



Review Paper

Mechanisms for generating credibility in nonprofit organizations

Stephen John Beaumont

Centro de Tecnología para el Desarrollo (Cented), Buenos Aires, Argentina
info@cented.org

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Abstract

In recent years, the great increase in the relative importance of Nonprofit Organizations (NPOs), also referred to as Civil Society Organizations (CSOs), in key areas such as health, education, human rights, culture and others that have a favorable impact on social development, entails greater responsibility in leadership and management of these organizations. Beyond the specific increase in the number of NPOs that exist in each country, they have also diversified their scope of activities, moving from more traditional areas such as health and education, to more innovative areas such as the development of alternative energies in isolated populations or evaluation of police forces. Today, there is practically no human development area where these organizations do not actively intervene. By increasing the number of organizations and the thematic areas they attend, there is a consequent increase in their share in the provision of public and private goods, occupying niches that previously belonged to the State or commercial organizations. This, in turn, implies a significant increase in several variables such as economic income, resource mobilization, number of organizations' stakeholders, media exposure, political influence, etc. All this favors a greater scrutiny of NPOs, both from their own stakeholders as from the public in general. In fact, the scrutiny by the stakeholders is usually fairly fair, or at least based on greater equity, since they usually have more information, mainly due to the need for it for decision making. On the other hand, the general public, while aware of the existence and, to a greater or lesser extent, of the work of these organizations, are often plunged into prejudices, both positive and negative, which alter the possibility of reaching a valid and substantiated conclusion. This is where transparency and accountability become decisive strategic decisions for the credibility of the nonprofit sector.

Keywords: Nonprofit Organizations, Transparency, Accountability, Credibility.

Introduction

As in nature, where species that occupy the same ecological niches compete for resources, the same thing happens in the world of Civil Society Organizations. In the case of these organizations, they compete for donors, volunteers, geographic areas of influence, media coverage, state subsidies, representations of international organizations, agreements with other institutions, getting the best candidates in the labor market, advertisers, sponsors, and even beneficiaries. What makes an organization more “attractive” than others? In the field of fundraising theory, it is said that donations depend, beyond the potential donors' ability to contribute, on commitment to the cause and trust in the effectiveness of the donations. With regard to the commitment to the cause, it will be in the nature of each person to determine with which causes they commit themselves: care of the environment, eradication of poverty, primary health care, etc. No one can cover all the causes. Their priorities will depend on individual and generally private preferences. Organizations can hardly establish competitive strategies with others that advocate markedly dissimilar causes. Instead, they do compete to demonstrate efficiency in resource management within a subset of organizations working on the same subject matter.

One of the ways in which an organization stands out over its peers is through credibility. Not only must they fulfill their mission, that fulfillment must be visible and credible.

So how is an organization credible? Through the exercise of transparency and accountability, Civil Society Organizations will be able to approach this objective. The next challenge for civil society organizations that want to excel is precisely this: be transparent and accountable efficiently.

Credibility, Trust and Legitimacy

The term “moral hazard” or “post-contractual opportunism” originates in the insurance industry and refers to the tendency of people who purchase insurance to alter their behavior in ways that are burdensome to the insurance company, such as taking less care to prevent the occurrence of an incident.

In economics, it refers to inefficient behavior within the framework of a contract, arising out of the different interests (or conflicting interests) of the parties involved in that contract and that exists only because one party cannot determine exactly whether the other party is complying or not with the agreement in the contract.

Problems of moral hazard often arise in principal-agent relationships, where one party (the agent) is called upon to act on behalf of another (the principal). This occurs because the interests of both parties often differ and the principal cannot determine how well the agent has acted and whether the agent has been honest.

An important instance of moral hazard is labor relations, where employees may tend not to carry out their responsibilities optimally. As F. Taylor once said, "It is almost impossible to find a competent employee who does not spend a considerable amount of his time studying how slow he can work and still convince his superior that he is working at a good pace."

This problem also occurs in management levels, albeit in a different way. The typical problem is not that managers of a company do not work enough, but have a tendency to pursue their own goals that are not necessarily the best for the company or for shareholders (for example, seek to obtain better representation expenses).

For there to be a moral hazard problem, three conditions must be present: i. There must be potential divergent interests between people. Conflicts often occur due to the scarcity of resources: what one party gets, the other does not. ii. There must be a profit in the exchange or another form of cooperation between the individuals (some reason to generate a transaction) so that the divergent interests are activated. Up to this point, it would be enough with the classic market rules, since divergent interests exist in most transactions and yet these develop normally, without being affected by the problem of moral hazard. iii. The third, and most critical condition, is that there must be difficulties in determining whether the terms of the contract have been fulfilled and, in addition, to be able to force these terms to be fulfilled. These difficulties often arise because monitoring actions or verifying reported information is expensive or even impossible. They can also appear when both parties know that some contract term has been violated but this fact cannot be corroborated by a third party with decision power (such as a judge or mediator)¹.

While there are ways of controlling moral hazard, these usually involve increasing the resources for monitoring or verification. Sometimes the way to prevent inappropriate behavior is to detect it before it happens. Although monitoring requires the development of sources of information about the agent's veracity and performance, this does not always imply an expense of resources. One possibility is to rely on competition between different parties with conflicting interests to generate the required information. Mintzberg defined it as "control by opposition of functions"².

In many circumstances, monitoring the behavior or veracity of reports may simply be too expensive to make it worthwhile. However, it may be possible to observe the results and provide incentives for good performance by rewarding these results.

Unfortunately, the perfect connections between unobservable actions and observable results are very rare. In general, the behavior of people only determines the results in part and it is impossible to isolate precisely what the effect of that behavior is¹.

For these reasons, many Civil Society Organizations have an important advantage over market and state organizations in the provision of public and private goods, since it is estimated that the probability of occurrence of moral hazard or post-contractual opportunism will be lower in these organizations because of the principle of non-distribution of the financial surplus.

This is mainly due to questions related to the fact that non-profits are endowed with a clause that gives an important signal: it is not possible to redistribute income derived from their activity, there is no residual income. With this restriction of non-distribution, it is intended to give consumers and donors a guarantee of trust³.

Likewise, this reasoning is often extended to its leaders, since the honorability and legitimacy of the governing bodies of associations and foundations are presumed to be non-profit-making⁴.

The issue of the imperative need to generate trust is also mentioned in the Transparency Report of 2008, "Transparency of Non-Governmental Organizations," of the organization Chile Transparente (Chilean Chapter of Transparency International):

It is essential that NGOs generate public confidence to be a viable sector and that they can fulfill their objectives responsibly. These entities receive contributions from public, international and private sectors and Chilean citizens, so the public has the right to know if they are conducting themselves in an efficient and ethical way. The consolidation of this public trust depends on the degree of transparency with which NGOs work, reporting on their management and preventing fraud and other abuses. The members of their boards have a responsibility to ensure compliance with these obligations⁵.

With respect to trust, Fukuyama defines it as the expectation that arises in a community with an orderly, honest and cooperative behavior, based on norms shared by all the members that integrate it. These norms can refer to questions of "deep value," such as the nature of God or justice, but also encompass deontological norms such as professional norms and codes of conduct⁶.

In the case of many services provided by Civil Society Organizations, the information asymmetries between service providers, those receiving them and those who control them are very important, so that trust becomes a critical component. To quote Andrés Alonso, "the altruistic halo that surrounds the activities developed by these organizations usually materializes

in a moral guarantee that resources will be allocated efficiently. As a general rule, the activities carried out by these organizations and the people who work in them receive an important support from society³”.

Monopolies, externalities of team production and information asymmetry are factors that create barriers in the efficient resolution of social dilemmas. The result is that individuals may find themselves spending much more time negotiating a solution to a problem of group inefficiency than what it really is worth. This, in turn, becomes an argument in favor of hierarchy. An asymmetric assignment of authority to direct the behavior of others allows us to impose results that could never be efficiently negotiated⁷.

Now, do these arguments suffice to justify an asymmetric assignment of authority in favor of Civil Society Organizations to direct the behavior of others as regards the provision of public and private goods?

One of the main theories that try to explain the origin of these organizations is the Theory of Market and State Failure. This theory was developed by the economist Burton Weisbrod to try to reconcile the persistence of Non-Profit Organizations with classical economic theory⁸.

The starting point for this theory is the “failure” of the market in producing a sufficient quantity of public goods. Public goods are goods that are available to all, regardless of whether or not they have paid for them, like for example: street lighting, an environment without pollution, safety for all citizens, etc.

In fact, classical economics not only recognizes this limitation on the part of the market but this is the main justification for the existence of the State. But, in turn, the State also has limitations in producing enough public goods. The reason for this, according to Weisbrod, lies in deciding what public goods should be produced and in what quantities. In democratic societies these decisions will reflect the preferences of the average voter, leaving many with needs not covered. Faced with this situation of dissatisfaction of needs by a part of the population, they will turn to nonprofit organizations to provide those public goods that neither the market nor the State are able to provide.

Ortmann and Schlesinger, in their article “Trust, repute and the role of non-profit enterprise,” examine the “confidence hypothesis” and agree with the assertion that asymmetric information can in itself explain the domain of non-profit organizations in certain markets⁹.

In dissidence with these authors, Hansmann argues that the existence of a sector dominated by Non-Profit Organizations cannot be attributed simply to the problems of asymmetric information. However, he does acknowledge that “in the case of efficient organizations (in terms of costs), even a slight potential

for additional trust could justify, and perhaps cause, their existence¹⁰”.

Without wishing to delve into the debate of which percentage of organizations exist due to the “trust hypothesis,” it is clear that it is not a minor issue. In fact, this is demonstrated by various conclusions in various works on the subject, such as the following:

In the “Yearbook 2009 of the Third Sector in Catalonia, Spain,” it is stated that “social organizations will be able to develop their missions better insofar as they can maintain and expand the social trust that legitimizes them in their task.” But we are also reminded that “social trust is difficult to obtain but, instead, it is very easy to lose. Any doubts in the management or practices of the entities can result in a loss of support¹¹”.

This point is fundamental, since the loss of trust is an issue that frequently affects other organizations.

Today there are more non-governmental development organizations than ever and the funds they manage have grown substantially over the last twenty years. Some of these funds come from individuals and entities that pay taxes, make donations, etc., and these people and organizations deserve the maximum respect and transparency. In addition, we must bear in mind that the potential malpractice of a few organizations can damage confidence in the sector as a whole¹².

In Spain, the image of the non-profit sector fluctuates between a high level of confidence in relation to the rest of the institutions and the lack of knowledge about the management of these organizations. When an issue of corruption appears in the press, both the causal organization and the rest are affected because the public lowers the level of confidence deposited in them¹³.

As Sorj points out, “there are sectors of civil society that are state appendices and others depend on the private sector. The assumption about the autonomy of civil society is not always confirmed; in many countries, civil society organizations have become a means by which political parties, parliamentarians, unions or social movements, among others, channel public resources for their own benefit”. According to this author, “as a consequence, we cannot understand civil societies in Latin America outside the context of political and social dynamics in each country¹⁴”.

And it is at this point that debates about transparency and accountability appear as mechanisms to regain that confidence.

Citing once again the “Yearbook 2009 of the Third Sector in Catalonia, Spain”, we see that “Transparency and accountability are key elements in the social sector. In order to maintain and expand the social trust that legitimizes the task that the organizations develop, it is necessary to involve society. Accountability tools such as reports, websites, audits, ethical codes, etc. are increasingly present in the sector¹¹”.

Voluntary accountability infuses credibility with partners and other stakeholders. Credibility is the result of relying on the organization for the results it obtains and the policies and practices used to obtain them. "The more confidence a nonprofit organization can generate, the greater its influence in society will be. The more information the organization provides, the greater the link it will establish with the partners and the greater the trust it will generate¹³".

In fact, the interrelationship between trust and transparency and accountability is indissoluble.

"For nonprofit organizations transparency and accountability are in their genes, in their origins. It is related to trust¹⁵".

"Transparency and accountability are closely linked to social and institutional trust in the social initiative¹⁶".

The credibility of Civil Society Organizations is also related to their legitimacy.

According to Michael Edwards, the legitimacy of an organization is defined as "the right to be and do something in society, the logic that an organization is legal, admissible and justified in its course of action¹⁷".

In the work of the Latin American Association of Organizations for the Promotion of Development (Mexico), this subject is raised, arguing that "legality and legitimacy are not the same and this is sometimes confused. The first comes from a state decision. The second is a result of the relationships and actions undertaken by each CSO. It does not depend on the "propaganda" that each organization makes about itself¹⁸".

Another example is the one cited in the article "Transparency and Accountability of Civil Organizations in Mexico", published in the Mexican Journal of Sociology, which states that "the legitimacy and acceptance of civil organizations among stakeholders and the society in general is of great importance, both for the purposes of extending the values and principles that underpin those organizations, and for the possibility of access to sources of financing¹⁹".

In the paper "Accountability: from transparency to social legitimacy," from the Ecuadorian Center for Environmental Law, it is stated that "Talking about transparency and accountability necessarily means talking about legitimacy. Conceptually, legitimacy can be understood as the perceptions of different stakeholders that the existence, activities and impact of CSOs are justified and appropriate in terms of social values and institutions²⁰".

In another work of the Observatory of the Third Sector, Pau Vidal maintains that "To increase the capacity of advocacy of the Third Sector in any of its areas of action, it is necessary to continue working actively to maintain its legitimacy as a

relevant social agent. This construction of legitimacy depends on many factors, like the coherence between the institutions' way of working and their mission and values, transparency and accountability, quality of work, impact of actions, etc²¹".

Conclusion

As stated previously, Civil Society Organizations compete for donors, volunteers, geographic areas of influence, media coverage, state subsidies, representations of international organizations, agreements with other institutions, getting the best candidates in the labor market, advertisers, sponsors, and even beneficiaries.

And one of the main ways in which an organization stands out over its peers is through credibility. And this credibility is harder to obtain as more organizations are created and issues of corruption tend to appear. Through the exercise of transparency and accountability, Civil Society Organizations will be able to become more credible. The next challenge for civil society organizations that want to excel is precisely this: be transparent and accountable efficiently.

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