

**Collective Action and Private Governance:
Explaining Variation in Nonprofit Voluntary Regulation Regimes**

Mary Kay Gugerty
Daniel J. Evans School of Public Affairs
University of Washington
Seattle, Washington
gugerty@u.washington.edu

Paper prepared for the Public Management Research Conference
University of Arizona
Tucson, October 2007

Draft paper: comments welcome

Please do not cite or quote without author's permission.

1. Introduction

This paper examines the emergence and structure of private forms of governance among nonprofit organizations. These governance structures consist of voluntary codes and certification programs designed to shape nonprofit management and performance. A large literature examines voluntary regulation programs among private, commercial firms, but the emergence of such programs among nongovernmental organizations (NGOs) and nonprofit organizations remains under-researched, in spite of the substantial growth in such programs over the last decade. Voluntary programs among firms arise in part as a response to the potential for opportunistic behavior among profit-maximizing agents. Given that nonprofits are supposed to be trusted agents of the public good, why do such agencies seek to create and join costly voluntary programs that potentially constrain their flexibility and operations? This paper argues that voluntary programs among nonprofits arise when information asymmetries between nonprofits and their stakeholders threaten a failure in the market for nonprofit resources. This threat gives nonprofit organizations the incentive to participate in costly collective action in order to provide signals about organizational quality. Although nonprofits share a number of similarities with firms as collective actors, there are important differences in nonprofit governance and institutional environment that might shape nonprofit voluntary programs in distinctive ways.

The literature on private voluntary programs is focused in large part on voluntary environmental programs (VEPs). The available studies investigate the determinants of program participation and effectiveness, largely within single programs (see King, Lenox and Terlaak, 2005; Delmas and Keller, 2005; Potoski and Prakash, 2004; and Rivera and de Leon, 2004 among many others). Only a few studies have sought to connect the structure of program design

to program participation or effectiveness (Sasser, Prakash, Cashore, Auld, 2006; Darnall and Carmin, 2005). But program design itself might be a response to the particular policy problem or market failure faced by governments, firms or their stakeholders. In addition, with the proliferation of available programs, the decision to participate may involve a choice by firms among several programs, so that the choice of design is intimately related to levels of program participation.

Examining the emergence and design of programs among nonprofit organizations offers the opportunity to make a number of contributions to the literature on voluntary programs. First, comparing nonprofit to for-profit programs sheds light on the impact of institutional context and governance on program emergence and design. While some of the drivers of nonprofit voluntary programs are similar to those of for-profit firms, differences in the policy and regulatory rationale for such programs, in the institutional environment in which nonprofits are embedded, and in organizational governance structures of nonprofit organizations may affect emergence and structure. Second, analyzing program structure across a number of programs permit analysis of how key features of private governance regimes are related to the characteristics of industries and participants.

This chapter addresses these questions with cross-sectional data on eighteen nonprofit voluntary programs. The paper first outlines the motivation for nonprofit programs, characterizing such programs as signaling devices. The paper then examines the domains in which such programs have emerged and their structure and characteristics. Finally, the paper examines the determinants of program structure.

2. Voluntary Programs as Signaling Devices

Voluntary programs are conceptualized as rule-based initiatives that seek to create institutional incentives for participating organizations to adopt specific practices beyond what is legally or administratively required of them (Prakash and Potoski, 2006). These practices are tied to outcomes that are desired by key stakeholders. But by requiring members to undertake these activities, voluntary programs can impose substantial membership costs on participants. The willingness to undertake this costly action provides a signal about firm quality (Darnall and Carmin, 2005). Programs must provide participants some benefit in exchange for incurring the costs of participation. Benefits can be bestowed by program sponsors or by stakeholders. In the case of VEPs, for example, benefits might include regulatory relief or the ability to charge a price premium for environmentally sensitive products.

Voluntary programs consist of two related mechanisms: standards and rules for entry and compliance along with monitoring and enforcement systems that verify conformance with program requirements (Prakash and Potoski, 2006; Darnall and Carmin, 2005). The stringency of program standards creates the informational signal of participant quality, since low quality organizations will find it costly to join programs with high standards. Monitoring and enforcement systems enhance the credibility of program signals by increasing stakeholders' confidence that participants are adhering to program rules.

There are two rationales for voluntary programs among firms, both of which arise in response to market failures. First, participation in voluntary programs can help to remedy market failures that emerge when firms do not have incentives to internalize the negative externalities of production. Voluntary programs help firms provide credible information, or signals, on their performance in producing social benefits, 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. In return for participation (which presumably involves a change in behavior), program participants receive the value of a positive reputation or "brand" 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. The presence of asymmetric information means that buyers cannot distinguish high quality from low quality products (or firms). In such a case, producers of high quality products cannot charge a premium for their product and so withdraw from the market, given rise to problems of adverse selection that result in a market for "lemons" (Akerlof, 1970), even in when suppliers do not engage in strategic, opportunistic behavior. But of course large information asymmetries may also provide scope for opportunistic behavior on the part of suppliers if buyers cannot easily observe the quality of goods or services. Reputation is one mechanism for overcoming this dilemma (Kreps, 1990) but reputational mechanisms work best when interactions are repeated and flows of information are strong (Tirole, 1989).

In cases where reputations cannot be easily built through repeat interaction, firms may search for signaling or certification mechanisms that differentiate firms by quality. Such signaling mechanisms can differentiate firms because low quality firms will find it too costly to undergo certification. Thus participation in voluntary quality certification programs, such as ISO 9000, can provide a signal about firm quality to customers or buyers (Terlaak and King, 2006). This may be particularly important when buyers are physically distant from customers or located in another country (King, Lenox and Terlaak, 2006).

Particular individuals or groups may have incentive to initiate and sponsor such programs. Governments may sponsor programs when the burden of regulatory oversight is high and where the benefits produced by voluntary programs have a strong public rationale. Thus, for example, government-sponsored VEPs are relatively common. Such programs can offer governments a potentially lower-cost, more flexible regulatory tool that produces important public benefits (Fiorino, 2008). In industries where the reputation of one firm can easily tarnish the entire sector, industry associations may wish to sponsor voluntary programs to maintain leverage over the behavior of firms in the industry. Moreover, where firms in a particular industry share common challenges in signaling firm quality, they may find it advantageous to join with similar firms in order to develop more industry-specific standards. Self-regulatory collectives may emerge for similar reasons, but in arenas where no dominant industry association exists. Finally, various third-party stakeholders (particularly NGOs) may initiate voluntary programs in order to affect firm behavior.

Voluntary programs among Nonprofits

A key rationale for many commercial voluntary programs is the regulatory potential of such programs to mitigate the market's failure to internalize negative externalities that arise in the production process. This rationale is unlikely to apply to nonprofits. But nonprofit scholarship does propose two ways in which market failure might encourage the emergence of nonprofit voluntary programs. First, nonprofits can provide public goods when governments "fail" in the sense of providing less of a public good or service than certain constituencies desire (Weisbrod, 1988). Second, nonprofits may emerge in the presence of strong information asymmetries between providers and consumers, particularly where goods are idiosyncratic or

quality is hard to observe. In this situation, suppliers bound by prohibitions on the distribution of profits (the ‘non-distribution constraint’) may be viewed as more trustworthy providers of services (Hansmann, 1980). These asymmetries will be particularly salient in organizations that raise revenues from donors to deliver benefits to third parties– what have been termed “donative” nonprofits (Hansman, 2003; Weisbrod, 1975). In this case, unlike in fee-for-service nonprofits, donors are unable to observe the goods and service produced with their donation. These asymmetries can be exacerbated by large physical or other distances between those underwriting the production of goods and services and those receiving them. To the extent that nonprofit principals, whether individual or institutional, have difficulty distinguishing among high and low quality organizations, nonprofits have incentives to create credible signals about nonprofit quality.

In the presence of such asymmetries, nonprofits, like firms, need to find ways to signal their quality to their key stakeholders. But this raises the question: who are the stakeholders or principals to which nonprofits need to signal? Unlike firms, nonprofits do not have clear ownership structures in which owners, as principals, have claim to the residual. Instead, nonprofits face multiple claims from a number of principals: the boards that advise them, the donors that fund them, the governments that host them, and in some cases, the members who pay them fees (Lynn and Smith, 2007). Complicating the nonprofit signaling problem is the fact that nonprofits do not raise capital through the market, so they are not embedded in institutions (such as the stock market) where common valuations of performance help to drive the behavior of managers across firms in quite different industries (Johnson and Prakash, 2007). Unlike firms, nonprofits commonly pursue “multiple bottom lines.” The presence of multiple nonprofit

principles can be expected to complicate the development of common standards for quality across organizations.

The literature on nonprofit accountability suggests that the claims of donors and governments are often privileged over the claims of beneficiaries and clients (Ebrahim, 2005). Donors and governments are typically the principals with the greatest ability to provide rewards, either through funding or authorization. Governments are key stakeholders for nonprofits; in most countries governments subsidize nonprofit activity through the provision of tax exemptions and tax deductions for nonprofit donors. Governments also contract with nonprofits to provide public services. In the wake of post-9/11 concerns about the use of charities to channel funds used to support terrorism, governments have an even larger concern with nonprofit oversight (Sidel, 2004). For all these reasons, governments may wish to distinguish high quality from low quality nonprofits, but may not have the oversight capabilities to do so.

Nonprofits have strong reasons to provide signals of quality to donors. While the proportion of revenue raised through donations varies widely across countries and across areas of nonprofit activity (Salamon, 2006), in many areas such as international assistance and culture and arts, donations provide a relatively large source of revenue. The need to signal credibility and quality to donors, whether individuals or institutions, gives rise to the fundraising problem (Ortman and Schlesinger, 2003) which is a specific form of the signaling problem described above.

The need for nonprofits to send signals of quality is highlighted by the high level of publicity surrounding public accounts of nonprofit mismanagement (Greenlee et al, 2007; Gibbelman and Gelman, 2004). Such scandals tarnish the reputations of all nonprofits and reduce public confidence in the trustworthiness of nonprofit managers (Bekkers, 2003). The impact of

these reputational scandals is born out by the crescendo of calls for increased nonprofit accountability as well as the tremendous increase in efforts to develop private voluntary accountability programs among nonprofits. Lloyd (2005) documents 24 different NGO self-regulation and accountability initiatives globally. Gugerty (2007) documents 12 country-level voluntary programs in sub-Saharan Africa and Sidel (2003) finds 17 in Asia. The next section examines the characteristics of nonprofit governance and institutional environment in order to generate preliminary hypotheses about the expected patterns in the emergence and structure of nonprofit voluntary programs.

Emergence, Sector and Scope

In what domains are nonprofit programs likely to emerge and who will initiate or sponsor them? The literature on firm programs suggests that signaling programs will be in more demand 1) where firm behavior and the quality of a firm's product is hardest to observe, especially when customers and producers are separated by large distances (King, Lenox and Terlaak, 2006), and 2) when transactions are not repeated and/or goods and services are idiosyncratic (Ortmann and Schlesinger, 2003). By this logic, voluntary programs should be more common among nonprofit industries or types that face higher informational asymmetries, particularly those that serve distant, vulnerable, or hard to reach populations. This could include international organizations, nonprofits that provide non-fee based services to clients and beneficiaries, and those nonprofits that seek to produce hard-to-define products such as "community development" or "empowerment." Such nonprofits face high hurdles in communicating quality to donors, governments and beneficiaries, creating potentially large benefits to mechanisms that can give credible signals about nonprofit quality.

Are nonprofit programs more likely to be sponsored by governments, independent third party agencies, industry associations or self-regulatory collectives? Given the low levels of extant nonprofit regulation, and the lack of clear regulatory and public benefit from nonprofit voluntary programs, we would not expect to observe large number of government-sponsored nonprofit voluntary programs. Given the impact of public scandals on nonprofit reputation, voluntary programs are most likely to be sponsored by nonprofit industry associations with a clear stake in maintaining the reputation of the industry. Third-party initiated programs may be more likely to emerge (with donor support) where donors have a strong stake in developing mechanisms that can distinguish legitimate, high-quality nonprofits from ‘lemons.’ Thus we expect third-party programs in nonprofit sectors that are highly donor reliant.

Are nonprofit voluntary programs more likely to be organized around specific nonprofit “industries” (such as social-service provision, advocacy or international development) or will they encompass the entire sector? A related question is whether we might expect to see nonprofit programs emerge at the national or transnational level. A priori, we would not expect to see a large number of nonprofit transnational programs for several reasons. First, the institutionalization of valuation and performance is much lower among nonprofits than among firms and reporting standards exhibit wide variation across countries, complicating the development of transnational standards. Second, the typical ‘supply chain’ of transactions in the production of nonprofit goods and services is not transnational (an exception is the relief industry, discussed below) so demand for transnational standardization is likely to be lower. Third, donors rarely give unrestricted funds that nonprofits can choose to use at will. Instead funds are given for specific programs located in specific countries and nonprofits are expected to provide information to donors on those specific nationally-based programs. For these reasons we

would not expect to see the emergence of transnational nonprofit voluntary programs. Programs are likely to be national in scope.

Within national boundaries, are programs likely to be organized around industries or to be sector-wide? Here two opposing forces make predictions less clear. The weak institutionalization of nonprofit reporting standards suggests that programs might be more easily formed within particular nonprofit industries (such as relief and development, health, social service delivery, and so forth) where common standards might be more easily developed and trust across organizations may help to facilitate collective action. Similarly, in nonprofit industries where donors play an important role and funding is channeled through industry-specific mechanisms (such as in international development) we might expect to see industry-level programs emerge. On the other hand, governments are also important nonprofit stakeholders and are often the gatekeepers for entry in a given national nonprofit 'market.' Moreover regulatory and reporting policy typically takes place at the national level and is applied to the nonprofit sector as a whole, rather than at the industry level (the U.S. federal system, authority might be delegated to the states). Governments are likely to prefer programs that are sector-wide in scope and may be more willing to provide supportive benefits to such programs. Where government regulation of nonprofits is more centralized and/or where governments are more hostile or suspicious of nonprofit activity, we would expect programs to be sector-wide in scope. Thus we might expect to see more national-level programs in developing country settings or in more centralized, as opposed to federal systems.

To summarize, this discussion suggests several hypotheses about nonprofit program emergence, scope and sponsorship.

- 1) Voluntary programs are more likely to emerge among nonprofits that are highly ‘donative’ in nature, have relatively high levels of reliance on donor funds, serve clients who are distant from donors, and implement programs with outcomes that are hard to observe and measure.
- 2) Programs are more likely to be national than transnational in scope
- 3) Nonprofit programs are most likely to be sponsored by industry associations, rather than governments, although third-party programs may be particularly likely to emerge where donors have strong interest in assessing nonprofit quality
- 4) It is unclear whether programs are more likely to be organized at the industry or the sector level.

The next section explores the key features of voluntary program structure and develops hypotheses about how key features of nonprofit governance and institutional environment affect the structure of voluntary programs.

Nonprofit Governance and Program Structure

Voluntary programs consist of two related mechanisms: standards for entry and compliance with the system, and monitoring and enforcement systems that verify conformance with program requirements (Prakash and Potoski, 2006; Darnall and Carmin, 2005). Standards consist of the rules governing entry and specify the actions required to be in compliance with the program. The more stringent the standards, the more credible the signal of organizational quality, since only high quality organizations can bear the costs of joining the program. At first blush, stringent standards appear preferred to lenient ones, since lower quality organizations will find it more difficult to meet costly standards and stringent standards help avoid adverse selection into

programs (Potoski and Prakash, 2005; Darnall and Carmin, 2005). But stringent standards may be difficult to agree upon and can discourage widespread participation, dampening the total social benefit provided by the program. Lenient standards will create a more attractive program for potential participants, but will not be as effective in distinguishing high quality from low-quality firms or in changing organization behavior.

On average, nonprofit programs might be expected to have weaker standards than for-profit programs, for many of the reasons already discussed, including weak institutionalization of reporting requirements and low oversight of nonprofits in general. The most lenient standards for nonprofit programs are likely to consist largely of broad, aspirational principles for behavior. Medium strength standards might include reporting requirements on basic organizational governance and financial information; for example, this information is required by the U.S. IRS Form 990. Stronger standards would include documentation of specific management practices and detailed financial information. The most stringent standards would require reporting on organizational performance, including both financial and program performance.

Because strong standards are costly to meet, participating organizations may have incentives to 'shirk' on meeting their obligations. Voluntary programs do not operate with the force of law; providing the informational signal requires collective action on the part of participants in producing a public good, since all participants benefit from the positive reputation and none can be prevented from enjoying it (Olson, 1965). Producing a credible signal may therefore require monitoring and enforcement that determines whether organizations are complying with program requirements and sanctions those who are not. The literature available on voluntary environmental programs suggests that programs without strong monitoring or sanctions may suffer from adverse selection (Lenox and Nash, 2003; Rivera and De Leon, 2004;

Delmas and Keller, 2005) and may not be effective in changing firm behavior (King and Lenox, 2000; Rivera, De Leon and Koerber, 2006).

Some nonprofit scholars suggest that nonprofits may not be subject to severe shirking because of the importance of principled beliefs and norms to nonprofit action (Keck and Sikkink, 1998), because of isomorphic and normative pressures (DiMaggio & Powell, 1991; Scott, 1995), or because managers will act in more trustworthy ways because of the nondistribution constraint (Hansman, 1980). Such pressures may help to mitigate shirking, but it is not obvious that these pressures will be sufficiently credible to all stakeholders, particularly in light of the non-trivial incidence of nonprofit malfeasance. Thus nonprofit voluntary programs will require some form of monitoring and enforcement to be credible, and the evidence suggests that most programs are increasingly aware of this.

Monitoring and enforcement mechanisms include three potential features: monitoring and verification mechanisms; rules governing information disclosure, and the specification of sanctions in cases of non-compliance (Potoski and Prakash, 2005). Monitoring mechanisms may include only minimal reporting requirements or may use self-monitoring or self-certification. Stronger programs use sponsor, peer or third-party verification systems in which experts outside the organization certify compliance. The literature on firm programs suggests that programs with strong third-party monitoring can both attract higher quality firms and improve facility environmental performance (Toffler, 2006; Potoski and Prakash, 2005; Terlaak and King, 2006). Stronger monitoring can be expected to produce a more credible signal about participant quality, but stronger monitoring increases the cost of participation for organizations, again potentially limiting program participation. Public disclosure requirements may be able to substitute in part for active monitoring, but such information is less credible when not verified by a third party.

Sanctions can also increase the likelihood that program participants will comply with program requirements. Sanctions might include public censure or disclosure of violations, fines, or possible de-certification or expulsion from the program.

The literature on voluntary programs among firms suggests that industry-sponsored programs will be weaker than programs sponsored by independent agencies (King and Lennox, 2000; although Darnall and Carmin (2005) find few sponsorship does not affect program design or strength) but makes few other predictions about the determinants of program strength. A close reading of the existing literature suggests that national programs may be stronger than transnational programs, since the strongest programs described in the literature appear to be environmental programs sponsored by national regulatory authorities, such as the Environmental Protection Agency's Performance Track program. Transnational programs, such as ISO 9000 and ISO 14001, focus on management standards rather than performance standards and while they include third-party monitoring, they typically do not employ public disclosure or sanctions.

3. Data and Hypotheses

This section evaluates the hypotheses developed above with data on eighteen nonprofit voluntary programs. This dataset represents some of the first available comparable cross-sectional data on nonprofit voluntary programs. Four criteria were used to identify programs for inclusion. First, programs must be inter-organizational in scope. Second, programs must be 'voluntary'; participants must have control over the choice to join. Programs run by 'watchdog' groups are thus excluded. Third, programs must require participants to pledge commitment to the code through a written document and must have some mechanism in place for monitoring participants (at minimum an institutionalized complaints mechanism). These criteria distinguish

voluntary programs from the numerous passive nonprofit codes of conduct in existence. The focus is on programs serving ‘donative,’ rather than fee-based nonprofits. Accreditation programs that serve fee-based organizations such as schools, university, or health-care facilities, are not included (although examining variations in these programs is an important area for future research). These limitations also exclude programs serving membership-service organizations such as unions, professional associations, and other member-support and social groups.

Candidate programs were identified through a comprehensive literature review, web searches, public lists of extant programs, and by interviews with nonprofit managers and industry analysts. Within the definitions given above, nonprofit voluntary programs were considered for inclusion without regard for industry, location, sponsorship or geographic scope. Data on the standards, program requirements, institutional structure and current membership for each program were gathered from a detailed review of program documents and requirements. This dataset, while not fully comprehensive, represents a reasonably representative sample of existing programs.¹ A full list of the programs is given in Appendix A.

Patterns of Emergence and Sponsorship

Table 1 summarizes the characteristics of the programs in the sample. Over half the programs were formed within the last ten years, reflecting the increasing interest in nonprofit accountability. The programs are distributed around the globe, with five in the U.S or Canada four in Europe, five in Africa or Asia, and two transnational programs. The European programs tend to be the older and more established programs. Most programs have remained small in scope, relative to their potential participant base. Only three programs are estimated to include more than half of potential participants in the program.

¹ Central and Latin American-based programs are likely under-represented.

Nonprofit programs appear more commonly national, than transnational in scope; sixteen programs are national in scope, while only two transnational programs could be identified. Not surprisingly, the two transnational programs serve large international development and humanitarian NGOs, whose operations commonly span a number of countries and locations.

In addition to being largely nationally-based, half the programs identified in the sample are based in developing countries, a potentially surprising feature given that broad-based associational institutions in many developing countries are often weak. But the pressures for private governance may be stronger in these settings, since the regulatory capacity of governments tends to be lower and the regulations governing nonprofits relatively underdeveloped or outdated. In many developing countries, the rapid growth in NGO activity has led governments to propose revisions to the laws and statutes governing nonprofit activity, often in ways that nonprofits find threatening or intrusive (Gugerty, 2007). All of these factors may motivate the development of private regulation in these contexts.

Programs are relatively evenly divided between those that are specific to a particular nonprofit 'industry' (such as humanitarian relief) and those that span the nonprofit sector. Ten programs are sector wide, meaning that they are open to all organizations with nonprofit status. Eight programs are industry-specific. Of those eight programs, six are nationally-based programs for NGOs engaged in international development and relief. The prevalence of industry-based programs among international development and relief agencies is not surprising, given the large distances between donors and recipients in such programs. International organizations face large information asymmetries and voluntary programs may be one means by which they can signal quality to stakeholders.

Eleven of the eighteen programs are comprised of international development nonprofits, defined as organizations that either 1) operate transnationally in multiple developing or transition countries or 2) are domestic organizations based in a developing or transition country but receiving funds from international sources. Again, this can be explained as a response to the large information asymmetries facing donors to such programs and the relatively high reliance of international development nonprofits on private donations.

Patterns of sponsorship conform to expectations. There are no examples of government-sponsored voluntary programs. However, in five of the eighteen cases, governments provide a clear mandate for voluntary programs by either conferring limited regulatory powers (typically the power to certify for tax exempt status) on the sponsoring agency or by giving participants privileged access to government funds or partnerships with government. The majority of programs (11) are sponsored by industry associations or quasi-independent arms of such associations. Only seven programs are run by a fully independent agency.

Patterns of Program Structure

The credibility and power of the informational signals sent by nonprofit voluntary programs depend on two features of program structure: the stringency of standards and the strength of monitoring and enforcement. As noted above, program strength will be positively related to the signaling potential of the program. Because costs of participation will be lower for high quality organizations, only those organizations will join stringent programs.

Table 2 shows the main features of program standards and enforcement in voluntary programs. There is substantial variation in the strength of program standards, which range from broad, principle-based standards to more detailed outcome and performance standards, with the

majority of programs having medium or strong standards that focus on financial reporting and management practices. This suggests both the difficulty of specifying common performance measurements across diverse organizations and a tendency for nonprofit programs to focus on the concerns of donors and governments for financial accountability. In addition, a number of voluntary programs are run by associations or collectives in which members have substantial input into the development of standards. This can encourage 'buy-in' on the part of participants, but also makes it more difficult for potential participants to agree on specific standards.

The strength of monitoring also exhibits substantial variation. Two programs have no monitoring or certification mechanisms in place, and two programs use a form of self-certification in which program participants themselves certify compliance with program standards. Nine programs use second-party certification, which consists of having some form of peer evaluation, typically appointed peer evaluators who review the organizational compliance reports. Only five programs use independent, third-party auditors to certify compliance. The use of relatively weak forms of monitoring is the result of several factors: first the use of third-party auditors substantially increases the costs of participation, which could limit the viability of some programs given limited nonprofit resources. In addition, managers of programs run by nonprofit associations often express fears of appearing to be overly 'harsh' on association members, as well as a desire to foster learning among members, which will be more difficult to do if organizations exit the system. These factors may also explain the tendency of nonprofit programs to avoid strong forms of public disclosure; no programs make audit or compliance information available to the public, and only seven programs make public any information at all. Typically, the information revealed in these cases does not go far beyond already existing legal requirements.

Evaluating Patterns of Program Strength

What factors are associated with program structure and strength? In order to evaluate these relationships, the strength of voluntary programs is evaluated by assigning a numeric evaluation of each attribute of program standards and monitoring/enforcement. The full criteria used in the ranking are provided in Appendix B. Program standards are evaluated according to two sets of criteria. First, the level of specificity and detail in the standards was evaluated through a review of program documentation. Programs specifying only broad, principle-based behaviors were awarded one point, while those detailing more specific, process-oriented standards were given two or three points, depending on the level of detail, specificity and number of standards. Those programs that attempt to measure nonprofit outcomes and performance were awarded four points. The second set of scores evaluates the level of documentation required for compliance. Each of those components was awarded one point. The maximum possible score for program standards is seven.

The strength of enforcement is evaluated across three components: monitoring, disclosure and sanctions. Monitoring strength was assessed by characterizing the nature of the verification mechanism for each program. Programs with no formal reporting requirements received 0 points. First party certification in nonprofit programs is characterized by self-certification of compliance by the managers of the organization (1 point).² Second-party review consists of reviews by program sponsors (2 points) or reviews by sponsor-appointed peer evaluators (3 points). Third party certification is conducted by independent bodies approved by the sponsor (4 points).

² Many NGOs are not large enough to maintain fully staffed internal audit or quality control units. Most certification programs do not require such a unit for certification. In some cases, the Board of Directors is required to sign off on the self-certification.

Programs received an additional point if compliance is formally monitored on a periodic basis and another if periodic random audits are undertaken.

Disclosure policies are assessed by examining program rules on public disclosure of application status, compliance information, and complaint status (1 point each). One additional point is given if the program maintains a permanently staffed complaints board and/or has a clear, written publicized complaints procedure. Finally, the use of sanctions is evaluated by assessing whether the program has a credible option for a sanctioning or removing non-compliant organizations, whether such action had ever been undertaken, and whether sanctions are made public. The maximum monitoring and enforcement score is fourteen.

Together, the evaluation of standards and enforcement allows us to characterize the 18 programs according to their strength. Program strength is evaluated in by program scores on 1) stringency of standards, 2) strength of monitoring and enforcement mechanisms and 3) overall program strength. Table 3 summarizes the scores.

The paper next examines variation in patterns of program strength by industry, geographic scope, sponsor, and characteristics of membership. Table 4 presents the results, which compare mean program scores by program characteristics. As an example, the first row compares the scores for standards, monitoring and overall program strength for industry-level versus sector-level programs. A two-tailed t-test is used to assess whether mean scores differ significantly between these two types of programs. In this case, they do not. Program strength also does not vary between national and transnational programs.

The largest impact on program strength is through sponsorship. Programs that are sponsored by independent agencies are significantly stronger in terms of standards, monitoring and overall program strength. Programs serving international development agencies tend to have

somewhat lower strength than programs serving domestic agencies or a mixed constituency, although the test for strength of standards is significant only at the 10% level. Some international development programs, particularly those located in developing countries, may find it difficult to develop strong standards because of the mix of organizations in the program, which typically include both large international NGOs, local affiliates of international organizations and smaller domestic nonprofits.

The data also suggest a tradeoff between the level of program participation and program strength. Programs in which more than 50% of eligible nonprofits participate are substantially weaker than the programs with more limited participation. The programs with wider participation are all sponsored by industry associations and participation in the voluntary program is a condition of association membership. Industry programs linked to industry association membership involve a clear tradeoff. These programs encourage widespread participation, but at the cost of program strength and signaling effectiveness.

Finally, not surprisingly, programs that offer certification or some official “seal” to participants are substantially stronger than those that do not. The provision of certification is more common among programs with independent agency sponsorship, which is itself associated with program strength. Presumably the signaling power of an official ‘seal of approval’ means that sponsors can set higher, more costly standards since the signaling benefit of participation will be higher.

Disentangling the impact of the various program characteristics on program strength is difficult, since many of the explanatory characteristics are themselves related. Table 5 examines the determinants of program strength across multiple characteristics using ordinary least squares regression. Due to the very limited sample size, these results should be interpreted with caution

and interpreted as measures of association, rather than causation. The table indicates that program sponsorship remains positively associated with program strength, even when controlling for other program characteristics. Older programs tend to be weaker than newer programs. This may be because new programs find it easier to establish strong standards and enforcement while existing programs suffer from some institutional stickiness. Finally, the level of program participation remains negatively related to program strength; programs with wide participation are substantially weaker.

4. Conclusions

This paper examined the emergence of private forms of governance among nonprofit organizations by analyzing the development of voluntary regulation programs. These programs are conceptualized as signaling programs formed in response to problems of asymmetric information between nonprofits and their key stakeholders. Data on eighteen voluntary programs is used to examine the relationship between nonprofit governance and institutional environment and the emergence and structure of voluntary programs. The data suggest that nonprofit programs are more likely to be national than transnational in scope and are more likely to emerge among nonprofits engaged in international development. The predominance of national programs is presumed to be a response to the signaling needs of both governments and donors, the strongest nonprofit stakeholders. The predominance of programs serving international development organizations is a response to the high information asymmetries facing these organizations and their primary funders. The most common sponsors of nonprofit voluntary programs are industry associations; programs are rarely sponsored by governments.

Sponsorship is the primary determinant of program strength; programs run by independent agencies are significantly stronger than industry association programs, even when

controlling for other determinants of program strength. Older programs tend to be weaker than programs formed more recently, and programs with wide participation are weaker than more selective programs, suggesting a tradeoff between breadth of participation and signal quality.

The low participation rates in most nonprofit voluntary programs indicate the difficulties of creating and scaling up voluntary programs. Many obstacles to club formation are no different from those in the for-profit sector. Nonprofit organizations and representative industry associations are reluctant to police their peers and are also reluctant to share information when they are in competition for the same donors. The formation of credible programs involves a delicate balance between stringency of standards and the willingness of organizations to join the program. Nonprofits may face some additional hurdles. Many nonprofits have relatively low capacity for monitoring and reporting and few donors are willing to fund these activities. Many nonprofits lack the capacity to comply with minimal program requirements, such as documentation of self-certification. The lack of funding for nonprofits to support their governance and reporting activities makes it difficult for nonprofits to pay accreditation fees limiting the financial base available to support stronger programs. Quite often club sponsors must seek external funding for the development of voluntary programs, since high participation fees would crowd out most nonprofits. Finally, the existence of multiple nonprofit 'principals' complicates the development of specific standards, since each principal may desire a different type of signal.

This paper has focused largely on describing the institutional structure of nonprofit voluntary programs. To fully understand their rationale and effectiveness, we need better information on who joins these programs (and who does not) as well as more nuanced ways of evaluating both the benefits of club membership and the impact of participation on nonprofit

behavior and performance. In addition, more concrete measures of the costs of participation could help in understanding both participation decisions and the level of benefits provided by the programs. Future work should also compare the types of programs studied here with other forms of voluntary accreditation comprised largely of nonprofits, such as educational accreditation programs and with voluntary programs that include both commercial firms and nonprofit organizations.

The analysis presented here suggests that nonprofit voluntary programs are unlikely to become a credible substitute or even complement to government regulation in the near future, in contrast to many commercial programs. First, the rationale for nonprofit voluntary programs has little to do with public or social benefit. Nonprofit voluntary programs may produce social benefits as a positive externality of operation, but such benefits are not the primary focus of these programs. Instead these programs seek to provide private benefits for nonprofits in the form of higher funding and government benefits. Second, the size of most programs remains too limited to provide sufficient regulatory coverage. In cases where participation is wider, programs are typically quite weak. There are exceptions to this pattern, however. The Netherlands accreditation program has been able to scale up quite quickly and evidence suggests donors are willing to trust the credibility of its signal (Bekkers, 2006).

The signaling model presented here can provide a coherent institutional explanation of the structure of nonprofit voluntary regimes. This incentive-based approach to understanding voluntary programs, however, could be supplemented by norm- or learning-based approaches that may be particularly important in understanding mission-based nonprofit behavior. For example, the literature on NGO advocacy and accountability politics indicates that verbal commitments made by international actors can be used to pressure them to change their behavior

(Keck and Sikkink, 1998; Fox and Brown, 1998). The same tactics could be applied to NGOs, and there are an increasing number of watchdog groups doing so. Moreover, as nonprofit voluntary programs proliferate they diffuse new norms and raise the standards for judging nonprofit behavior and performance. The full impact of private governance programs among nonprofit may therefore include the ways in which these programs raise the bar for generally accepted monitoring and reporting behavior among nonprofits.

References

- Akerlof, G. A. 1970. The Market for 'Lemons': Quality Uncertainty and the Market Mechanism. *Quarterly Journal of Economics* 84 (3): 488–500.
- Bekkers, Rene, 2006. “The Benefits of Accreditation for Fundraising Nonprofits.” Paper prepared for the annual ARNOVA conference, November, 2006.
- Bekkers, Rene, 2003. “Trust, Accreditation and Philanthropy in the Netherlands.” *Nonprofit and Voluntary Sector Quarterly*, 32(4),
- Darnall, Nicole and JoAnn Carmin, 2005. “Greener and Cleaner? The Signaling Accuracy of U.S. Voluntary Environmental Programs.” *Policy Sciences*. 38:7 1-90.
- Delmas, Magali and Arturo Keller, 2005. “Free Riding in Voluntary Environmental Programs: The case of the U.S. EPA WasteWise Program.” *Policy Sciences*. 38: 91-106.
- DiMaggio P. and Powell, W. eds, 1991. *The New Institutionalism in Organizational Analysis*. Chicago: University of Chicago Press.
- Ebrahim, A. 2005. *NGOs and Organizational Change: Discourse, Reporting and Learning*. Cambridge: Cambridge University Press.
- Fiorino, Dan, 2008. “Environmental Performance and Green Clubs: A New Tool for Governance?” In Prakash, Aseem and Matthew Potoski, eds. *Voluntary Programs: A Club Theory Perspective*. Forthcoming, MIT Press.
- Gibbelman, Margaret and Sheldon Gelman, 2004. “A Loss of Credibility: Patterns of Wrongdoing Among Nonprofit Organizations.” *Voluntas*, 15(4).
- Greenlee, Janet, Mary Fischer, Teresa Gordon and Elizabeth Keating, 2007. “An Investigation of Fraud in Nonprofit Organizations: Occurrences and Deterrants.” *Nonprofit and Voluntary Sector Quarterly*, forthcoming, 2007.
- Gugerty, Mary Kay, 2007. “The Emergence of NGO Self-Regulation in Africa.” Paper presented at the Symposium on Nonprofit Self-Regulation in Comparative Perspective, University of Washington, March 2007.
- Hansmann, Henry B. 1980. The Role of Nonprofit Enterprise, *Yale Law Review*, 89: 835-898.
- Hansman, Henry B. 2003. “The Role of Trust in Nonprofit Enterprise.” In *The Study of Nonprofit Enterprise: Theories and Approaches*. Helmut Anheier and Avner Ben-Nur, editors. New York: Kluwer Academic Publishers.

- Johnson, Erika and Aseem Prakash, 2007. NGO Research Program: A Collective Action Perspective. *Policy Sciences*, forthcoming, 2007.
- Keck, M. and Sikkink, K. 1998. *Activists Beyond Borders: Advocacy Networks in International Politics*. Ithaca: Cornell University Press.
- King, Andrew A. Michael J. Lenox and Ann Terlaak, 2005. "The Strategic Use of Decentralized Institutions: Exploring Certification with the ISO 14001 Management Standard." *Academy of Management Journal*, 2005 48(6): 1091-1106.
- King and Lenox, 2000. "Industry Self-Regulation Without Sanctions: The Chemical Industry's Responsible Care Program" *Academy of Management Journal*. 43 (4)698-716.
- Kreps, David, 1990. "Corporate Culture and Economic Theory." In *Perspectives on Positive Political Economy*, K. Shepsle and J. Alt, eds. Cambridge: Cambridge University Press.
- Lawrence Lynn and Smith, Steven Rathgeb, 2007.
- Lenox, Michael, 2006. "The Role of Private Decentralized Institutions in Sustaining Industry Self-Regulation." *Organization Science*. 17(6): 677-690.
- Lenox Michael J. and Jennifer Nash, 2003. "Industry Self-Regulation and Adverse Selection: A Comparison Across Four Trade Association Programs." *Business Strategy and the Environment*. 12: 343-256.
- Lloyd, R. 2005. "The Role of NGO Self-Regulation In Increasing Stakeholder Accountability." One World Trust, www.oneworldtrust.org.
- Ortmann, Andreas and Mark Schlesinger, 2003. "Trust, Repute and the Role of Nonprofit Enterprise." In *The Study of Nonprofit Enterprise: Theories and Approaches*. Helmut Anheier and Avner Ben-Nur, editors. New York: Kluwer Academic Publishers.
- Potoski, Mathew and Aseem Prakash, 2004. "Regulatory Convergence in Cross-National Regimes? Cross-National Adoption of ISO 14001 Certifications." *Journal of Politics*, 66 (3), 885-905.
- Potoski, Mathew and Aseem Prakash, 2005b. "Covenants with Weak Swords: ISO 14001 and Firms' Environmental Performance." *Journal of Public Policy and Management*.
- Potoski, Mathew and Aseem Prakash, 2005a. Green Clubs and Voluntary Governance: ISO 14001 and Firms' Regulatory Performance. *American Journal of Political Science*.
- Prakash, Aseem and Mathew Potoski. 2006. *The Voluntary Environmentalists: Green Clubs, ISO 14001 and Voluntary Environmental Regulations*. Oxford: Cambridge University Press.
- Rivera, Jorge, Peter de Leon and Charles Koerber. "Is greener whiter yet? The Sustainable Slopes Program after five years." *Policy Studies Journal* 34.2 (May 2006): p195(27).

Rivera, Jorge and Peter de Leon. "Is greener whiter? Voluntary environmental performance of western ski areas." *Policy Studies Journal* 32.3 (August 2004): p417(21).

Sasser, Erika and Aseem Prakash, Benjamin Cashore and Graeme Auld, 2006. "Direct Targeting as NGO Political Strategy: Examining Private Authority Regimes in the Forestry Sector." *Business and Politics*, 8(3): 1-32.

Scott, WR. 1995. *Institutions and Organizations*. Thousand Oaks, CA: Sage Publications.

Sidel, M. 2003. Trends in Nonprofit Self-Regulation in the Asia Pacific Region. Paper presented to the Asia Pacific Philanthropy Consortium.

Sidel, Mark. 2004. *More Secure, Less Free?: Antiterrorism Policy and Civil Liberties After 9/11*. Ann Arbor: University of Michigan Press.

Terlaak, Ann and Andrew King, 2006. "The effect of certification with the ISO 9000 Quality Management Standard: A Signaling Approach." *Journal of Economic Behavior and Organization*. Vol 60, 2006, 579-602.

Tirole, J. 1989. *The Theory of Industrial Organization*. Cambridge: MIT Press.

Toffel, Michael W. 2006 "Resolving Information Asymmetries in Markets: The Role of Certified Management Programs. Harvard Business School Working Paper 07-023.

Weisbrod, Burton. 1988: *The Nonprofit Economy*. Cambridge, MA: Harvard University Press.

Table 1
Characteristics of Nonprofit Voluntary Programs

	Characteristic	Number of programs
<i>Club and Membership Characteristics</i>		
Club Age	Less than five years	6
	6-10 years	6
	11-15 year	4
	More than 15 years	2
Club Size	More than half of potential members participate	3
	Less than half participate	15
Club location	U.S./N. America	5
	Europe	4
	Developing country (Asia & Africa)	5
	Transnational	2
	Other Commonwealth countries	2
Geographic Scope	National	16
	Transnational	2
Industry Scope	Industry Specific	8
	Sector-wide	10
Sponsorship	Industry Association/Self-regulation	11
	Independent Agency	7
	Government	0
Participation	Nonprofits working internationally or receiving funding from overseas	11
	Domestic nonprofits	3
	Mixed	4
Government backing	None	13
	Govt provides mandate and/or additional benefits	5
		4

Table 2
Program Standards and Enforcement

Program Characteristics		Number of programs
Type of Standards	Broad principle-based standards (weak)	2
	Basic management/financial (medium)	3
	Detailed management/financial (strong)	8
	Outcome/Performance (stringent)	2
Monitoring & Certification	None (complaints only)	2
	First-party (self)	2
	Second-party (peer)	9
	Third-party (indep 3 rd party)	5
Disclosure	Full public disclosure of audit info	0
	Partial disclosure of audit info	7
	No disclosure of audit info	11

Table 3
Summary of Program Strength Scores

	Mean score (standard deviation)	Minimum Score Observed	Maximum Score Observed	Maximum Score possible
Sanctions	0.944 (0.725)	0	3	3
Monitoring and Evaluation	6.11 (2.78)	1	11	14
Strength of Standards	4.33 (1.91)	1	7	7
Total program strength score	10.44 (4.51)	2		21
Benefits score	2.28 (1.13)	1	5	6

Note: Detailed criteria for ranking given in Appendix B.

Table 4
Voluntary Program Characteristics and Strength

Program Characteristics	Number of programs in each category	Stringency of standards (std dev)	Mean Score	
			Monitoring & Enforcement (std dev)	Total Program Strength Score (std dev)
Industry scope	Industry (8)	4.13 (1.89)	6.0 (3.54)	10.1 (5.28)
	Sector (10)	4.5 (2.01)	6.3 (2.20)	10.7 (4.08)
Geographic scope	National (16)	4.44 (1.79)	6.36 (2.54)	10.69 (4.11)
	Transnational (2)	3.50 (3.54)	5.0 (5.65)	8.5 (9.19)
Sponsoring Agency	Independent Agency (7)	5.57** (0.787)	7.71** (2.21)	13.29** (2.63)
	Industry association (11)	3.55 (2.02)	5.09 (2.70)	8.64 (4.61)
Membership Type	International only (11)	3.72* (2.24)	5.63 (2.23)	9.36 (5.04)
	Domestic/mix (7)	5.29 (0.49)	6.86 (1.86)	12.14 (1.86)
Program Coverage	More than 50% of potential (3)	1.67*** (0.67)	3.67* (0.67)	5.33** (1.33)
	Less than 50% (15)	4.87 (0.40)	6.60 (0.72)	11.47 (1.07)
If certification or seal offered	Seal	5.5*** (0.80)	7.66*** (1.82)	13.2*** (2.29)
	No seal	2.0 (1.10)	3.0 (1.26)	5.0 (2.10)

Note: Table cells are mean scores for each category. Standard deviations are given in parenthesis. A two-tailed t-test was performed on the null hypothesis that the two means are equal. Rejection of the null hypothesis of equality is indicated at the 99% (***), 95% (**) and 90% (*) level and these differences are shown in bold.

Table 5
Determinants of program strength
Ordinary Least Squares Regression

Explanatory Variables	Dependent Variable: Program Strength Score				
	OLS estimate with robust standard errors (standard error)				
If sponsor is independent agency	6.91 ^{***} (1.79)	6.44 ^{***} (2.05)	7.67 ^{***} (1.20)	6.98 ^{***} (1.30)	5.08 ^{**} (1.97)
Age of program in years	-0.078 [*] (0.041)	-0.088 [*] (0.047)			-0.063 [*] (0.035)
If program is over 10 years old			-3.96 ^{***} (1.33)	-4.38 ^{***} (1.31)	
If industry-level program	2.16 (2.07)	2.16 (2.02)	2.57 (2.02)	2.61 (1.98)	1.21 1.70
If composed of international development nonprofits		-1.15 (1.90)		-1.67 (1.03)	
If more than 50% eligible orgs participate					-3.62 [*] (1.83)
R-squared	0.37	0.38	0.47	0.50	0.44
No. Observations	18	18	18	18	18

Note: All regressions are ordinary least squares with robust standard error. Significance noted at 99% (***), 95% (**) and 90% (*) level. Because of the small sample size, each regression was re-estimated with outlying values removed; all results hold.

Appendix A – Nonprofit Voluntary Programs in Sample

Program	Scope	Industry Scope	Sponsor	Year initiated	Number of Partic
Interaction Self-Certification Plus (SCP)	National	Industry: intl development	Industry association	2001	160
Interaction Child Sponsorship Certification	National	Industry: international development/child sponsorship	Industry association	2004	5
Australian Council for International Development	National	Industry: international development	Industry association	1997	110
Evangelical Council for Financial Accountability	National	Industry: (evangelical Christian)	Independent agency	1979	2092
Land Trust Alliance Accreditation Program	National	Industry: Land Trusts	Industry association	2006	44
Canadian Council for International Cooperation Code of Ethics	National	Industry: International development	Industry association	1997	90?
Humanitarian Accountability Partnership - International	Transnational	Industry: International human dev & relief	Industry association	2006	2
National Standards for Excellence Institute (SFX)	National	Sector-wide	Industry association	1998, national in 2001	150
Philippine Council for NGO Certification	National	Sector-wide	Independent agency	1999	424
Pakistan Council on Philanthropy Certification Program	National	Sector-wide	Independent agency	2003	121
Uganda Quality Assurance Mechanism	National	Sector-wide	Two industry associations	2007	brand new
Kenya National NGO Council Code of Conduct	National	Sector-wide	Quasi-governmental agency	1993	3000+
Christian Relief and Development Agency, Code of Conduct for Ethiopian NGOs	National	Sector-wide	Industry association	1999	262
International NGO Accountability Charter	Transnational	Industry: International development NGOs	Group of Indep NGOs	2006	11 founders +37, OR +2 if don't count affiliates
Swiss (ZEWO)	National	Sector-wide	Self-reg collective	1940	475
German (DZI)	National and supra-regional	Sector-wide	Independent agency	1992 (1893)	200
Dutch (CBF)	Nation and supra-regional	Sector-wide	Independent agency	1995 (1925)	200
Austrian (OIS)	National	Sector-wide	Foundation/catholic church?	1996	100

Appendix B Explanation of Voluntary Program Scoring

A. Stringency of Club Standards

	(1-4 points possible)
Principle-based broad standards for behavior, organization must 'sign on'	1
Clear process standards used for reporting with moderate level of detail (often largely financial)	2
Detailed process standards used for reporting	3
Outcome/Performance Stds used	4
Detailed elaboration of criteria for judging compliance exists and is accessible	1
Detailed documentation required for reporting/entry	1
Full, documented compliance for each standard required	1

Standards Score (Maximum 7)

B. Monitoring & Enforcement

	(1-5 points possible)
Official self-certification (involving prep of specific report)	1
Desk review of certif doc by assoc	2
Desk review by peers or other 2nd body	3
Desk + on-site review by 2nd party	4
On-site review by 3rd party	5
Annual (periodic) report monitored for submission	+1 addtl
Periodic/random 2nd party audits	+1 addtl
Disclosure (1 point each)	
Public disclosure of application and/or status of compliance	1
Public disclosure of compliance info (partial in most cases)	1
Clear, written complaints procedure, complaints body OR procedure for review of certification	1
Substantiated complaints made public	1

Sanctions (1 pt each)

Credible option of removal	1
Has removal option been exercised	1
Are sanctions made public	1

Monitoring Score (Maximum 14)

C. Club Benefits Provided

Public recognition (website, etc).	1
Certification or Seal of Approval	1
Membership Association Benefits	1
Tax exemption, govt funding or partnership	2
Connections to Donors	1
Benefits ranking total	5