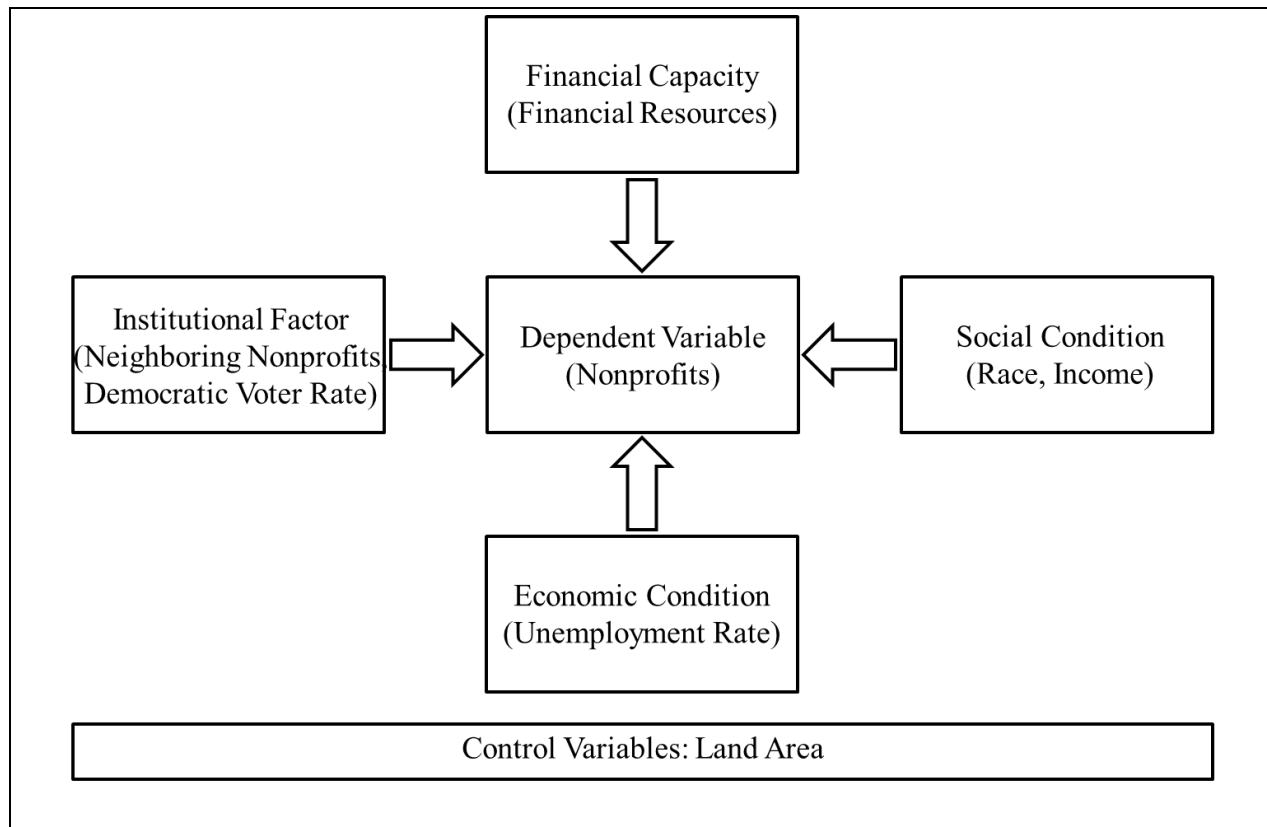
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Figure 1: Conceptual Framework of Nonprofit Organizational Diffusion



**Table 1: Variable Specification: Variables, Descriptions, and Data Sources**

Variable	Description and Data Source
<i>Dependent Variable</i>	
Nonprofits	Total number of nonprofit organizations; Source: Maryland Nonprofits ( <a href="http://www.marylandnonprofits.org">www.marylandnonprofits.org</a> )
<i>Independent variable</i>	
Revenue per capita	Total revenue divided by total population (amount expressed in millions of dollars); Source: Comprehensive Annual Financial Reports (CAFR) in each county and U.S. Census Bureau
Neighboring nonprofits	The number of nonprofit organizations in boundary/ neighboring counties (measured in 1,000); Source: Maryland Nonprofits ( <a href="http://www.marylandnonprofits.org">www.marylandnonprofits.org</a> )
Democratic voter	Number of Democratic voters out of the total population in each county (measured in percentages); Source: The State Board of Election in Maryland and U.S. Census Bureau
Land size	Land size of each county measured in 1,000 square miles; Source: U.S. Census Bureau
Unemployment rate	Unemployment rate in each county from 2007 to 2012; Source: U.S. Bureau of Labor Statistics
Personal income changes	Percentage of total income change from preceding year in each county from 2007 to 2012; Source: U.S. Bureau of Economic Analysis
Hispanic and African-American	Number of Hispanics and African-Americans out of the total population in each county measured in percentages; Source: U.S. Census Bureau

**Table 2: Descriptive Statistics**

Variable	Mean	SD	Min	Max
<i>Dependent Variable</i>				
Nonprofits	6.120	1.192	4.111	8.625
<i>Independent Variable</i>				
Revenue per capita	0.003	0.005	0.001	0.057
Neighboring nonprofits	3.508	3.888	0.232	16.151
Democratic voter	36.355	25.750	4.461	102.663
Land size	0.402	0.153	0.081	0.660
Unemployment rate	6.684	2.298	2.600	12.200
Personal income change	3.499	2.434	-6.130	9.560
Hispanic and African-American	0.250	0.185	0.015	0.810

**Table 3: Regression Model Results**

Variable	Coefficient	Standard Error
Revenue per capita	-0.690	1.592
Neighboring nonprofits	0.116 ***	0.018
Democratic voter	0.016 ***	0.003
Land size	-0.013	0.045
Unemployment rate	0.025 ***	0.005
Personal income change	-0.001	0.003
Hispanic and African-American	1.889 ***	0.632

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