Nonprofit Accountability Clubs: Voluntary Regulation of Nonprofit and Nongovernmental Organizations

Volume Overview and Chapter One

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Preface

The growth in the scale and scope of the nonprofit sector has been accompanied by accountability challenges. Nonprofits have responded to demands for increased accountability in a variety of ways. This volume focuses on one of the salient accountability instrument employed by nonprofits: voluntary programs or codes; voluntary clubs, as we term them. Voluntary clubs seek to create institutional incentives for participating actors to adopt specific codes of conduct and practices beyond what is legally required of them. If accountability issues can be viewed as “agency problems,” voluntary clubs provide an opportunity for nonprofits (as agents) to signal to their resource providers and authorizers (the principals) that they are governing as agreed and delivering as promised. By virtue of their membership in such accountability clubs, nonprofits expect that the resource providers will reward them with more resources and less onerous governance costs.

Voluntary clubs are complex institutional structures. To explore their institutional design issues, we draw on the club approach which is well established in political economy. We bring in the principal-agency perspective to explore agents’ motivations for establishing and joining voluntary clubs, and the principals’ responses to them. The empirical chapters explore three core themes: (1) The Emergence of Voluntary Accountability Clubs, (2) Club Sponsorship and (3) Club Design and Effectiveness.

This volume makes two key contributions. Theoretically, it outlines an accessible yet robust framework for studying voluntary programs in the nonprofit sector. The book expands on club theory to account for variations in the emergence, recruitment, and efficacy of voluntary programs. Empirically, this book provides careful application of the club perspective
across a range of voluntary programs and contexts. These programs vary by sector type, sponsor type, and target participant type. This is the first book we know of that examines a wide range of voluntary programs in the nonprofit sector by employing a single theoretical perspective.

We began working on this project in the summer of 2007. We developed an introductory concept chapter and carefully identified scholars doing interesting work on nonprofit accountability. Thanks to generous financial support from the Office of the Dean, Daniel J. Evans School of Public Affairs and the Marc Lindenberg Center, both at the University of Washington, we organized a workshop for the authors at University of Washington in April 2008. At this workshop, the contributors presented the first drafts of their chapters. They received valuable feedback from each other and from UW graduate students and faculty who served as discussants. After the workshop, we provided detailed feedback on every chapter; our feedback also reflected the comments offered by Cambridge reviewers. The chapters were revised in the summer and fall 2008. The result is a series of very strong chapters which respond to the theoretical framework outlined in introductory chapter and which cohere.

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Chapter 1

Nonprofit Accountability Clubs: An Introduction

Mary Kay Gugerty & Aseem Prakash

The “associational revolution” (Salmon, 1994) of the 1990s has led to the substantial expansion of the scale and scope of nongovernmental and nonprofit organizations – the nonprofit sector. During this growth phase -- marked by massive infusion of funds from governments, international organizations, foundations, and individuals -- this sector became a target for close scrutiny, partially because it seems to have attracted “bad apples.” Scandals and charges of mismanagement and misappropriation have been extensively covered by the media (Greenlee, et al, 2007; Gibelman and Gibelman, 2004; Fremont-Smith and Kosaras 2003). Consequently, nonprofits face demands for accountability from resource providers as well as the constituents they claim to serve (Edward and Hulme, 1996; special issue of Chicago Journal of International Law, 2002; Ebrahim, 2003). High profile cases of governance failure have imposed negative reputational externalities on all nonprofits. A recent global opinion survey found that in a number of countries worldwide, the nonprofit sector is now less trusted

1 Since both NPOs and NGOs are subjected to the non-distributional constraint – they cannot distribute their profits to their principals – we will use the term nonprofits for both types of organizations.

2 Nonprofits are also criticized for accentuating “democracy deficits,” especially if they appear to be substituting for democratically elected governments. This volume does not examine this issue. We focus on voluntary programs which have emerged in this sector response to perceived governance failures.

3 The accountability literature is too large to be cited. For a recent overview see Grant and Keohane (2005), Rubinstein (2007) and Ebrahim and Weisband (2007).
than government or business (Edelman 2007). If scandals undermine the credibility of nonprofits as a category of actors, credible nonprofits might find these scandals reducing their ability to raise funds (Arumi, et al, 2005; Light, 2004), and to function with a reasonable degree of autonomy. Scandals can also attract the interest of regulators, who come under increased pressure to “do something” about the problem. In the United States, corruption and governance scandals in the for-profit and nonprofit sectors led to increased Congressional scrutiny of the regulatory framework governing the nonprofit sector (Independent Sector 2007; 2005). In many developing countries, rapid growth in the nonprofit sector combined with weak regulatory institutions have spurred government initiatives to increase regulatory authority over nonprofits, often with intent of controlling or curtailing what is viewed as political activity (Gugerty, 2008a). Thus, credible nonprofits, the good apples, seek ways to differentiate themselves from the bad apples, and to credibly signal their commitment towards good governance to their principals. This volume examines how voluntary clubs might be employed, successfully as well as unsuccessfully, as institutional vehicles for this task.

We begin with the premise that the governance and accountability challenges nonprofits face can be viewed as agency problems. Given the widespread perceptions of such agency conflicts, the challenge for “good” or “credible” nonprofits is to demonstrate to their resource providers and authorizers that they are governing as agreed and delivering as promised. These agency problems are accentuated because multiple principals, legal and as well as “constructed” (Mahon, 1993), make accountability claims on nonprofits, and these
claims may not always cohere. Thus, nonprofits need to decide which concerns to address and through what mechanisms.

In response to accountability issues, scholars, policymakers and nonprofits themselves have invested considerable effort in identifying appropriate and effective oversight and governance mechanisms to mitigate agency conflicts and make nonprofits more accountable. Potential policy options include increased government regulation (including more stringent operating and reporting requirements), self-regulation through industry associations, and the use of private accreditation or certification mechanisms. This volume examines the role that voluntary programs, defined as rule-based systems created and sponsored by nongovernmental actors, can play in mitigating agency conflict and resolving agency dilemmas between nonprofits and their principals. We conceptualize these programs as ‘clubs,’ in the political economy sense of the term (Prakash and Potoski, 2006). While the club framework has been employed to study voluntary programs among for-profit firms (Potoski and Prakash, 2009), this is the first book to systematically apply the framework in the context of the nonprofit sector. In doing so, we also extend the club perspective by bringing in the agency theory to explore how principal-agent dynamics influence club emergence, design, participation, and efficacy.

Nonprofit accountability clubs are rule-based institutions that create standards for behavior, regulate membership, and enforce compliance among members. In some cases, they offer certification or formal accreditation. The number of these programs is on the rise (Lloyd 4

Agency relationships can be formal and legal. Here, the principals have legal course to shape the activities of their agents. In some others cases, a given set of actors may construct themselves as principals of some other actors. While such constructed principal might not be able to make legal claims on their agents, they may still be able to shape agent’s behaviors by imposing costs and bestowing benefits.
2005; Lloyd and de las Casas 2005; Sidel 2003; Bothwell 2001). According to the NGO Regulation Network, nonprofit codes of conduct have been developed in over 40 countries. Lloyd (2005) documents 24 different NGO self-regulation and accountability initiatives globally. Gugerty (2008b) examines 32 programs in operation globally; Sidel (2003) documents 17 programs in Asia alone. These programs can take a number of different forms including self-regulatory collectives, third-party accreditation programs, or industry association-sponsored programs. We argue that underlying this apparent institutional diversity is a set of common collective action challenges, and that these voluntary programs constitute a common institutional response to these challenges. Below we outline how a deductive, theoretical perspective derived from agency and club theory can add to the study of voluntary programs among nonprofits. Our objective is to develop a generalized approach that can help cumulate knowledge about nonprofit accountability programs across a range of settings.

**Accountability and Agency in Nonprofit Organizations**

An agent is an actor who acts on behalf of a principal (Mitnick, 1982). Agency conflicts arise when agents working on behalf of principals do not act according to the wishes of the principals. Instead, they act in response to their own preferences, which may not align with those of the principals (Berle and Means, 1932, Ross, 1973; Mitnick, 1982; Fama and Jensen, 1983; Moe, 1984; McCubbins et al., 1989; Wood, 1988; Waterman and Meier, 1998; Shapiro, 2005). In essence, preference substitution by the agent lies at the heart of agency conflict.

Nonprofits can be viewed as agents charged with undertaking specific activities on behalf of various principals, particularly donors and governments. Agency dilemmas among
nonprofits, as with other kinds of actors, may arise when the preferences of nonprofits (more specifically, preferences of the key individuals who manage them) diverge from those of donors or other principals, when the preferences of principals are not clearly defined, or when the preference of multiple principals are in conflict.

In this volume, we are most interested in the first category of problem: preference substitution. Governments are increasingly charging nonprofits to provide a variety of public services but have weak regulatory and oversight mechanisms. Private donors often provide funding to nonprofits to undertake specific activities in areas such as education, public health, environment, women’s empowerment, and economic development. While they expect nonprofits to spend these resources judiciously and effectively to deliver services to the target populations, they often do not have the capacities to adequately monitor nonprofits’ operations. Citizens provide resources to advocacy nonprofits with the expectation that they will effectively advocate issues which the citizens care about. Again, they do not have the resources to monitor how their funds have been spent. In sum inadequate monitoring creates opportunities for nonprofits to indulge in preference substitution.

Principals may be inclined to provide resources to nonprofits to undertake desired services because they view them as more ‘trustworthy’ actors. Nonprofits may be viewed as trustworthy because they are constrained from distributing profits to owners – the assumption being that the generation and appropriation of profits makes actors do “bad things” such as cutting back on quality in order to increase profits (Hansmann, 1980; Rose-Ackerman 1996). The absence of the profit motive may be particularly important when organizations produce ‘credence’ goods whose quality is difficult to observe even after purchasing. Of course,
governments do not generate or distribute profits and yet trust in governments is highly variable across countries. Indeed, the literature recognizes that trust may not be a sufficiently robust basis for contracting (Ortmann and Schlesinger, 2003), particularly when principals—such as institutional donors and governments—are themselves accountable to others for demonstrating results. Moreover, it is no clear that the non-distribution constraint will fully constrain opportunistic behavior since it provides only a ‘negative’ protection against potential malfeasance, rather than providing positive incentives for managerial performance (Ben-Nur and Gui 2003). And even in the absence of outright fraud, nonprofits may suffer from ‘goal displacement’ or ‘mission drift’ in which nonprofits operate according to the preferences of managers and boards (themselves unelected), while disregarding the preferences of funders, beneficiaries, or government authorizers (Steinberg and Gray 1993; Ben-Nur 1996; Ortmann and Schlesinger 2003).

As any other category of collective actors, there are “good” and “bad” nonprofits. There is no evidence to believe ex ante that the nonprofit sector is more (or less) prone to agency failure than the public or commercial sectors. However, if there is a non-trivial percentage of “bad apples” (which could mean corrupt or merely ineffective organizations) in the pool of nonprofits, principals have an incentive to identify these bad apples to avoid supplying them with resources. If principals are unable to distinguish between “good” and “bad” nonprofits, they may begin to view all nonprofits with more caution, perhaps even suspicion. In extreme cases, they may become wary of providing any resources lest they fall into the wrong hands. The inability to differentiate nonprofits may depress the overall volume of resources principals are willing to provide to nonprofits. Some studies suggest that in the United States, the costs of
this reduction in resources may be as much as $100 billion a year (Bradley, Jansen and Silverman 2003). Many nonprofits, including the good ones, may be forced to exit the market, or curtail the scale or scope of their activities, a situation that neither the principals nor the nonprofits desire. These dynamics are analogous to the lemon’s market described by Akerlof (1970). When there are information asymmetries between the buyer (principal) and the seller (nonprofit), and heterogeneity in quality of the seller, bad sellers can eventually drive good sellers out of the market.

But even if every nonprofit is ‘good’ and seeks to follow principals’ preferences, goal conflict among multiple principals can give rise to similar agency dilemmas. Governments may care more about equity in the provision of nonprofit services, while institutional donors may care more about responsiveness to their particular constituency (Smith and Lipsky, 1993). When each principal has a distinct contract with the nonprofit, these contracts may differ substantially in their goals. Nonprofits might not be in a position to order these competing demands. When principals are unable to observe whether nonprofits are addressing their concerns, they may again be reluctant to provide resources.

The presence of information asymmetries and multiple principals in the nonprofit sector may result in increased inefficiencies, or agency costs or agency slippages. Principals may stipulate extensive reporting requirements and oversight mechanisms. Furthermore, principals may begin to make only small, short-term grants to nonprofits as opposed to larger, long-term ones.\(^5\) Given the difficulties in observing nonprofit quality, principals are likely to create

\(^5\) Another option might be for principals to establish on-going, collaborative oversight and reporting arrangements with funded organizations; this is the “venture philanthropy” model. Such relationships may help mitigate agency conflicts, but given that the number of such
reporting requirements that are appropriate for the ‘average’ nonprofit. Consequently, the
good nonprofits are likely to be over-regulated while the bad ones are likely to be under-
regulated. Adverse selection problems may follow. If the heterogeneity among nonprofits is
substantial, bad nonprofits might even drive the good nonprofits out of the funding market.
Even if this dire prediction about adverse selection does not come true, agents will be forced to
devote an increasing share of their resources to governance and oversight rather than to
program implementation. Particularly ‘good’ nonprofits that attract funding from multiple
sources may find themselves facing especially high administrative costs; many nonprofits argue
that multiple reporting requirements consume a great deal of organizational time and energy
(Ebrahim, 2005). Short-term funding may lead nonprofits to prioritize short-term projects
where benefits can be demonstrated more quickly, over long-term projects which might have a
greater impact but only in the long run (Henderson, 2002). In sum, in response to agency
conflicts rooted in information asymmetries, principals may reduce the supply of resources to
nonprofit or increase governance costs that constrain nonprofits’ effectiveness.

The anticipation of ‘market failure’ in the philanthropy market gives “good” nonprofits
the incentive to proactively address accountability concerns. Nonprofits may voluntarily
establish (or join) mechanisms that supply informational signals about their internal governance
and activities to their principals along with providing assurances that nonprofits are making
serious effort to conform to the objectives set by the principals (Ortmann and Svitkova, 2008).
By doing so, nonprofits hope to obtain an on-going or increased supply of donor funds, greater
operational freedom, and decreased governance costs. Further, their proactive voluntary
relationships that any one principal can undertake will be limited, it may still have the effect of
depressing the overall amount of funding available to nonprofits.
regulation might dampen the demand for new laws that restrict their activities in even less desirable ways. The next section examines the agency dilemma faced by nonprofits and their principals in more detail and suggests some ways in which voluntary accountability programs among nonprofits may address these dilemmas.

Agency Dilemmas among Firms and Public Bureaucracies

Principal-agent theory derives originally from theories of the firm in which principals wish to contract with agents to carry out specific tasks (Alchian and Demsetz, 1974; Holstrom, 1982). Problems can arise because principals can observe only outcomes and not the full effort of agents. If unanticipated or unwanted outcomes are observed, principals may have difficulty distinguishing the extent to which bad luck or malfeasance contributed to the outcome. To overcome these obstacles, principals can attempt to write detailed contracts, but contracts typically cannot cover all contingencies. Principals can engage in costly monitoring, but will likely always face some agency losses because of asymmetric information. Principals may thereby attempt to minimize these losses using additional mechanisms including screening and selection of agents prior to contracting or institutional design that includes built-in checks and balances (Kiewert and McCubbins, 1991).

Among firms, shareholders, as providers of capital, are the principals who attempt to exercise control over the agents (managers) through the board of directors. While the firm is accountable to several “stakeholders” (Freeman, 1984), in the final analysis, shareholders are the ultimate principals because they have the claim over the residual. Because agency conflict leads to a reduction in the residual, shareholders have incentives to monitor agents. The firm,
therefore, devises mechanisms (with varying levels of success) to align agents’ preferences with those of the principals, with the objective to maximize the production of the residual. The most common strategy is contract design: agent compensation is tied to performance.

Where agents are unable to refuse a contract and face multiple competing principals, however, agency dilemmas can be conceptualized as a problem of delegation, analogous to the dilemmas faced by Congress and the President, both of whom wish to control the actions of bureaucrats. Public agencies cannot refuse to contract with Congress but may exercise substantial autonomy in the implementation of policy. In this case the competing principals tend to focus on monitoring, procedural controls and the development of institutional checks and balances to reduce agency costs and exert influence over agents (Miller, 2005). Monitoring may take two forms. Principals can engage in expensive ex post monitoring and hearings, or ‘police patrols,’ or they can rely on lower cost ‘fire alarms’ – complaints from constituents when they are not receiving what they want from bureaucrats (McCubbins and Schwartz 1984). Another option is to focus on procedural rules and the professionalization of agency staff with the goal of making the procedural aspect of bureaucratic action more transparent to all sets of principals (Moe, 1987). The focus is on legitimacy of procedures, rather than control of outcomes (Miller, 2005). Alternatively, principals can rely on institutional design, agreeing to a set of checks and balances in the bureaucratic process that ensure that no one principal can gain undue influence over outcomes. Thus, in the context of public organizations, agency

6 In the U.S. context, this focus on procedures assumes the existence of interest groups with the interest in monitoring the activities of bureaucrats and a court system that can enforce procedural mandates (Miller, 2005).
dilemmas often give rise to procedural mechanisms of control, rather than to more expensive monitoring mechanisms.

**Agency Dilemmas among Nonprofits**

We have noted how governance among private firms in market economies tends to rely on contract design between shareholder-owners and manager-agents to address problems of hidden information and hidden action. The effectiveness of contract design is supported by the institutional environment of the market. Share value is publicly available information. Unhappy shareholders have mechanisms through which they can discipline managers. They can use “exit” (divestiture) as well as “voice” (voting out the board) (Hirschman, 1970) to signal their appreciation or displeasure regarding agency issues. Contract design is not perfect, of course: shareholders are collective actors who face collective action dilemmas in monitoring managers and managers can game the system by artificially inflating share value and then selling their options (Gourevitch, 2002). Market institutions provide additional control. An active market for corporate control provides another venue for “discipline” (Manne, 1965). Third party ‘reputational intermediaries’ that include stock analysts, investment banks and bond rating agencies, provide outside information on the performance of managers.

Nonprofits, on the other hand, do not have shareholders. They do not have a well defined primary principal with claim to the residual and, therefore, with incentives to monitor and restrain agency conflict. Furthermore, nonprofits cannot distribute the residual even if they were to generate it (Hansman, 1980). Unlike firms which seek to maximize the residual, nonprofits commonly pursue multiple goals, a condition which accentuates their agency
problems since the claims of their various principals are not ordered in any clear or consistent way (Johnson and Prakash, 2007). The external institutional environment does not help nonprofits to mitigate agency issues either. For one, nonprofits are not embedded in institutions (such as the stock market) where standardized evaluations of performance help to assess agent behavior (Spar and Dail, 2002). Instead, nonprofits face multiple, sometimes conflicting, claims of accountability from a variety of actors (boards, donors, host governments, and members), each wanting nonprofits to be assessed in their own particular institutional setting, and with their own preferences as benchmarks.

In this way, nonprofits are analytically similar to public bureaucracies, in that they are collective agents that face demands from multiple principals exerting varying amounts of influence and control. Unlike public agencies, however, nonprofit principals are rarely ‘warring’ over alternative outcomes (Moe, 1984). Congress (and political parties), the president and bureaucrats are all relatively well informed of each others’ identity and interests, while nonprofit principals may even not be aware of each other’s identity. Nor are principals typically concerned with controlling the overall agenda of the nonprofit. Rather, each principal has an interest in ensuring that its own particular preferences are addressed. But nonprofit principals, unlike Congress and the President, cannot rely on judicial enforcement of procedural requirements, nor can they rely on interest groups with vested interests to monitor the activity of nonprofits. Nonprofit beneficiaries can seldom vote with their dollars as can customers and shareholders, and often cannot exercise voice, as can Congressional constituents. This raises additional accountability concerns for nonprofits because their beneficiaries cannot signal their pleasure or displeasure in obvious ways.
This analysis suggests that agency dilemmas in nonprofits, while analogous to those in the public and private for-profit sectors, will exhibit substantial differences. Given the context of multiple principals with individualized agendas, weak institutionalization of public information and reporting requirements, and the lack of a constituency with either purchasing or voting power, nonprofits and their principals have every incentive to develop mechanisms for reducing agency losses. But in the context of multiple principals and multiple goals, contract design will be a limited tool. The development of institutions that provide checks and balances as well as public information is a long-term process. The options in the short- and medium-term are therefore likely to focus on the development of mechanisms for monitoring and reporting and institutions for screening and selection. In particular, nonprofits have incentives to develop signaling mechanisms that provide a reputational signal to principals. Principals might also prefer to rely on a reliable signal of quality rather than engage in expensive monitoring. But nonprofits and their principals may differ on how this signaling is to be accomplished. Institutional donors may want a more specific signal that ensures that nonprofit activities are aligned with their funding priorities. Governments want to ensure that nonprofits are serving charitable purposes that justify their tax-exemption. Individual donors want a straightforward mechanism for identifying worthy organizations for giving. Nonprofits, on the other hand, would like a signal that is credible for multiple stakeholders. In this way nonprofits might avoid having to face ‘police patrols,’ either in the form of individualized reporting requirements for multiple donors, or in the form of stricter government regulation. How can these competing interests best be met? What constitutes a credible signal? What kinds of information must it contain?
Signaling as a Response to Agency Dilemmas

The economics literature has long examined problems of signaling under conditions of asymmetric information. The classic treatment is Spence’s (1974) discussion of labor market signaling. Since true information about the quality of potential employees is not fully visible to employers, job applicants have incentives to find signals of quality. A college education is one such signal. Since high quality individuals will find it more costly to obtain a college education than low quality individuals, a college education serves as a signal of quality, regardless of whether a college education actually improves employee productivity. Education induces a ‘separating equilibrium’ in which ‘good’ and ‘bad’ types are revealed.

Where pre-existing signaling institutions do not exist, however, signal-seekers, such as nonprofits, face the challenge of creating credible signaling institutions. To do so, they must ascertain what type of signal induces a separating equilibrium that distinguishes high quality from low quality nonprofits. In other words, what kind of signal establishes sufficient information on reputation? A second challenge has to do with who will bear the costs of constructing the signal and how the flows of information will be coordinated. The institutional design of voluntary signaling programs must solve both the external credibility problem and an internal collective action problem.

Among for-profit firms, two types of signaling institutions have arisen, both of which are responses to market failures. First, firms may join voluntary certification programs to signal their adoption of policies that internalize the negative externalities of production, such as such as reduced pollution or emissions, higher labor standards, or the use of environmentally-
friendly or sustainable cultivation and harvesting practices. Voluntary environmental programs work by encouraging ‘beyond compliance’ behavior on the part of firms and, sometimes, by making information on compliance public. In return for participation, program participants receive the value of a positive reputation for which stakeholders can choose to reward them (Prakash and Potoski, 2006).

Second, firms may join voluntary programs in response to problems of asymmetric information between sellers and buyers, when buyers cannot fully observe supplier quality. Voluntary certification programs such as ISO 9000 (King, Lenox, and Terlaak, 2005; Potoski and Prakash, 2009) and ISO 14001 (Prakash and Potoski, 2006) can help firms to communicate their adoption of particular management practices to potential buyers. The problem of asymmetric information between firms and customers is analogous to the information asymmetries faced by nonprofits and their principals. Creating a credible signal implies that the cost of program participation must be sufficiently high that low quality organizations do not participate. In addition, the institution must be able to ensure that participants do not shirk in meeting the program obligations. To return to our job market example, universities have degree requirements and grades to certify graduates. How do voluntary programs certify their members? Previous work on voluntary programs sought to strengthen the analytics of for-profit voluntary programs by employing a common, deductive framework rooted in club theory (Prakash and Potoski, 2006). Extending the club theory perspective to nonprofits raises interesting and important questions about the design of accountability institutions. In particular, how do key features of nonprofit governance, structure, and context affect the
emergence, design, and participation in voluntary regulation programs? The next section turns to these questions.

**Voluntary Clubs among Nonprofits**

In economic theory, clubs are rule-based institutions that create benefits that can be shared by members, but which non-members are excluded from enjoying.\(^7\) Clubs thus function to produce and allocate impure public goods, i.e. goods that can only be created or enjoyed collectively. Such goods are neither fully private (in which case they could be provided by markets) nor fully public (in which case it would be impossible to exclude others from enjoying them). Club goods are excludable goods that are non-rival within the club. Excludability means that it is feasible for one actor to exclude others from appropriating the benefits of a good for which the actor has contributed resources; in the case of clubs non-members can be excluded. Without excludability, other actors have an incentive to “free ride,” that is, to enjoy the good’s benefits without contributing to its production, maintenance, or protection (Olson, 1965). Rivalry means that if one actor consumes a particular unit of a good, it is no longer available for another actor to consume: if I am eating an apple, then you cannot eat the same apple. Among club members, all participants can enjoy the benefits of club membership. Clubs can therefore be viewed as institutions that provide excludable, collective benefits for members. In the case of nonprofit clubs, the club good being produced is a reputational signal of nonprofit quality that distinguishes high quality from low quality nonprofits. Thus, an actor (such as association

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\(^7\) The literature on clubs is large. Key contributions include Tiebout (1956), Wiseman (1957), Buchanan (1965), and Cornes and Sandler (1996).
of nonprofits), might establish an institution (a voluntary program) which produces positive reputation or signal (a club good) for its members.

Voluntary programs as clubs perform three functions (Prakash and Potoski, 2008). First, they require club members to adopt policies and undertake activities that go beyond what is legally or operationally required of them. These activities and policies are tied to outcomes that nonprofit principals care about. Second, by requiring members to undertake these activities, clubs impose non-trivial membership costs on members; these costs create the separating equilibrium and therefore form the basis for the reputational signal created by the club. Third, to compensate members for incurring new costs, the club provides benefits. The most important benefit, the benefit of a good reputation or ‘brand,’ has characteristics of a club good because all members can benefit from it at any given time, but it is available only to members and cannot be appropriated by nonmembers.

By joining a voluntary program, nonprofits agree to incur the costs of adopting new governance mechanisms. This signals to principals that nonprofits are serious about tackling agency conflict. Thus, voluntary club membership provides information about practices and management systems that principals cannot observe and therefore helps to mitigate information asymmetries between principals and agents. Further, because club membership is a public declaration of the intentions of a nonprofit, reneging on its club obligations imposes ‘audience costs’ (Fearon, 1994). Thus, club membership also provides assurance to principals that agents have incentives not to renge on their obligations.

Principals may welcome voluntary clubs because they serve to reduce the monitoring and enforcement costs that principals might otherwise face. Arguably, voluntary clubs also
produce positive externalities for society that flow from the effective use of funds provided by the principals. These externalities might include building social capital (Putnam, 1993), providing citizens with civic experience (Almond and Verba, 1965; Verba, Brady and Scholzmann, 1995), and providing goods and services that are underprovided by markets and government (Weisbrod, 1988). However, these social externalities, by their very nature, are not captured by participating nonprofits and therefore cannot serve to draw nonprofits to clubs.

For members, club membership creates two types of benefits: branding (collective) benefits and private benefits (Prakash and Potoski, 2006). Branding benefits, the central analytical feature of voluntary clubs, accrue to club members only and are a key incentive for joining the club, since non-participants are excluded from enjoying them. These benefits manifest as goodwill, funding, contracts, or other compensation that members receive from their principals in response to their club membership. These benefits are tied directly to the credibility and strength of the signal produced by club membership. For example, club members often receive a certification that enables them to advertise that they are different from non-members by virtue of their club participation. For nonprofits, there are several potential benefits tied to this reputational signal. To the extent that donors and potential members, whether individual or institutional, have difficulty distinguishing among high and low quality organizations, nonprofits have incentives to create credible signals about the quality of their governance and the effectiveness of their programs. There is some evidence that donors are willing to reward club participants with additional funding (Bekkers, 2006). In addition, in countries where government attitudes towards nonprofits are hostile, such a signal may also help protect an organization from unwanted government interference or scapegoating.
(Gugerty, 2008a). In addition to the benefits created through the nonprofit “brand,” nonprofit clubs might provide tangible material benefits to participants that also have the characteristics of club goods. For example, club membership or certification might be a pre-requisite for tax-exempt status or for receiving government grants or contracts.

Participation in a voluntary club may create private benefits through organizational learning. Through complying with club requirements, organizations may find ways to streamline or reduce the costs of other reporting requirements. Compliance procedures may encourage more efficient or effective use of donor or government funds; to the extent that increased effectiveness can be documented, this may in turn lead to both increased funding and higher social benefit. Analytically, however, nonprofits can appropriate such benefits by establishing accountability systems but not formally joining the club. After all, the obligations imposed by such clubs are often quite straightforward. While the benefits of organizational learning might emerge by participating in a club, they can also be generated and appropriated independent of club membership. Unlike branding benefits, they do not have a collective character to them. Thus analytically, private benefits do not constitute the raison d’être for nonprofits to join an accountability club.

If reputational benefits are so important, why don’t nonprofits create them by unilateral action in order to boost their credibility with principals? This might be a lower cost option. In other words, why are signals via clubs more credible than signals by an individual nonprofit? Club membership offers several advantages over unilateral actions for mitigating agency conflict and enhancing reputation with principals (Prakash and Potoski, 2007). From the principals’ perspective, a unilateral declaration by a nonprofit to abide by certain standards is
less credible because when individual nonprofits make and enforce their own rules, they can more easily change them. Further, there is no exit cost in terms of loss of face among peers who have decided to continue in the club.

In contrast, clubs are institutionalized systems whose rules and obligations are often sticky; club membership therefore signals a long-term commitment to curb agency conflict. Second, there are exit costs. When a nonprofit joins a club, it shares the same institutional space with other nonprofits which have taken public vows to fulfill club obligations. Hence, if a nonprofit exits, its absence is quickly noticed in the peer group, and loss of reputation follows. Furthermore, because clubs can also gain from “network effects” (Bessen and Saloner, 1988; Prakash and Potoski, 2006) in building reputations, actions taken as part of a club can do more to boost a nonprofits’ standing with the principals than the same action taken unilaterally.

This raises the issue of how clubs emerge and who organizes or ‘sponsors’ them. In market settings featuring asymmetric information, entrepreneurs are likely to enter the market in order to sell information about suppliers to willing buyers. The profit motive provides the incentive for intermediaries to develop signaling mechanisms. Among nonprofits, however, most voluntary clubs are developed by entities that are themselves nonprofit (Ortman and Svitkova, 2007; Gugerty, 2008b). Are nonprofit clubs more likely to be sponsored by donors, independent third party agencies, industry associations or self-regulatory collectives? Given the impact of public scandals on nonprofit reputation and fundraising, voluntary clubs are likely to be initiated by nonprofit industry associations with a clear stake in maintaining the reputation of the industry. Clubs could also emerge in response to external threats to the
sector, such as the threat of increased government regulation; again in this case we might expect that nonprofit associations would be likely sponsors.

Third-party initiated programs may emerge in response to donor needs (and with donor support) where donors have a strong stake in developing mechanisms that can distinguish legitimate, high-quality nonprofits from ‘lemons.’ These principals may desire signals with stronger separating properties and may favor third-party systems using trusted intermediaries whose reputation depends on the production of quality information (Ortmann and Svitkova, 2007; Biglaiser, 1993).

If club emergence is the result of agency dilemmas, the design of clubs may be most responsive to the preferences of the most salient principal. If club standards vary with sponsorship, we may expect to see more than one club emerge in the same policy domain, and perhaps even see clubs competing for members. This also implies that club design may vary across sectors. For example, in nonprofit sectors where organizations are particularly reliant on individual donors and the perceptions of the public for fundraising, club sponsors will be particularly concerned with finding clear and accessible signals of quality that are easily understood by the public at large. This may come in the form of a ‘seal of approval’ or other symbolic gesture. Empirically, however, it is not clear to what extent principals will concern themselves with the actual content or enforcement of the standards that lie behind the seal. In this case, the reputation of club sponsors may be as important as club design.

Clubs composed of similar organizations may be able to more easily create specific signals of quality of interest to key principals. Thus accreditation programs with industry-specific standards have been initiated by the American Association of Museums, the Land Trust
Alliance, and by the Council of Foundations for U.S. Community Foundations. Clubs are also quite common among international development agencies (Gugerty, 2008c). But many of these programs co-exist alongside more general clubs designed to serve all nonprofits.

Where clubs signal are targeted at multiple principals with heterogeneous preferences, it is unclear how standards will be agreed upon. Assuming that each principal provides separate guidelines, the most stringent guidelines may be the appropriate benchmark to assess the level of ‘beyond guideline’ behavior required by the club. The literature on delegation suggests that the presence of multiple principals results in a stronger focus on procedural activities, rather than on measuring outcomes. Procedural signals may also be more likely in broad-based clubs that are open to all nonprofits. Guidelines for such might be extensive (in terms of documentation required and the range of policies and practices covered) but not particularly stringent.

**Mitigating Collective Action Dilemmas in Clubs**

Like any other governance mechanism, clubs are vulnerable to institutional failures if they do not solve their collective action dilemmas. For voluntary clubs, two collective action dilemmas are most salient (Prakash and Potoski, 2006). The first, the Olsonian dilemma, centers on a club’s capacity to create excludable benefits that are sufficient to offset the cost of club membership. In response, clubs must develop brands that create separating equilibrium. To do so, clubs must impose obligations on their participating members that are stringent enough to demonstrate their credible commitment to mitigating agency slippage, yet are reasonable enough that some minimum number of participants is willing and able to pay the costs of
meeting them.

The second dilemma, the shirking dilemma, pertains to a club’s ability to compel participants to adhere to its rules. This is a challenge because participants might have incentives to free ride on the club’s reputation: they could join the program and enjoy the benefits of its reputation, but shirk their responsibility to adhere to its standards. Not all members might shirk. However, is a certain proportion of participants shirk, it might undermine clubs’ credibility with principals. To curb shirking, clubs need to monitor participants’ behaviors and sanctions non-compliance. A club that sets high standards and has a reputation for effectively policing its participants is likely to have a stronger standing among its principals. Thus, the two attributes, club standards and club monitoring and enforcement, are the key institutional dimensions of voluntary clubs.

*Club standards*

Club standards establish the requirements for club membership. Given that principals, including donors and governments, often specify reporting guidelines for nonprofits, club standards can be viewed as establishing the amount of “beyond guideline” behavior required by the program. The amount of beyond guideline behavior required by the club is important because it establishes the credibility of the signal of participant quality and demonstrates the seriousness with which the club seeks to reduce agency conflicts. Nonprofits that are already closer to the standards will incur lower additional costs to join. Thus, the expectation is that high quality nonprofits will be more likely to join voluntary programs, potentially increasing the strength of the reputational signal provided by the club.
For analytical purposes, we can consider two ideal types of standards: lenient and stringent (Prakash and Potoski, 2006). Lenient club standards require marginal effort (above the legal and donor requirements) for potential participants to join the program. These tend to be low-cost clubs. They also tend to have a marginal impact on correcting agency slippages. Consequently, while nonprofits might find it easy join a lenient voluntary club, they should also expect small reputational gains by virtue of their clubs membership.

Stringent club standards impose requirements which are substantially beyond the legal and donor guidelines. The advantage of stringent standards is that the club brand is more credible and can serve as a robust signal of club members’ commitment to reducing agency conflicts. While these are high cost clubs, they can also be expected to create sizeable reputational benefits to their participating members.

Clubs design should take into account multiple, sometimes competing objectives. Ideally, one might want to design a low cost club which creates significant reputational benefits. This is not possible and club sponsors need to be cognizant of this trade off. Further, while stringent standards might enhance the club’s credibility with the principals, they might lead to low membership as well. As a result, such clubs might capture only low levels of network effects and scale economies in building the club brand simply because only a few nonprofits will be able to meet the more demanding membership requirements. Thus, pitching the club standards at a level appropriate for the potential nonprofits and yet acceptable to key principals is an important institutional design issue that the designers of any club must confront (Prakash and Potoski, 2007).

What standards should be set to send an appropriate signal to principals about
nonprofit quality? The determination of appropriate nonprofit club standards is not clear-cut, given the diversity in the nonprofit sector and the lack of clear reporting standards across organizations. The determination of appropriate standards is often hotly contested. The presence of multiple principals complicates the issue if principals vary in their information requirements. For many nonprofit third-party ratings systems, fundraising and other ratios that measure overhead and fundraising expenditures as a percentage of revenues are quite common, in spite of the belief that comparison of such ratios across organizations are meaningless (Bowman, 2006; Steinberg, 1994). Moreover, rewarding organizations on the basis of a narrow set of outcomes can give rise to perverse outcomes as organizations attempt to ‘game’ the system. Given the focus on fundraising ratios, for example, nonprofits have the incentives to organize their reporting in such a way that such expenses are minimized.

Given the lack of consensus on appropriate reporting standards for nonprofits, many clubs may emerge with relatively lenient standards, particularly in the early phases of club development. As an example, in the U.S. context a club might require that members make their IRS 990 tax reports and audited financial accounts public, and may impose certain requirements regarding board governance, such as the number of members or composition of the board. Such requirements do not go significantly beyond legal requirements, but bundled together and made public by club sponsors, they can serve as a signal of quality. A more stringent club might articulate more detailed standards. The Evangelical Council for Financial Accountability, for example, lays out 26 detailed financial and management standards for members. To have any signaling power whatsoever, clubs might clearly articulate the standards for nonprofit behavior,

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8 For the Forestry case, see Sasser et al. (2006)
even if minimal, and make those standards public so that they are available to nonprofit principals to use in judging nonprofit quality. Stronger standards will typically be associated with stronger signals, but the credibility of the signal also depends on enforcement, as discussed below.

*Club Monitoring and Enforcement*

The stringency of standards represents one component of club credibility. The second component is the extent to which clubs can demonstrate that members are complying with standards. Willful shirking among club members can occur because: (1) the goals of the participants and the club sponsors diverge, and (2) participants are able to exploit information asymmetries (regarding their adherence to club standards) between themselves and club sponsors.

Club sponsors can be viewed as agents of the nonprofits, as well as agents of (nonprofits’) principals. One way is to think of club sponsors as reputational intermediaries. If club sponsors can be viewed as agents acting on behalf of (nonprofits’) principals, there is arguably a second order agency problem here: club sponsors may collude with nonprofits to send incorrect signals. They may design clubs in a manner that conveys an impression of stringency (and therefore higher accountability levels) but, in reality, it is lenient. On the other hand, design issues may also occur if principals have not adequately communicated their goals to club sponsors, a likely scenario given that specifying goals not only entails non-trivial investments but also restricts the principals’ discretion in directing how the funds might be used. Here is source of shirking is not the sponsoring actors’ strategic behavior but the laziness
of the principals. Net, multiple principals with heterogeneous preferences also create opportunities for shirking. First, the sponsoring actor may play off one principal against another (a form of willful shirking). Alternatively, sponsoring actors might be genuinely confused as to what to do in response to divergent principal preferences. Either way, information asymmetries can ultimately prevent principals from differentiating program shirkers from non-shirkers and the club signal will be substantially devalued.

One perspective suggests that nonprofits may not be subject to the same collective action problems as firms because of the centrality of principled beliefs or values to their actions (Keck and Sikkink, 1998), because of normative sociological pressures for behavior (March and Olson, 1989), or because the actions of managers are more trustworthy since they face a non-distribution constraint (Hansmann, 1980). Such normative beliefs and pressures could potentially mitigate shirking, but it is not clear if they will be sufficiently credible to outside stakeholders. As we noted at the outset, increasing pressure on nonprofits to demonstrate ‘accountability’ and ‘results’ suggest that these normative tendencies are not perceived as sufficiently strong by many stakeholders. In the absence of credible normative pressures, nonprofits, like firms and bureaucracies, will need some kind of enforcement mechanism. Monitoring and reporting in clubs attempts to enhance the credibility of the club signal by providing information about adherence to standards that mitigates between club members and club sponsors as well as between club members and principals. While a reduction in such

\[9\] While analytically, one can draw these fine distinctions, empirically it is difficult to identify which part of shirking was strategic and therefore willful, and which was due to structural factors beyond the control of the agent. Voluntary clubs seek to curb both willful and structural shirking.
asymmetries may mitigate agency conflicts, clubs may also need to incorporate sanctioning mechanisms to further enhance the credibility of compliance.

Voluntary club theory identifies various components (‘swords,’ in short) of effective and credible monitoring and enforcement systems (Prakash and Potoski, 2006). The first component is verification – how do clubs verify that members are complying with established standards? Clubs can use disclosure or transparency requirements that require nonprofits to provide and make public particular information. Alternatively, clubs could require that participants produce documents and certify compliance. The certification could be first-party (self-certification), second-party (peer certification) or third-party (independent agent). Once verification mechanisms have been established, clubs face the question of how to handle cases of non-compliance, the second component of credible monitoring and enforcement. Club sponsors must decide how to respond when organizations are not in compliance. First, they must decide whether to make that information public. In addition, they may need to develop penalties that are imposed on non-compliant organizations. The threat of sanction may be credible because the club sponsors have a vested interest in ensuring the club’s credibility. At the same time, club sponsors may not want to acquire a reputation of being harsh and adversarial. They may want to promote organizational learning which can only happen if organizations are willing and able to report mistakes. In clubs sponsored by nonprofits themselves, there may be a fear that public sanctions will identify ‘bad apples’ that weaken the reputation of the sector as a whole. In addition, club sponsors may arguably have a greater impact if they retain nonprofits with imperfect compliance in the club because they can retain leverage over these nonprofits’ policies. Enforcement mechanisms may run the gamut from weak to strong: the weakest
enforcement is asking club members to pledge their adherence to the code, without actual verification. Stronger enforcement might involve some form of self- or peer-verification or certification, with the very strongest clubs relying on third party certification. Clubs may make public the names of those organizations that do not provide required information or are found to be out of compliance, or they may be removed from the club.

The strength of voluntary accountability clubs among nonprofits is thus comprised of two features: standards and enforcement. The strength of clubs can be seen as a continuum from very weak to quite strong, depending on the mix of standards and enforcement employed. Figure 1 below lays out an analytic typology for nonprofit clubs and illustrates how principals will view various combinations of standards and swords that give rise to weak or strong clubs. The reduction in agency loss or agency slippage is expected to be smallest in clubs with lenient standards and weak swords; such clubs are analogous to ‘fire alarms’ since their monitoring mechanisms typically rely on complaints, rather than institutionalized reporting. These are low cost clubs that may be able to attract larger numbers of participants but are likely to create only marginal branding benefits for participants since they are likely able to identify only extreme cases of malfeasance. Such clubs typically have standards that are relatively broad and aspirational in nature and include only minimal monitoring mechanisms. Agency losses will be better reduced in strong clubs; these clubs feature stringent standards and significant enforcement, such as third-party certification mechanisms.

As we discuss below, many nonprofit accountability initiatives are very weak clubs, but they meet the most minimal definition for a club: they impose certain obligations on members (no matter how lenient) and seek to convey this to outside principals (no matter how
imperfectly). Another key feature of the clubs we study is that nonprofits make a conscious choice to participate in them, and this participation is voluntary. Thus, ratings systems (such as Charity Navigator) established by watchdog agencies are not clubs in the sense we employ the term because nonprofits do not make a conscious decision to “join” them. Thus, the collective action issues (the Olsonian and shirking problems) which are key elements in our theoretical approach are less relevant for these rating systems.

In spite of the hurdles to collective action we outline, nonprofit accountability clubs continue to emerge and strengthen, suggesting that they have a role to play in mitigating the information asymmetries that plague relationships between nonprofits and their principals. While the prevalence of these initiatives is by now well documented, there is little systematic cross-program analysis to provide consistent data on the emergence and structure of nonprofit clubs, the impact of sponsorship on club design and effectiveness, and the kind of club benefits they produce for members. Moreover we know relatively little about the potential unintended consequences of their development or about the effectiveness of these voluntary programs in shaping nonprofit behavior.
**Figure 1**

Analytical Typology of Nonprofit Clubs

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<thead>
<tr>
<th>Club Standards</th>
<th>Weak</th>
<th>Strong</th>
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<tr>
<td><strong>Lenient Standards</strong></td>
<td>Costs: Low joining cost</td>
<td>Costs: Medium cost to join</td>
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<td></td>
<td>Benefits: Marginal branding benefits</td>
<td>Benefits: Moderate branding benefits</td>
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<tr>
<td></td>
<td>Principals’ assessment: Marginal</td>
<td>Principals’ assessment: Moderate</td>
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<td>reduction in agency loss</td>
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<tr>
<td><strong>Strong standards</strong></td>
<td>Costs: Medium cost to join</td>
<td>Costs: High cost to join</td>
</tr>
<tr>
<td></td>
<td>Benefits: Moderate branding benefits</td>
<td>Benefits: High branding benefits</td>
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<td></td>
<td>Principals’ assessment: Significant</td>
<td>Principals’ assessment: Significant</td>
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**Book Outline**

This volume seeks to develop a robust yet accessible theoretic framework that demonstrates how voluntary programs, defined as rule-based systems created and sponsored by nongovernmental actors, seek to mitigate agency conflict and resolve agency dilemmas in nonprofits. The club framework seeks unify disparate work on these initiatives by providing a useful and tractable way to analyze programs across a range of academic disciplines, empirical settings, and institutional actors. In this chapter we have identified a number of questions about the emergence, sponsorship, design and effectiveness of nonprofit accountability clubs.
Given this backdrop, the rest of the volume explores voluntary accountability programs in nonprofits using detailed empirical data on a number of initiatives. The volume is organized around three themes. The first theme examines club emergence. The chapters in this section examine the potential for nonprofit clubs to increase accountability in relationship to current requirements, how and why voluntary initiatives arise, and how key features of their environment affect the prospects for emergence. The second theme pertains to club sponsorship. The chapters examine how the identity and characteristics of club sponsors affect club emergence and design. A particular focus is on the effectiveness of self-regulatory clubs versus those sponsored by third parties. The third section looks at club design and effectiveness. Chapters examine the relationship between sponsorship, participant identity and how club standards and enforcement are set and developed. A key issue that emerges is the relationship between sponsorship, club design and club effectiveness. The volume has twelve chapters, including the introduction and the conclusion. We briefly describe the chapters and their organization below.

Chapter 1, “Nonprofit Clubs: An Introduction,” is co-authored by Mary Kay Gugerty and Aseem Prakash and presents an overview of the book. Drawing on principal-agent and club theory, the chapter outlines the theoretical perspective of the volume and provides a summary of the chapters.

Part I of the volume examines club emergence. Chapter 2, “Filling the Gaps in Nonprofit Accountability: Applying the Club Perspective in the U.S. Legal System” is authored by Dana Brakman Reiser. The chapter examines from a legal perspective the potential roles that voluntary clubs might play in the U.S. context in complementing and supporting enforcement of
legal and regulatory mandates. Brakman Reiser examines the baseline standards for nonprofit reporting relating to financial, organizational, and mission accountability. She argues that financial standards are the most developed, yet still leave room for agency losses. Nonprofit donors and beneficiaries lack legal standing to sue, although large donors may have scope to write contracts with nonprofits enforcing certain kinds of reporting. The observation and enforcement of governance and organizational accountability is even more problematic, she argues. Nonprofits are required upon incorporation to file documents reporting on their governance structure, but subsequent enforcement opportunities are minimal. But it is in the area of mission accountability that Brakman Reiser observes the largest scope for voluntary clubs to improve nonprofit accountability. Currently, baseline standards on how nonprofits report on their mission are almost non-existent, in spite of the fact that the mission forms the rationale for an organization's tax-exempt and nonprofit status. Thus, at least in the U.S. context, Brakman Reiser observes significant scope for ‘beyond compliance’ standard-setting by voluntary clubs.

Having established some sense of baseline standards the scope of nonprofit voluntary club activity, the next two chapters examine the emergence of voluntary clubs. Chapter 3, “Trends and Patterns in Third-Party Accreditation Clubs” is authored by Woods Bowman. Bowman examines the development accreditation and certification clubs in the United States. Paralleling the growth of the nonprofit sector, he finds sharp increases in the number of accreditation programs since 1980. The U.S. landscape is dominated by education and health accreditation clubs that are sponsored by independent agencies. Bowman attributes this to the role of the dominant principal in these sectors, the U.S. federal government. The standards set
by clubs tend to cluster on one of two sets of standards: either quality of services and outcomes, or on governance, finances and fundraising. Voluntary clubs in health tend to focus on the former, while the health field focuses on the latter. A case study of one of the largest health accreditation agencies, the Joint Commission, illustrates the interplay between the U.S. federal government and the accreditation agency in the development of standards and enforcement.

Chapter 4,” Self-regulation at the State Level by Nonprofits: The Membership Association Form as a Self-regulatory Vehicle,” by Mary Tschirhart, examines the emergence of voluntary clubs among state-level nonprofit associations and finds a very different story. Given that the vast majority of U.S. nonprofits are locally-based, statewide associations might be expected to develop voluntary clubs that respond to state-level principals, including state attorney generals’ offices. Seventy percent of states have state-wide nonprofit associations; out of these 35 states, twenty have developed codes of conduct for the sector but only five associations sponsor clubs that include any active screening or monitoring. Tschirhart examines the reasons underlying these patterns and finds that neither nonprofit sector size, state association capacity nor association membership in the National Council of Nonprofit Associations are associated with club development. In a federal system such as the U.S., and given the potential discussed by Brakman Reiser for clubs to act as important complements to state regulatory activity, the relatively weakness of state-level clubs is somewhat of a surprise. But as the next two chapters argue, this may stem in part from the conflicting incentives in these associations.
Part 2 of the volume examines club sponsorship and design. The empirical chapters focus on clubs sponsored by nonprofit associations as a form of self-regulation. A common theme is the tension that exists in these organizations between the desire to recruit and support membership and the need to develop signals of quality that external principals find credible. Dennis Young examines the development of nonprofit ‘infrastructure’ organizations in Chapter 5, “Nonprofit Infrastructure Associations as Reluctant Clubs.” He studies two organizations, the Independent Sector and the Nonprofit Academic Centers Council (NACC), that in their early years were largely concerned with professionalization and field development. In more recent years, however, both associations have faced demands from nonprofit principals for stronger quality certification mechanisms. In recent years, the Independent Sector has developed a weak club in which nonprofits can sign on to a code of ethics developed by the association; the code and its signatories are posted to the organization’s website. As Young describes, the association’s accountability initiatives over the last five years have been in larger part a response to initiatives by Congress to increase the regulation of the nonprofit sectors. In contrast, the NACC has resisted pressure to become an accreditation agency and continued its focus on the legitimation of the field of nonprofit studies. Young is pessimistic about the ability and the utility of such infrastructure organizations developing stronger accountability clubs since they recruit and reflect such a broad-based and diverse set of institutions. It remains to be seen whether the initiatives such as that of the Independent Sector are a sufficiently credible signal to government regulators.

Foundations are an interesting case, since they are resource dependent and do not face the same kind of conflicting demands from multiple principals faced by many service and advocacy nonprofits. Frumkin shows how accountability clubs among foundations developed as a response to proposals for increased government regulation and as a mechanism for maintaining foundation autonomy. Like the Independent Sector case discussed by Young, the Council on Foundations was motivated to develop principles for conduct only when faced with the threat of government regulation. In part, this reluctance also stemmed from the difficulty of promulgating standards covering a wide variety of organizations, and in fact, the development of standards led to a schism in the field with a number of foundations forming a competing association. While he describes and acknowledges the shift towards club sponsorship among both national and regional level associations of foundations, Frumkin, like Young, is pessimistic about the potential and ability of foundation associations to sponsor strong accountability clubs.

Chapter 7, entitled “Do Self-Regulation Clubs Work? Some Evidence from Europe and Some Caveats from Economic Theory,” is co-authored by Andreas Ortmann and Katarina Svitkova. This chapter examines the development of a voluntary club in a post-transition economy. The Czech Donors Forum (CDF) was established to promote philanthropy and trust in the nonprofit sector. To accomplish these goals, CDF set out to develop a self-regulatory mechanism for members. As Ortmann and Svitkova argue, however, the CDF has consistently resisted pressures for transparency in its own reporting as well as resisting demands for more stringent standards and enforcement for the self-regulatory club. Drawing on the economics of certification and signaling, they show how self-regulatory institutions contain incentives that mitigate against the development of strong clubs, and suggest that the CDF club may be a
transitional phenomena, on route to the development of third-party certification clubs more common in western Europe.

The third section of the volume examines club design and effectiveness across a range of settings. In Chapter 9, “NGO Accountability Clubs in the Humanitarian Sector: Social dimensions of club emergence and design,” Maryam Deloffre explains the divergent paths taken by two humanitarian accountability clubs in the wake of post-Rwanda evaluations of humanitarian activity. Humanitarian agencies form an important test case for the clubs framework, since their claims to legitimacy are strongly rooted in a normative principles, often described as the humanitarian ‘imperative.’ She outlines how principals stressed the need for third-party certification mechanisms, which were resisted by agencies on the grounds of this imperative, particularly around the principle of independence. She argues that the inter-agency evaluation that took place stimulated an intense period of self-reflection in the sector, and that how agencies interpreted demands for accountability and the humanitarian imperative ultimately influenced club structure. One set of agencies favored a strong ‘beyond compliance’ approach with respect to legal duties and obligations for humanitarian assistance as well as detailed standards for quality assistance, resulting in the Sphere Humanitarian charter. The other set of agencies did not believe that humanitarian agencies could meet their moral duty by means of technical standards, and this group split off to form its own accountability program, the Compas Qualité. This club is organized around a set of 12 principles and members are to engage in a systematic process of self-reflection on these questions, designed to lead to organizational learning and enhanced effectiveness. Deloffre’s chapter shows how norms and ideas can play an important role in structuring club design in this space.
In chapter 9, “The Impact of Club Sponsorship on Club Design,” Angela Bies also examines the development of two competing clubs in the state of Minnesota, one sponsored by the Minnesota Council of Nonprofits (MCN), a membership association of nonprofits and the other by the Minnesota Charities Review (MCR), a charity watchdog agency. From its inception, MCR has had a focus on monitoring charities on behalf of donors. In relation to the MCR, the MCN is a more recent creation. The MCN focuses on improving the operations and effectiveness of its members and advocating for the sector. Until recently, the MCR rating system was non-voluntary; the association established accountability standards, reviewed organizations against those standards, and made the results of those evaluations public. In 1994, MCN began to develop its own detailed set of principles for nonprofit accountability, but explicitly decided against having a monitoring or enforcement mechanism, since the goals of the principles were educational. At the same time, the MCR began to establish its own voluntary accountability club, the Accountability Wizard. This club incorporated the basic principles that had formerly been used to rate charities, but participation was now voluntary. The development of these two parallel clubs appears to be a function of cooperation, rather than contestation. A notable feature of the Minnesota case is thus the way in which these two associations ultimately cooperated to ‘divide up’ the accountability landscape in the state.

Chapter 10, “The Emergence and Design of Nonprofit Clubs in Africa,” by Mary Kay Gugerty, examines the development of accountability clubs in sub-Saharan Africa, a region that has witnessed an explosion in the number and scope of nonprofits over the last two decades. The need for signaling mechanisms in this region is critical, since rapid nonprofit growth has taken place in an environment characterized by relatively weak regulatory capacity and
resource scarcity. In this environment, flows of donor funds to nonprofits tend to attract the attention of both well-intentioned and opportunistic actors, threatening the reputation of legitimate organizations. In response to scandals and the lack of regulatory oversight, governments in Africa have often proposed new regulations for the sector that are often quite repressive in nature. This threat of new regulation is key factor in the development of accountability clubs in this region and Gugerty shows how clubs are more likely to emerge where governments propose new regulation. The desire by nonprofits to protect their autonomy often leads to the development of national level clubs sponsored by nonprofit associations, which tend to suffer from the same tendencies towards weak standards and lenient enforcement noted by Young, Tschirhart, and Frumkin. A novel feature of the African story is the attempt at government-nonprofit partnerships in which governments essentially outsource regulatory activities to these associations, accompanied by some minimal regulatory authority. In these cases, the potential for clubs to send signals of quality depends on their ability to screen and monitor members, since participation is mandated. Most national clubs, however, ultimately proved quite weak in terms of their regulatory power and therefore their ability to send credible signals to nonprofit principals. In response, nonprofits in a number of countries initiated voluntary certification clubs that seek to establish more stringent standards along with monitoring and enforcement intended to send more credible signals of nonprofit legitimacy and quality. Thus, as in the humanitarian sector and in Minnesota, parallel programs often co-exist side-by-side.

The final empirical chapter, “The Benefits of Accreditation for Fundraising Nonprofits,” by René Bekkers, examines the impact of charity certification on donor giving and on the
fundraising revenue received by certified organizations. He studies the Central Bureau on Fundraising (CBF) charity accreditation program in the Netherlands. The CBF is an example of a strong club that elaborates detailed standards that are verified by the CBF before the accreditation seal is issued. Using detailed national-level data, Bekkers shows that individuals who are aware of the CBF program give more to charity, a clear indication that voluntary clubs can increase the faith of principals in the nonprofit sector. He also shows that certified foundations increase their fundraising revenues in the years following accreditation, indicating the strong clubs can induce principals to reward nonprofits, allowing clubs to deliver important club goods to their members. Interestingly, Bekkers also finds that the CBF tends to be ‘leaky’ – nonmembers as well as members benefit from the accreditation program, albeit not to the same extent.

Chapter 12, “Conclusions: Nonprofit Accountability Clubs” is co-authored by Aseem Prakash and Mary Kay Gugerty. This chapter pulls together the theoretic and empirical findings of the various empirical chapters. In so doing, it highlights the strengths and weaknesses of the club approach to understanding nonprofit accountability programs, and highlights areas for future research.
References


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