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Abstract:

Private not-for-profit organizations combine characteristics of public sector agencies and private, proprietary firms. In particular, nonprofits must address designated social missions while breaking even financially. This structure underlies the difficulty that nonprofit organizations face in making resource-related decisions: choices that would achieve maximal mission impact may differ from choices that reward the organization financially. Thus, nonprofit managers face trade-offs between mission responsive and financially rewarding actions. This paper considers such tradeoffs in the context of pricing decisions. The paper draws on alternative theories of nonprofit pricing. In one theory, nonprofits are viewed as revenue maximizers, pricing their services to garner as much net revenue as possible to support their organizations. In an alternative theory, nonprofits are conceived as mission maximizers, pricing their services to achieve maximum mission impact within the constraint of financial solvency. The efficacy of these theories is explored through three case studies of organizations offering a variety of services within the context of a local social services federation. Alternative behavioral patterns are found, including pricing to balance financial and mission impacts for each service offering as well as coordinated, strategic pricing policies to achieve overall mission impact. It is clear from all cases observed that nonprofit managers struggle with mission-market tensions as they relate to pricing and that they could benefit from a system to sort through these decisions in ways that resolve these tensions. One case is developed in depth as an exemplar to demonstrate how a nonprofit organization can develop such a system.

Introduction

Structurally, private not-for-profit organizations combine characteristics of a public sector agency with those of a private, proprietary firm. In particular, nonprofits are required to address designated social missions while breaking even financially. As a result, nonprofits are often described as having a “double bottom-line”, that is both a financial and programmatic standard by which their performance is to be assessed (Bell-Rose, 2004; Clark et al, 2004). In fact, from a normative point of view, the notion of a double-bottom line is misleading. Achievement of the mission *is* the bottom line, while financial success may be prerequisite to such achievement. While devices such as double-bottom lines or balanced scorecards (Kaplan and Norton, 1996; Clark et al, 2004) may be helpful management tools, they can be counterproductive if allowed to obfuscate the ultimate criterion of success.

In terms of a positive theory, however, it is less clear how nonprofits actually behave. As organizations have a natural inclination to survive and grow, their managers and leaders are as likely to be judged by standards of organizational sustainability and growth as by any objective measure of mission achievement. This behavioral reality underlies the difficulty that nonprofit organizations face in making decisions with important resource implications (James, 1998). Specifically, choices that would achieve maximal mission impact may differ from choices that reward the organization in purely financial terms. As a result, nonprofit managers and their governing boards require clear focus, strong discipline and appropriate measurements in order to keep to the normatively prescribed path, and they face a variety of trade-offs between mission-responsive and financially rewarding actions.

Certainly nonprofits are not entirely unique in facing mission/market tensions and requiring a clear focus and direction. For-profit businesses and governmental organizations also have missions and must sustain themselves economically. And sometimes business or government executives will, for personal or other reasons, be dedicated to mission in ways that fail to align completely with maximum financial gain or to the prevailing political mandate that drives the allocation of public resources. However, mission/market tension is generally more wrenching for nonprofits because

financial sustenance and mission achievement are less likely to be as congruent as they are in business or government. In business, mission is generally instrumental to the ultimate goals of profit-making and wealth enhancement of owners and stockholders. Thus, missions are often adjusted or reframed with this in mind, usually without extraordinary conflict. In government, agencies are charged with a mission through the same political process that allocates their resources, so tensions between mission and market may be restricted to bureaucratic enclaves that challenge the majority view. For nonprofits, however, financial success is instrumental to the achievement of social mission, while the acquisition of financial resources often requires choices that can limit mission effectiveness. For example, financial success can be enhanced by selling services to those who can better afford to pay, or by promoting causes that are popular with certain donors, although such actions may short change the social mission for which the organization was established. Thus, special tensions are created that can pit organizational prosperity against mission achievement. (For an in-depth perspective and research on the relative centrality of mission in nonprofit economic decision-making, see Brown and Slivinki, (2006)).

The purpose of this paper is to consider how tensions between mission and market manifest themselves in the context of nonprofit pricing decisions and how those tensions might be resolved. Through case studies, we explore the efficacy of two alternative theories (James, 1998). One theory posits that nonprofits simply price their services in a manner that maximizes their net revenue. This is a bureaucratic model premised on organizational sustenance and growth within the constraints of addressing demand in a particular field of service. A second theory posits that nonprofits price their services to maximize mission impact, often forgoing revenue potential in the process of targeting their services. This is a classical view of nonprofits as organizations seeking to achieve maximum social good within financial constraints. We investigate these theories at two levels – at the service level and the organization level. One possibility is that nonprofits follow the same pricing logic for each service. Another possibility is that they mix their logics in order to achieve some combination of mission impact and financial success. In fact, what we find is that our case study agencies tend to use different heuristics without an overall systematic rationale. However, in one case the organization has developed a

sophisticated software-based system to weigh mission and market considerations in its overall program decision making processes. We describe this case in some depth as a prospective prototype for nonprofit organizations attempting to formulate and coordinate their pricing decisions for multiple service offerings.

Literature Review

Mission-market tension is not a new issue for nonprofits. Indeed, it has been examined in various forms over the past three decades, though with much greater attention since the 1990s. The literature on mission-market tensions can be traced to studies of nonprofit-government relations and concerns about “vendorism” in the delivery of social services. Kramer (1981) worried that heavy reliance on government funding in the form of purchase of service contracts would lead nonprofit social service agencies to become service delivery appendages to government and lose their independent perspectives as advocates for improvements in social welfare policy. More specifically, Young and Finch (1977), studying nonprofit foster care agencies, recognized the constraining factors on their mission-related behavior deriving from government per diem funding. However, a general review of research on this subject by Kramer (1987) found “the dysfunctional consequences of agencies receiving public funds [namely] dependency, cooptation and a dilution of advocacy and autonomy, goal deflection and loss of an agency’s voluntaristic character through increased bureaucratization and professionalization” to be “considerably exaggerated” (p.247). Nonetheless, these concerns continued to build and a key study by Smith and Lipsky (1993) expressed alarm over the loss of autonomy by nonprofit social service organizations stemming from contracting with government.

Paradoxically, some research studies have been more concerned with changes in the public funding environment that have driven nonprofit social service organizations towards greater involvement in the *private* marketplace, with other mission vs. market consequences. In particular, Alexander (1999) noted that, especially for smaller and medium sized community and faith-based nonprofit organizations, changes in government policies, including funding cutbacks, cost pressures deriving from new reporting and staffing requirements, opening of competition with for-profit suppliers, and

a more distressed clientele population, have created financial pressures that force nonprofits to make mission-related compromises, including raising prices, retrenching certain services, redirecting services away from the neediest clients, and reducing emphasis on research, education and advocacy for client needs. Indeed, similar coping strategies were documented by Liebschutz (1992) when funding cutbacks occurred during the Reagan administration.

The *State of Nonprofit America* project led by Lester Salamon (2002) made a special point of highlighting mission/market tensions, citing growing reliance and pervasiveness of fee revenues, an increasingly entrepreneurial culture within the nonprofit sector, growing involvement of nonprofits with corporate partners, and intensifying competition with for-profit service providers. With these forces in play, Salamon observed: “The move to the market may thus be posing a far greater threat to the nonprofit sector’s historic social justice and civic mission than the growth of government support before it.” (p.47).

Mission/market tensions appear to take different forms in different fields of service. For example, in social services Smith (2002) highlights increasing for-profit competition, the advent of managed care arrangements, and a new emphasis on performance measurement that requires nonprofits to focus on service output measures to the possible neglect of less quantifiable accomplishments in advocacy or work with more difficult clients for whom it is harder to show results. In health care, Gray and Schlesinger (2002) note that increased competition with for-profit providers, and pressures from third party payers to control costs, have reduced the ability of nonprofits to devote resources to their traditional public service missions such as education and charity care. These researchers cite a convergence in the behaviors of for-profit and nonprofit providers, noting that “Even where nonprofits have maintained their role, they have often found it necessary to respond to the challenges confronting them in the health care field by becoming more like commercial enterprises.” (p.92). Indeed, in the hospital field, the U.S. Senate Finance Committee recently asked pointed questions of major institutions about the nature of their charitable work and the degree to which it may be compromised by market-oriented practices (Trefinger, 2005).

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In higher education, Stewart, Kane and Scruggs (2002) find institutions struggling, in the context of escalating costs, to set tuitions that will allow good students of modest means to attend, and to cope with new for-profit competitors and pressures from corporate funders to commercialize research. Kirp's (2003) in-depth study of the practices of a selected sample of U.S. universities expresses particular concern about the infusion of business values into American higher education.

In the arts, Wyszomirski (2002) cites the uncertainty and instability of government funding, escalating costs, changes in technology and competition with the profit-making sector. Pressures to increase earned income have resulted in "...changes in marketing, more emphasis on entrepreneurial activities, and a sharper concern for cultivating new audiences and new donors" (p.191). These developments are forcing nonprofit arts organizations to continually reconcile their mission foci with market incentives and pressures, and reappraise their relationships with the business sector and with for-profit arts organizations.

Studies of mission/market tensions in nonprofits generally recognize the complexity of the issues and the challenges nonprofit managers face in dealing with them. Dees (1998), for example, argues that nonprofits span a wide spectrum of motivations and interests, ranging from philanthropic to commercial, and that this richness can be a source of innovation and increased capacity so long as social mission is kept firmly in mind. Other authors such as Weisbrod (2004) and Foster and Bradach (2005) complain that nonprofits' pursuit of commercial ventures is diverting these organizations from fulfilling their social missions. A common theme is the need for nonprofits to maintain a clear identity and focus tied to social mission. To do that, various authors cite the need for better means of measuring nonprofit performance in order to reconcile financial and mission-related performance. For example, Bell-Rose (2004) suggests a social return on investment approach and the use of logic models to identify intermediary indicators that lead to desired social outcomes. Anheier (2005) reviews several other generic approaches to nonprofit performance measurement, including Kendall's and Knapp's production of welfare framework, the balanced scorecard, corporate dashboards, benchmarking, and other sets of performance measures developed by umbrella organizations such as Independent Sector, the National Council of Voluntary

Organizations, and United Way of America. And Paton (2003) offers a comprehensive study of performance measurement in “social enterprises”. An interesting dimension of Paton’s analysis is his inquiry into whether performance measurement itself, often encouraged or imposed by outside (market) agents, can compromise mission in the quest of better performance.

Conceptual Framework

While tensions between financial return and mission-achievement in the nonprofit context are problematic, these goals are not necessarily in diametric opposition. Given that nonprofits are intended to address a social mission, financial performance may be viewed as an instrumental variable contributing to that mission. The degree to which financial success is required to achieve mission may indeed depend on the nature of the mission. In some cases, nonprofits may legitimately decide to use their resources in a time-limited manner to achieve some goal, and then disband when resources are depleted. The Markey Trust provides one such illustration where a foundation (Dickason and Neuhauser, 2000) decided to concentrate its grant making for biomedical research over a limited period of time. Similarly, the John M. Olin Foundation is intentionally closing up shop after having financed a generation of conservative intellectual programming (DeParle, 2005). In these and other cases, part of the rationale for the time limitation was to concentrate resources on the mission, to avoid having that mission become obsolete, and to limit spending funds on maintaining the organization.

However, time-limited nonprofits are the exception rather than the rule. (Research by Hager et al (1996) found that approximately one-fifth of deceased nonprofits studied attributed their demise to completion of the organization’s mission.) The classic case of a nonprofit deciding to continue operations once the mission was achieved is the March of Dimes, which adopted a new mission to address birth defects once polio was cured (Bowen et al, 1994). Here the rationale was that the existing organizational infrastructure represented valuable capital that could be effectively redeployed for a new, related mission. Unfortunately, many nonprofits fail to address the desirability of sustainability and growth explicitly. Many organizations die a slow death or slide into dormancy without ever determining if this was the best way to allocate

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charitable resources. Indeed, it is even hard to find official records of what happened to many nonprofit organizations that stopped reporting their operations or filing tax returns (Bowen et al, 1994).

Given that most nonprofits decide, implicitly or otherwise, that ongoing economic viability is a prerequisite to mission achievement, further understanding of their behavior can be developed through the theory of nonprofit organizations as multi-product firms – first proposed by James (1983) and later expanded by Weisbrod et al (1998). In this framework, nonprofit organizations are viewed as producing two kinds of services – those which are profitable and help sustain the organization, and those which directly impact its mission and may require subsidy. If managers of the organization intend to maximize its mission impact while maintaining financial integrity, their challenge is to find just the right combination of these two types of activities. Hence, in each instance they must determine what the objective of each activity is – profit or mission impact – and then design effective policies for its execution.

In reality, nonprofit programs are not easily separated into profit making and mission-focused activity. Rather, many nonprofit activities combine both objectives. For example, a fund raising event may have a community-building objective as well as a financial one. And a mainstream mission focused activity such as providing day care for young children may be counted on to produce a certain level of revenue as well as to achieve a social goal. In all cases, however, the nonprofit manager must deal explicitly with the balance of financial and mission goals and the tensions between them. Thus, while a double bottom line rationale is dubious for the organization as a whole, it commonly applies in some way to the components of activity that make up the nonprofit's overall portfolio of activity. That is, it often makes sense to measure both the mission and financial impacts of individual programs separately, without attempting to reconcile them at that the program level.

Pricing. Nonprofit organizations produce many services for which charging a fee is feasible, i.e., where it is possible, at reasonable cost, to exclude people from consuming the service unless they pay for it. Such nonprofit services include arts performances, museum visits, social service counseling, day care, educational programs, health and mental health treatment services, memberships in YMCAs and JCCs, gift shop sales and

many others. While certain nonprofit products, such as policy advocacy or public art cannot be priced, a host of nonprofit services certainly can. The real questions are whether prices should be charged, and if so, how price schedules should be designed.

From a market incentive viewpoint, any excludable nonprofit service can be priced in such a way as to maximize net revenues, although in some cases (e.g. high fixed costs and modest demand) even a profit maximizing price may result in losses (negative profits; see Young and Steinberg, 1995). Given the decision to produce such a service, a nonprofit manager responding solely to market incentives will likely decide (a) to charge a price, and (b) to set prices in a manner that yields maximum net revenues. From a mission viewpoint, however, the price decision could be quite different. If charging a price substantially contravenes the mission or values of the organization, the mission-driven manager may decide not to charge a price at all. A “Free Clinic” that provides basic health care services to indigent or uninsured community residents is based on the very notion of free care. An endowed museum established as a community resource may have a long standing tradition of free access to galleries that is considered intrinsic to its institutional identity.

In many other cases, however, the imposition of a fee is accepted. Here, the mission-market tension is manifested in the nature of the pricing policy or fee schedule. For example, maximizing mission impact may require serving as many clients as possible. Such services may be associated with “external benefits” that accrue to society at large as well as to the individuals who actually consume the service. Examples include children in pre-school programs, recipients of inoculations for various diseases, clients in therapeutic mental health or substance abuse programs, or visitors to museums. In such cases, mission focus favors a price lower than that which would maximize net revenues (Young and Steinberg, 1995).

Furthermore, a mission-driven pricing policy may wish to differentiate among alternative groups of consumers. Fine arts organizations or institutions of higher education may wish to encourage younger consumers or accommodate lower income community residents. Accordingly, they may wish to tailor price schedules through sliding scales or other differential measures. A net-revenue maximizing price policy might also employ price discrimination so as to better capture the willingness to pay of

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high demanders. But in general, such a market responsive pricing policy would not reflect a prejudice to serve any particular societal group aside from those who can pay.

In order to resolve the mission-market tension in pricing decisions, the nonprofit organization must first decide the particular purpose of any given service or activity. If the gift shop or facility rental program is designed solely for fund raising purposes, then the tension is resolved by recognizing that the rules for profit-maximizing pricing apply. If, on the other hand, the children's concert series or the vaccination program is intended to maximize mission impact then pricing must be designed to serve the target groups and to maximize the net social benefits associated with consumption by those groups.

Often, nonprofits find it difficult to make such a clear differentiation between mission-serving and revenue generating programs. In particular, some programs may serve both purposes. A nonprofit might decide as a matter of policy or fiscal discipline, for example, to run a day care service on a break even basis. This may be an appropriate value judgment in the context of the larger picture of how the organization intends to maximize its overall social impact. In essence, it says that the day care program should maximize its mission benefits within an imposed fiscal constraint. Setting that constraint at zero profits is only one of many possible choices, depending on the availability of financial support from other sources.

Finally, it is worth observing that over time there may be homogenizing forces at work in nonprofit pricing practices. Under intense competition a nonprofit must price its services to permit economic survival, no different from its for-profit or nonprofit competitors. In particular, as traditionally nonprofit service areas open up to for-profit provision, or where government changes the form of its support from supply-side grants and contracts to demand side vouchers and reimbursements, nonprofits often lose the flexibility to differentiate their pricing practices from competitors in order to address mission-related objectives. Nonetheless, the tension between mission and market remains, even if the ability to adjust to mission imperatives is highly constrained.

Recent experiences of the Salvation Army and the American Red Cross illustrate several of the tensions and issues associated with nonprofit pricing. In September 2003, the Salvation Army chapter in Louisville, Kentucky began to charge homeless families \$5 per night after the first week, for staying the night at its downtown shelter. The shelter

policy had a dual purpose: to help alleviate a budget crisis and as “an incentive to pull people out of homelessness” (AP, 2003b). In the Louisville chapter, 12 workers were laid off in that year due to budget pressures which originated in part from accommodating some homeless people at the shelters for several months. Although the \$5 fee was far below the (marginal) cost to house and feed a person for one night, and the shelter makes exceptions for those who cannot pay, the policy faced harsh criticism from the National Coalition for the Homeless. After the story was published in a national newspaper, the local Salvation Army director rescinded the fee (AP, 2003a).

It is clear in this case that the Salvation Army was aware of the tensions associated with charging a fee for staying in the shelter; its designation of a \$5 price was designed to produce some revenue while not impacting seriously on the emergency use of the shelter. However, the organization may have misgauged the level of mission-market tension here, and needed to recognize that any fee at all was going to adversely affect the people it was charged to help. Hence, some other means of raising revenue to alleviate budget pressures was probably preferable – perhaps donations from some of the individuals who objected to the fee policy or from government agencies charged with keeping homeless people off the streets. Without such an alternative, however, imposing the fee might still have been better than having to close down or reduce capacity.

The American Red Cross (ARC) provides two key fee-based products/services: blood products and health and safety education. Blood products are managed centrally by the Biomedical Services department and depend almost entirely on fees. Health and safety education is managed by local chapters and supported by fees and local donations. Both services have lost market share due to competition, leading managers to search for better pricing strategies. Through a series of focus group interviews and a survey of senior managers, Chetkovich and Frumkin (2003) found that mission-market tensions were indeed felt by managers across the chapters and departments, and that the strength and resolution of such tensions varied according to the nature of services, competition in the market, and the impact on the mission.

One strategy used to regain market share was to reduce prices. However, this strategy came at a cost. In exchange for price leadership and a larger share of markets, product quality was sacrificed. Moreover, a serious problem arose from elimination of

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cross-subsidies between more profitable products and less profitable ones – raised access barriers or reduced quality for people in less profitable regions. In essence, decisions based on profit-maximizing pricing generated tensions among managers trying to address ARC’s mission locally.

Chetkovich and Frumkin, (2003) found that the ARC could cope with these tensions in three ways. The first was to adjust product, quality, or provider reliability in order to attract more customers at competitive prices. The second was to depend more on donations. The third was to pursue product and organizational innovations. The ARC case illustrates that tensions in pricing arise from market competition and the strength of these tensions varies with market conditions. However, tensions may sometimes be relaxed without too much compromise in a variety of indirect ways that circumvent the pricing decision and reduce the pressure for additional fee revenue.

Using Metrics to Manage Mission-Market Tensions

As the above experiences with pricing illustrate, a critical aspect of making resource-related decisions in the nonprofit context is to recognize the purpose of each activity as it relates to sustaining the organization financially versus contributing directly to its mission impact. To develop this recognition, a set of simple metrics which translate into specific decision choices might be helpful, for example simple Likert-type scales. Such metrics could serve as practical tools for managers to think about each resource-related (pricing) decision they make, and as research tools to enable scholars to understand the levels of tension present in the operations of nonprofit organizations in different fields and decision contexts.

Consider a youth-serving organization that offers recreational services to teenagers in a low income neighborhood. One pricing decision is to determine how much to charge families to be members of the organization. Choices associated with this decision can be listed on a scale from 1 to 5, according to the degree to which they favor (positive) mission impacts vs. financial impacts. Thus, a manager who is clear about the purpose of the decision will also be clear about what kind of choice needs to be made. See Table 1 which articulates the end-points and mid-point on a 5 point scale that can be useful in the decision on pricing.

Table 1 Mission/Market Scale for Pricing

Scale Value	1	3	5
Mission/Market Emphasis	<i>Mission emphasis</i>	<i>Mixed emphasis</i>	<i>Market emphasis</i>
Decision Protocol	Sliding scale with some prices below marginal cost to accommodate ability to pay	Sliding scale designed to break-even and accommodate differences in ability to pay	Single or multipart pricing at/above marginal cost to produce maximum net revenue
Impact	Maximum participation by target group; possible financial losses	Wide participation limited by financial constraint	Maximum profit/exclusion of low income families

It is interesting that this scale suggests fairly straightforward ways to pursue either purely market-focused goals or purely mission-focused goals. It is the middle of the scale that requires more imagination and creativity. As the table suggests, this point may be characterized by setting limits on acceptable mission and economic impacts and then searching within these limits for desirable options. Of course, the scale in itself does not indicate what decisions should be made. But it helps to accomplish two things: It forces decision-makers to specify their goals for any particular decision and, given these goals, it suggests what kinds of choices to make and what their impacts will be. It still remains for managers to put all the pieces together so that the sum total of their decisions puts the organization in its desired position of mission impact vs. financial success within its constraints of economic feasibility.

Table 2 illustrates various possible patterns for nonprofits with a range of services for which pricing decisions are made, ranging from revenue maximizers to mission maximizers. In this table, mission-focused managers select mission maximizing pricing strategies for each priced service they offer, revenue-focused managers select pricing strategies that maximize revenue for each service they offer, while mixed-focus managers choose a combination of these strategies, pricing for mission where mission impact potential is high and pricing for revenue where income potential is high. Note that these

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are possible behavioral models, useful for describing observed nonprofit managerial decision making, not necessarily optimal strategies for mission maximizers or revenue maximizers. For example, a mission maximizing organization could very well employ a mixed pricing strategy to achieve an overall maximum mission impact for the organization if it is able to find profitable offerings, or alternative revenue sources, which can subsidize mission-relevant ones. Similarly, a revenue maximizing organization might mix in some loss making activities if it increased its appeal to donors or to customers of its profitable services. However, the foregoing patterns are useful referents for understanding the case studies described below, and the manner in which nonprofit managers address the tensions they see inherent in their pricing choices.

Table 2: Alternative Nonprofit Pricing Strategies

Mission Centrality/ Mission-related Pricing Intent	1	2	3	4	5
1	MM MX	MM	MM	MM	MM
2		MX			
3	BE	BE	BE MX	BE	BE
4				MX	
5	\$\$	\$\$	\$\$	\$\$	\$\$ MX

MM = Across the board mission maximizing pricing

\$\$ = Across the board revenue maximizing pricing

MX = Mixed pricing strategy, pricing for mission where potential mission impact is high and pricing for revenue where mission potential is low

BE = Across the board break-even pricing strategy

Note: 1 indicates high mission potential or pricing intent to maximize mission impact; 5 indicates low mission potential or low mission-related pricing intent (i.e., 5 represents maximum revenue intent for pricing)

Case Studies

The chief executives and the chief financial, chief operating or development officers, of five different types of social service agencies, all belonging to the same local religiously-affiliated federation in a major city in the Southeastern U.S., were interviewed using a standard interview protocol (see Appendix A). This was a convenience sample in the sense that the researchers received assistance from the chief executive officer of the federation in securing the cooperation of the CEOs and top staff of member organizations. It was also a logical selection of cases for exploratory research since it allowed access to a group of nonprofit organizations with a variety of social missions, all within a common geographic and cultural context. This allowed us to search for different patterns of pricing behavior without confounding variation of the external environment. For purposes of brevity, we report here on three cases representative of the alternative patterns found in the five cases.

In each case, the interviewed officials were asked to rate each of their organization's key services in terms of centrality to mission and intention of its pricing policy (or in the case of the more complex organizations a selection of service typical of the agency's spectrum of services was selected). The results are depicted in Tables 3 through 5 below, following the format of Table 2. In all three cases, two top decision-makers were interviewed (simultaneously) and responses reflect their consensus views. We do not provide detail on the process through which pricing decisions were made, though it is our understanding that these were essentially executive level decisions made by the CEO in consultation with chief financial or operating officers. Since the interviews were held under conditions of anonymity, the case study organizations are described generically as follows:

- Assisted Living provides several different levels of care for older residents with varying levels of disability.
- Community Center offers physical fitness, camping, early childhood and other programs; its mission is to strengthen the quality of life of its local religious community.
- Family and Career Services offers multiple counseling, disabilities, career and employment, and other programs related to its mission of maintaining

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people in their communities and minimizing need for institutional care.

Assisted Living’s pricing strategy appears to be that each of its services should stand on its own financially, without any cash cows or heavily subsidized programs. This is illustrated in Table 3 which records the executive director’s ratings of each of Assisted Living’s programs in terms of mission centrality and pricing intent. Its services range in terms of their centrality to mission, but pricing is approached uniformly in a manner that aims at financial solvency and accommodates financially or medically needy residents where necessary. In terms of the generic patterns identified in Table 2, this is an example of the breakeven (BE) model. That is, each program is expected to stand on its own and contribute to mission, no matter the level of its centrality to mission, while the pricing objective is to extract revenues adequate to support expenses, rather than maximum possible revenues.

Table 3: Pricing Strategy for Assisted Living’s Programs

Mission Centrality/ Mission-related Pricing Intent	1	2	3	4	5
1					
2					
3	Residential Care Levels 1,2 and 3	Cable TV Laundry	Pet Care	Extra Care for Dementia	
4					
5					
No discretion					

Table 4 reports the pricing strategies for Community Center’s programs as assessed by its CEO and CFO. Here it is clear that membership is the driving factor, priced substantially with financial support in mind despite its centrality to mission. Other

highly mission-related programs, such as camping and early childhood programming, are even more driven by revenue generation in their pricing policies. Finally, with the exception of programs for the developmentally disabled, programs – such as swimming lessons and House Mate Match - less central to mission are generally priced to more heavily reflect financial concerns. Nonetheless, in all cases there is some sensitivity to mission in setting prices and no pure cash cows. Overall, perhaps because of financial problems experienced in the past, Community Center’s pricing strategy leans towards a subdued version of the “revenue maximizer” as modeled in Table 2. None of its services are priced purely with mission in mind, some are priced carefully so as not to cause problems in strongly mission-related activity, and with one area of exception each is priced with a strong revenue intent, regardless of mission centrality.

Table 4: Strategies for Pricing Community Center’s Programs

Mission Centrality/ Mission-related Pricing Intent	1	2	3	4	5
1					
2		Developmentally disabled			
3	Membership; Religious education			Theatre	
4	Camping; Early Childhood		Swimming lessons		Housemate Match
5					
No discretion					

Table 5 reports the characterization of program pricing policies by Family and Career Services’s CEO and COO. The pattern most closely resembles the stereotypical “mixed” pattern suggest in Table 2. The most highly mission-relevant programs tend to

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be priced to reflect that status, while there are cash cows as well. It is interesting that Family and Career Services’s pricing strategies vary widely by program, depending largely on centrality to mission, and that no offerings are considered highly peripheral to mission. This seems to reflect the organization’s explicit strategy of reviewing each of its programs and phasing out those that connect poorly with its mission focus, as explained below.

Table 5: Strategies for Pricing Family and Career Services’ Programs

Mission Centrality/ Mission-related Pricing Intent	1	2	3	4	5
1	Meals on Wheels; Big Brothers/Sisters	Senior Transportation; Dental Clinic; Project Connect			
2	Independent Living				
3	Home Care Geriatric Counseling				
4					
5			Psych and Educational Testing; Adoption		
No discretion					

It is interesting that Family and Career Services offers few services remotely connected to mission, yet it employs a variety of approaches to pricing, with some nuances that reflect mixed objectives. For example, in the cases of Home Care and Geriatric Counseling, policies reflect the opportunity to raise revenues despite their centrality to mission, while in the cases of Senior Transportation and the Dental Clinic,

pricing for revenue is de-emphasized despite their somewhat weaker connection to mission.

In most of the cases we examined, decision-makers approached their pricing decisions intuitively and pragmatically without any strong guiding methodology. They each recognized the tensions, at least implicitly, and dealt with them in their own ways, their varied circumstances and management philosophies leading to alternative logics for finding satisfactory solutions. Thus, in none of the cases did the organizations strictly follow either the mission-maximizing or net revenue maximizing strategies for each of its services, as depicted in Table 2. Rather the cases illustrate alternative tendencies towards breaking even, maximizing revenue or connecting pricing strategy with mission relevance.

The matrices we used to characterize the decisions of our case study organizations are our own construction, and were not an explicit element in the actual decision making of organization leaders. However in one case, Family and Career Services, such an analytical tool was actually used. The organization's executive director and chief operating officer recognized their mission/market tensions explicitly and sought to address them with a systematic methodology and series of metrics that resemble those employed in the discussion above. As such, this case may serve as a normative model for other nonprofits to emulate. Below we explore this methodology in further detail, as applied to the pricing decision of one of the organization's service programs.

The P.E.P.S. System

In 2005, Family and Career Services recognized that, in order to achieve the greatest impact for its clients while acting in a fiscally responsible manner, the agency had to improve its program planning and evaluation capacity. The agency was feeling pressure from a more competitive funding landscape, increased competition by other nonprofits and privately held businesses, requests for more accountability from the board and outside regulatory agencies, and higher costs associated with service delivery. To address these issues, the agency developed the proprietary Program Evaluation and Planning System (P.E.P.S.) which is now utilized by over 25 diverse entities across the United States.

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P.E.P.S. provides a comprehensive, easy to use tool for promoting active program management and for establishing a common language between staff, boards, and funders. P.E.P.S. is designed as a set of “wizards” in which the user is walked through a series of queries regarding his or her organization’s programs. Dependent upon the responses provided, the program offers conclusions that assist the agency in making strategic determinations regarding investment, divestment, maintenance and/or modification of the reviewed program, including pricing modifications. A review of one of Family and Career Services’ programs illustrates the utility of P.E.P.S.:

Family and Career Services’ provides a suite of supportive services to adults with developmental disabilities designed to empower individuals and their families to maximize potential and participation in all aspects of everyday life. The core is an independent living program (see Table 5) in which the agency supports clients with activities of daily living in their own homes.

The disabilities program aligns directly with the agency’s mission of strengthening individuals and families. Early in its history, the disabilities division maintained a small core staff with a corresponding small client load of less than 20 clients. Initially, revenue was derived primarily through private payments from clients and their families. To accommodate clients unable to pay regular rates, a scholarship process was implemented. Scholarships were derived from fundraising efforts and by allocation of unrestricted funds.

As the program matured, significant changes forced a reevaluation of the pricing structure. One of these changes was the increased cost of regulatory compliance. Under new regulations, the agency was required to hire more direct care staff, administrative staff and professional staff (such as nurses). The combination of private payments and the burden of issuing scholarships put the viability of the program in jeopardy. To address these pressures, the agency secured a license to serve clients that received a Medicaid Waiver. This waiver compensated the agency at a higher rate than the average private payer.

At the time of this writing over 70% of clients in the disabilities division were under the Medicaid Waiver. While this shift has relieved some financial pressure, the regulatory burdens placed upon the agency have continued to increase, client needs are

expanding as clients age, and the revenues received for clients (both waived and private-pay) are insufficient to cover the independent living program's expenses. While the agency has been forced to diminish its "official" scholarship process, Family and Career Services continues to subsidize all clients in the program to varying degrees. Competitive market pricing is prohibitive for private-pay clients, and the agency is precluded from charging Medicaid clients above and beyond waiver rates. In addition, a revised waiver system is on the horizon and there is much uncertainty about its impact on the agency. Under the new waiver system clients will receive funding based on their levels of need, rather than a set, predictable amount of funding. Families may choose to hire direct care staff themselves, rather than using an agency, and may choose to purchase from a menu of services, reducing funds that would be earmarked for direct support. All of these factors affect future planning.

Using the P.E.P.S. framework, lay leaders, board members, and management, staff in the Disabilities Division engaged in a comprehensive review of service delivery, pricing, and mission alignment to analyze these challenging realities. P.E.P.S. includes several "wizards" addressed to Revenue vs. Need, and Financial Analysis. The former includes assessments of the revenue potential juxtaposed against the mission-relevant need for each program; the latter assesses the potentials for different sources of revenue support including grants, government funding and fees. With this information, the agency is able to make well-reasoned decisions regarding client pricing, program structure and program design. The analysis allows the suite of programs in the Disabilities Division to be adjusted so that they are fundamentally sound, mission aligned, and meet critical community needs.

In general, utilization of the P.E.P.S. application has enabled Family and Career Services to objectively review its programs and to make informed decisions regarding the dynamic tension between missions and pricing. The benefit of P.E.P.S. is to add discipline to the program evaluation process and more specifically to pricing decisions.

Conclusion

In principle, nonprofit organizations should ultimately judge their performance in terms of impact on social mission. Nonetheless, because nonprofits operate in a market environment, tensions between responding to the incentives of the marketplace and

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addressing the mission pervade virtually all dimensions of their economic decision making, certainly pricing. In order to deal effectively with these tensions, nonprofits can analyze both the direct and indirect mission impacts of any program as well as its financial implications, and then consider the combination of its programs in order to determine its solvency and level of mission achievement.

The richness and complexity of this subject matter suggests this it is fertile for future research. Here, we have taken some initial steps to describing how metrics and systematic analytical tools can be helpful in understanding and formulating nonprofit pricing decisions. The matrices displayed here to gauge pricing policy intent in terms of mission and financial contribution, reflect various patterns discussed in the nonprofit management literature. These include revenue maximizing, mission-maximizing and mixed pricing strategies. The five case studies presented lend some credence to these stereotypes while also suggesting that the real world is somewhat more complex and that many nonprofits tend to approach pricing decisions in an improvisational rather than systematic way. In some of the simpler cases, where nonprofits offer relatively few services and face strong constraints (e.g., from government) that reduce or eliminate discretion in pricing for some of their services, we found somewhat naïve pricing behavior, namely pricing on a service by service basis, without much attempt to differentiate pricing policies according to mission impact and market potential. In most of our cases, this pattern resembled a kind of “soft” revenue maximizing behavior, where a revenue cushion for the organization was sought through pricing policies that generated surpluses where possible, with steps taken to minimize sacrifices to mission. In other cases, a more sophisticated approach to pricing was evolving, entailing explicit assessment of the mission relevance and financial contribution of each service so that as a whole, the organization could design a combinations of programs that would be both financially healthy for the organization and maximally effective in addressing its overall mission. In one of our cases, the organization had gone so far as to design a sophisticated software system that allowed it to engage its decision-makers in a comprehensive assessment of the revenue and mission implications of all of its programs, setting the stage for informed pricing decisions in a dynamic environment. That system utilizes

within its tool kit, the same kind of simple metrics that we used here to describe the alternative approaches to nonprofit pricing that prevailed in the cases we examined.

It is clear overall that nonprofits struggle with the tensions of mission and market, with pricing an explicit arena in which decisions to resolve such tension take place. It is reassuring that we did not find evidence of aggressive, revenue maximizing intent, nor did we find irresponsible mission impact seeking at the expense of financial health. Even in the cases where pricing policy was preoccupied with generating sufficient revenue, there was strong consciousness of mission and a clear preference to patch up the policies where mission-related impacts could be damaging, such as in service to individuals unable to pay. Nonetheless, it is also clear that nonprofits need to become more sophisticated in deciding how to price their services. What we did find was a range of sophistication among the cases we examined –from muddling through on a program by program basis with ad hoc pricing heuristics to a very sophisticated technology-based approach sufficiently robust to be marketable to other organizations. Such a system appears to be helpful in creating the bases of information, the communication among decision makers and the conceptual guidance both for the appropriate choice of pricing schedules for particular service offerings and for balancing the mix of services so that overall financial viability is maintained and mission is maximally achieved.

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APPENDIX A:

INTERVIEW PROTOCOL: Pricing Practices of Nonprofit Organizations

1. What services are offered by your organization for which you charge a price?
2. What services are offered by your organization free of charge? In each case, please state the reason for offering this service without charge?
3. For each service, whether free or priced, please indicate on a scale from 1 to 5 how important the service is to the overall mission of your organization, where:
 - a. 1 is extremely important
 - b. 5 is peripheral or unimportant
4. For each service for which a price is charged, please answer the following questions:
 - a. Describe your pricing policy or the price schedule you offer to (different classes of) consumers or clients
 - b. Did the service make a profit, run a loss, or breakeven in the last fiscal year?
 - c. Does the service require the use of volunteer labor?
 - d. On a scale from 1 to 5 select the number that best describes the purpose of your pricing schedule, where:
 - a. 1 denotes that the price schedule is designed solely to permit maximum mission-related impact
 - b. 5 denotes that the price schedule is designed solely to maximize financial profit (or minimize financial loss)
 - e. If the service runs a loss, please indicate what other sources of funds are used to support its provision
5. Over the past five years, have you increased or decreased your reliance on fees to support your organization? Please explain.