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The Changing Landscape of America’s Societal Sector

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Introduction

This paper will outline the changes in the nonprofit sector since 1945 and will attempt to show that these changes are the result of various shifts in the contextual environment in which the sector has developed. This review of the history of the nonprofit sector\(^1\) will trace the influence of such factors as World War Two and the controversy which surrounded foundations mainly until the 1960's (although foundations do still have critics today). Other contextual factors include more academic transformations such as the influence of Keynesian economic theory and the 1960’s research on the roles of mediating structures in American democracy.

This review is designed to provide the background for a later project which will examine currently-occurring contextual changes and will use these to predict what characteristics will define the successful civic organizations of the new century. While traditional civic organizations have either always had or have developed a narrow focus from their need to serve their constituencies (including their funders), the new century may require a new type of civic organization that supersedes organizational interests. It is hoped that understanding the third sector’s response to past contextual changes (i.e., the ones discussed in this paper) will make easier predicting how the sector will react to upcoming changes.

\(^1\) The terms “nonprofit sector,” “third sector,” and “independent sector” are used interchangeable throughout this paper.
Literature Review

Many works about the nonprofit sector begin by grounding themselves in the sector’s history; few, however, take their histories much past the superficial level by more deeply analyzing their accounts to determine the deeper causes and implications of various changes. Even fewer works are written with the sole purpose of detailing historical developments in the sector. Thus, the available literature is numerous but the quality and depth of most works is moderate at best.

While most works referenced were secondary material, Alexis de Tocqueville’s *Democracy in America*¹ was a key exception. De Tocqueville’s visit to America in the early 1800’s provided him with much fodder for his two-volume work. Among his many insights, his most famous is the oft-quoted observation about the tendency of Americans to form associations. He discussed Americans’ preference to combat problems by forming organizations rather than by relying on the government to provide solutions. Tocqueville’s analysis of America was a beginning of the study of what later scholars identified as “the third sector.” Consequently, almost all scholars who write today of the independent sector reference heavily de Tocqueville’s insights into American culture which often still prove relevant.

Like de Tocqueville’s, several works emphasize the role of the independent sector in democracy and democratic society. Couto’s *Making Democracy Work Better*² includes a lengthy chapter on mediating structures, the formal or informal organizations that intermediate between citizens and the larger institutions of their society, especially

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government. Citing social scientists David Sills and Charles Nisbet, Couto argues that nonprofits—or at least some nonprofits—are mediating structures. He then discusses the functions of mediating structures in society, including their importance in the maintenance of a democracy. Summarizing the work of Sills and Nisbet, he argues that a major purpose of mediating structures is to counterbalance the centralization of power which is found in the hands of government.

Works focusing solely on the philanthropic aspects of organizations or of the sector as a whole are plentiful. A benchmark work is Robert H. Bremner’s *American Philanthropy.* In addition to an extensive chronology, he provides an insightful analysis of the effects of the historical context and of the repercussions of governmental policies. Moreover, several situations such as the congressional investigations of the third sector were chronicled in great detail. Similarly, F. Emerson Andrew’s *Philanthropic Giving* contains much relevant discussion of foundations and their role in the first half of this century. Written in 1950, it discusses at length the relationship between taxation and charitable donations and the controversy that surrounded this topic in the 1940’s.

One especially thorough work is *The Nonprofit Sector: A Research Handbook,* edited by Walter W. Powell. Especially relevant was Peter Dobkin Hall’s assessment of the history and development of the sector. Hall’s research is detail-oriented but the scope of his project is so large that he could not possibly cover all aspects of the sector’s history. He commences his study with the 1780’s and finishes with present times; however, his

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section on the years of my focus, 1945-the present, only barely touch many key issues. For example, he devotes only one sentence to the influence of Keynesian economic thought on the development of the independent sector; without undertaking outside research one would not know what he meant.

In addition to Powell’s compilation, two other anthologies contain several useful historical selections. David Hammack’s *Making the Nonprofit Sector in the United States*⁶ is a collection of essays covering eras from Colonial times to the present while discussing issues from religion to current federal regulations. Much of the collection was beyond the scope of this project but some essays were of relevant time and topic. Similarly, Brian O’Connell’s *America’s Voluntary Spirit*⁷ has excerpts from the report issued to Congress by the Commission on Private Philanthropy and Public Needs, from de Tocqueville’s *Democracy* and from many opinion pieces about the third sector. However, the essays contained within it reference little hard data, relying instead on personal opinions and observations. Thus, O’Connell’s work provided useful insights into the sector but little objective evidence.

A less useful compilation was David Gies et al’s *The Nonprofit Organization: Essential Readings*.⁸ Most of the readings are geared towards those in administrative positions of nonprofit organizations. Though the book begins with several readings on the history of the sector, most of those were either not of the relevant time period or were

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otherwise irrelevant. Additionally, several articles in the compilation were contained in other anthologies as well. Thus, the only useful article in *The Nonprofit Organization* was Steven Block’s “A History of the Discipline,” which discussed the evolution of the tax-exempt status of both nonprofit organization and the charitable donations given to them.

Though it does not endeavor to tell the story of America’s nonprofits, James Patterson’s *America’s Struggle Against Poverty, 1900-1994* offers an adequate explanation of the social changes related to the 1960’s Great Society failure. Additionally, Patterson discusses the details of the early 1980’s recession and subsequent budget cuts, especially in the area of social services. These changes directly affected the independent sector and Patterson’s analysis is consequently quite helpful. One interesting contrast between the Great Society and Reaganomics, he noted, was “the goal of social policy in the Johnson (and even Nixon) years had started with the question, ‘How can we help the poor?’ Reagan, in contrast, tended to ask, ‘How can we cut costs, and how can we get people to work?’” However, Patterson’s true focus is poverty and the third sector is only a tangential area of research. Thus, his work can be analyzed in relation to the third sector but Patterson himself avoids such analysis.

James C. Crimmins and Mary Keil’s *Enterprise in the Nonprofit Sector* endeavors not to outline the history of the sector but to discuss case studies of several nonprofit organizations that have engaged in entrepreneurial activities. However, doing so

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10 Patterson, James T. p 212
requires a brief detailing of how the third sector has been shaped by changes in the political climate. Thus, their work contained a short history of the sector which proved to be a good outline of several topics, including the effect of Johnson’s Great Society programs and Reagan’s budget cuts. Unfortunately, the material was in no way more than a guide to useful topics which then had to be researched in other works.

In researching the effect of government funding on the independent sector, Steven R. Smith and Michael Lipsky’s *Nonprofits for Hire*\(^{12}\) provided substantive historical information along with unique insights concerning the government’s role in the sector’s growth. Specifically, the authors discuss at length what they call “the contracting regime,” that is, the tendency of the federal government to contract out to nonprofits for publicly-provided services.

An article that discusses societal changes and their effects on the third sector is Peter Drucker’s “The Age of Social Transformation.”\(^ {13}\) An account spanning the time from World War One to the present, it covers the changes in culture that have affected the way nonprofits respond to the world. Drucker’s work falls short of making the comparisons to the third sector but provides some relevant information useful in understanding the causes of the changes the sector experienced. For example, Drucker traces changes from the time of the decrease in the farm population to the current increasing demand for “knowledge workers.”

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Michael O’Neill’s *The Third America*\(^1\) divides the entire nonprofit sector into nine subsectors and examines briefly the scope and impact, historical developments and policy issues associated with each section. As this paper is limited mainly to the social service and civic aspects of the third sector, much of O’Neill’s work is irrelevant. Additionally, that his historical tracings begin in the colonial times leaves little room for a thorough discussion of this century’s developments. However, O’Neill’s research does provide some useful bases from which further research can be done. Analogizing about the increase in the role of the government in providing the social services that were traditionally identified with the independent sector, O’Neill says that due to the funding increases of the Great Society, “government service went from kid sister to big brother.”\(^15\) However, despite his unique ways of expressing his insights, O’Neill’s work overall is merely a brief summary of the other sources available.

Lester Salamon’s *America’s Nonprofit Sector*\(^16\) contains many statistics and essentially paints a picture of the sector’s demographics. Salamon also discusses the historical developments of the sector in some detail. Like several scholars, he focuses on the effects of Johnson’s Great Society. However, he does take his work further than most by analyzing in-depth the effects of the program and how specifically they changed the sector. Moreover, his discussion of economic and financial details such as budget figures and spending trends is much more thorough than that of most other researchers.

A second—and more current—work with superb financial and economic data is Virginia Hodgkinson and Murray Weitzman’s “The State of the Independent Sector.”

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2. O’Neill, p. 104
Overview and Highlights,” an article which is an update of the triennially-published 
*Nonprofit Almanac*. More than any other source, their work provided quite recent figures 
concerning funding of the sector as a whole and the various subsectors of which it is 
comprised.

   Overall, the literature is scattered and looks only at segments of the whole. The 
only work which really ties together the historical, social, political, intellectual and 
economic contexts of the sector is Hall’s “A Historical Overview of the Private Nonprofit 
Sector” in Powell’s *The Nonprofit Sector*. However, Hall covers such a length of time in 
his discussion can not help but to be limited by space constraints. Thus, the literature 
appears to be lacking a thorough analysis of the contextual changes that have affected the 
sector in this century. It is hoped that this study will fill this gap in the available literature.
Methodology

The purpose of this paper is to study and document major shifts that have occurred within the independent sector (e.g., the nonprofit sector) in the last fifty years. Specifically, it will focus on the social service providers and civic organizations of the nonprofit sector. I hope to answer the question, “What have been the major organizational challenges and changes in these types of organizations in America since World War II?”

This study hypothesizes that significant changes will be found in how the sector is viewed and treated throughout time due to shifts in the contextual landscape in which the sector has its being. Moreover, it proposes that the changes in public opinion regarding the sector have resulted in political and governmental policies and actions which have directly shaped the sector’s growth. It will be shown that although the third sector is often mistakenly considered to be an “alternative” to the first sector (e.g., government), the third sector’s growth and development have been directly affected by governmental decisions, especially those enacted at the federal level such as the tax-deductible status of charitable gifts.

Studying the contextual developments of the sector necessitates researching both academic literature and works designed to provide background information for nonprofit practitioners. Most literature consulted either briefly summarizes large periods of time or concentrates in detail about one or two aspects of the sector. It is hoped that compiling a great deal of both types of literature will create a more thorough picture of the historical developments. Once information about the societal and nonprofit sector changes has been compiled, it will be possible to draw connections between the historical context and the concurrent shifts in the independent sector.
One possible problem or source of bias for the project is that I am undertaking the project with the premise that a new type of civic organization is developing. It is possible, however, that this is not the case. As I research the history of these organizations, I will need to be careful to not “see” changes that have not occurred. I hope to be able to limit this source of bias by recognizing that I am attempting to find whether or not societal changes have changed the independent sector, rather than assuming that my hypothesis is correct.
The Changing Landscape of America's Societal Sector

"On the map of American society, one of the least charted regions is variously known as the voluntary, the private non-profit or simply the third sector. Third, that is, after the often overshadowing worlds of government and business."

— The Filer Commission

In 1975, when the Commission on Private Philanthropy and Public Needs (the Filer Commission) issued to Congress a report detailing its study of America's nonprofit organizations, the voluntary sector was for the first time labeled "the third sector." Yet voluntary associations were not a contribution of the 1970's to American culture. When Frenchman Alexis de Tocqueville wrote his two-volume Democracy in America in 1835 he noted, "Americans of all ages, all conditions, and all dispositions constantly form associations... Wherever at the head of some new undertaking you see the government in France, or a man of rank in England, in the United States you will be sure to find an association." It can be inferred that Tocqueville saw a clear distinction between the roles of government and voluntary associations. However, the two are not as separate as they are often portrayed. In fact, changes in political thought and action have driven much of the growth and development of America's third sector that has occurred since World War Two. These shifts in the political climate, in turn, can be shown to be the result of various contextual changes.

CONTEXTUAL DEVELOPMENTS

World War Two saw major increases in charitable contributions for several reasons. Bremner writes, "war needs and war prosperity contributed in about equal measure to the generous support accorded assorted philanthropic causes in the 1940’s." First, increases in tax rates were implemented to raise money for the war effort. However,
that philanthropic contributions are tax-deductible meant that much of what the federal
government hoped to gain in tax revenue actually found its way into the pockets of
nonprofit organizations. That citizens are allowed to deduct charitable contributions from
taxable income is a hallmark of the American tax code. The system is based on the idea
that private donations to charitable causes such as feeding the hungry save the government
from having to spend that same money (which they could have received in tax revenue) on
feeding programs. As a consequence, taxes and charitable donations are positively
related. F. Emerson Andrews wrote in 1950, “Tax evasion is illegal; but to take advantage
of the provisions written into the tax laws to increase the size of one’s gift is perfectly
proper.” That people noticed they could contribute to charitable causes with little
personal sacrifice was common. Bremner noted that due to the increasing wartime taxes
levied on citizens, personal charitable contributions increased fivefold from 1939 to 1945,
although he does not specify whether this was a nominal or real change.

The growth of available revenue for philanthropic activities was a cause of the
prominent growth of foundations. F. Emerson Andrews, the first president of The
Foundation Center and a noted scholar of philanthropy, provided the widely-accepted
definition that a foundation is:

a nongovernmental, nonprofit organization having a principal fund of its
own, managed by its own trustees or directors and established to maintain
or aid social, educational, charitable, religious or other activities serving the
common welfare.

In coordination with Andrews’ definition, Thomas Reeves identified five main categories
of foundations: 1) general-purpose foundations (e.g., the Ford or Carnegie), 2) special-
purpose foundations, 3) family or personal foundations (which become general-purpose
foundations upon the death of the person or family responsible for their creation), 4) corporation foundations and 5) community foundations. A foundation’s funding comes from one of three major sources: from a person or family, from a corporation or from small gifts by many people and corporations (generally, this is only the case for community foundations).

The proliferation of American foundations occurred primarily from the 1920’s to the 1960’s. In 1929, 239 existed in the US; the next decade saw this number more than double to 533. Yet the increase in the 1930’s was minimal compared with the exponential growth experienced between 1940 and 1959; in these twenty years, the number of foundations skyrocketed, resulting in 5,400 at the end of the 1950’s. This rapid growth has received much attention in third sector literature. While many of these foundations were established for charitable reasons, others were created to take advantage of the tax loophole that a foundation could access. Critics maintained that foundations were an easy way for families and corporations to look generous and yet to maintain control of their assets. They pointed to “self-dealing,” a process by which a foundation might make a grant to a business owned or otherwise controlled by a member of the foundation. While various causes for the growth of foundations have been offered, by far the most commonly-cited has been that the tax code allowed foundations what many consider a “loophole.” Noted third-sector historian Peter Dobkin Hall supports this factor to the exclusion of all others. Likewise, Reeves agrees that:

the primary impetus for the proliferation of foundations seems certainly to have been federal tax laws. Through foundations wealthy individuals and corporations have been able legally to reduce and circumvent taxes, often saving themselves large sums of money.....And foundations often permit retention of control of wealth, a benefit unavailable with donations to
operating charities such as the Heart Fund. The rise of the corporation foundation may be directly related to the excess-profits taxes of the Korean War years. The high personal income taxes of the Second World War caused a leap in the number of family foundations... In short, the higher federal taxes of [the 1940's through 1960's] have undoubtedly advanced the unprecedented growth of foundations.”

However, one cannot reasonably claim that tax benefits have been the sole cause of the expansion of foundations in these years. Zurcher, for example, while arguing that tax benefits were a driving force for the growth, quickly asserts that the financial tax gains were not the only and may not have even been the primary contributing factor. He writes:

"A sense of social trusteeship of great wealth may have been the principal, if not the exclusive, motive of men such as Carnegie or Rockefeller when they established their foundations and it is practically certain that such a motive also influenced most of the more recent creators of foundations—men like Alfred P. Sloan, Jr. or members of the Ford family.""14

One aspect of the controversy surrounding foundations stems from the argument that since foundations are funded to a large extent with money that otherwise would go to the federal government in the form of tax payments, there needs to be some degree of accountability and “public responsibility.” For example, Congress’ Reece Committee in its 1954 investigation offoundations argued that the money represents public funds and should be spent in ways which are “acceptable to current public opinion.” Whereas most foundations now provide annual reports chronicling their activities, less than 4% were found to do so in a 1965 report by the editor of Foundation News. Moreover, the lack of an annual report was not simply an oversight and was not left undone because of time constraints. Rather, foundations insisted on their right to “[shroud] their affairs in secrecy, claiming that their business was exclusively their own.”
In the 1950’s the Carnegie Corporation created The Foundation Center, an umbrella organization essentially to serve as a public relations group to “combat the secrecy” that existed among many foundations. It was hoped that having an organization to such as the Center could help foundations regain the trust of the American public and the realization that foundations did serve the public good in many ways by helping to publicize “what they do and do not do.”

Besides the increase of foundations in the third sector, another major change affecting the sector was the beginning in the 1960’s of social science research on “mediating structures.” Though generally thought of as the same as third sector organizations, the category of mediating structures does not necessarily include all members of the independent sector. Peter L. Berger and Richard J. Neuhaus, in the Mediating Structures Project, consider mediating organizations as those which “stand between the individual in his or her private life and the large institutions of modern society.” The difficulties identifying which organizations qualify as mediating structures is perhaps compounded by the fact that there is disagreement as to what roles mediating structures should play. Couto notes that from the dispute over the role of these organizations two main “camps” have emerged—“Minimalists” and “Maximalists;” the respective groups believe in limited or enlarged roles for mediating organizations. Couto writes, “Some proponents suggest a minimalist role…that is, public policy should protect and foster them and do them no harm. Other proponents suggest maximalist roles for mediating structures, form participating in the design of public policy to conducting public policy as service deliverers.
Despite their differences of opinion in some aspects or areas, most scholars agree about the role of mediating structures in relation to the power of government. Social scientists David Sills and Robert Nisbet, in their works on mediating structures, both discuss the topic. "This primary mediating role focuses on the state and the functions of voluntary associations to distribute political power. Like Nisbet, Sills concludes that the power of dispersed associations balances and limits the power of the state."\(^2\) As shall be shown, Salamon notes that the Mediating Structures project was an instrumental part of the foundation of the Reagan administration’s views of the nonprofit sector.

In addition to the acknowledgment of mediating structures, a second major intellectual change affecting the sector was the influence of Keynesian economic theory. Before the Great Depression, the commonly-held assumption was that despite minor fluctuations, a market economy if left alone could always hold itself in or close to equilibrium. The Great Depression showed that the Classicists’ *laissez faire* policies had yielded an economy that at the very least could take too long to right itself and at the extreme might never self-recover from a severe recession. In his 1936 work *The General Theory of Employment, Interest and Money*, John Maynard Keynes introduced a demand-side economic theory which emphasized that by acting quickly, the government could adjust its fiscal policies to help keep the economy stable. Moreover, Keynes demonstrated that government spending has a “multiplier effect” and thus benefits the economy many times over and above the actual dollar amount spent.

The post-WWII era found the relationship between the public and private independent sectors strengthened in part because of the Keynesian Revolution in economic thought. Hall notes that Keynesian theory contributed to this “public-private partnership”
since "both business and government leaders [recognized] their common interest in economic stability."22 Realizing the beneficial role the government could play in maintaining the economy’s health, the private sector leaders objected less to government intervention and increased participation in the economy. While one cannot claim that Keynesian theory eliminated Americans’ fear of large government, it at least mitigated their opposition. The postwar years were thus marked by significant government investment in the private sector that often occurred through the growing independent sector. The Hill-Burton Act, which provided funding for the building and equipping of hospitals, is an example of government funding which benefited the third sector. Over half of the Act’s money was utilized by the independent-sector organizations. Additionally, the government invested money into research and development in the post-war years, also often through nonprofits.

POLITICAL REACTION

These changes in American culture—the effect of WWII, the study of mediating structures, the increase in the number of and the controversy surrounding foundations, and the influence of Keynesian theory—were directly responsible for the governmental policies and actions which so shaped the sector’s development. That political and governmental affairs have played such a large role in the sector’s growth may surprise some. However, the first sector—the government—has played a leading role in America’s voluntary sector and to attempt to claim otherwise is naïve. From the post-World-War-Two public-private partnership to the tax code of today, government policies and actions have shaped the sector, despite popular notions to the contrary. (For example, Sills and Nisbet “both maintain the importance of mediating structures to disperse power in society and to check
the modern tendency to concentrate power in the hands of the state and bureaucratic organization." Third sector scholar Lester Salamon contends that several inaccurate theories concerning the role of the nonprofit sector have been responsible for the spread of the assumption that government's role is virtually nonexistent in the third sector. For example, he disputes the concept of nonprofits as a response to the "market failure" which causes socially beneficial goods and services to suffer from the free-rider problem. In this view, the only role government has in the sector's development is that its inability to produce the needed goods has created a third sector that can. The prevalence of this idea, Salamon argues, causes Americans to overlook the symbiosis between government and the independent sector. Agreeing with Salamon, Couto insists that the large role of government in the sector is due to the fact that "mediating structures do not occur naturally...If we want them, we need to support their origins and continuation through public policy."

That the first and third sectors, i.e., government and the independent sector, are inextricably connected is demonstrated by the significant ways in which the tax code affects and determines the direction of the sector's development. Although philanthropic, charity and volunteer activity have been present since the time of the founding fathers, one can easily make the case that nonprofit activity as a sector began with the IRS's 1954 creation of the 501(c)(3) tax status. Moreover, the tax code has been amended several times in direct response to activities relating to the third sector. However, even before 501(c)(3), American tax laws were enabling the "generous" spirit of citizens and corporations. During World War Two, the high tax rates on corporations, coupled with the patriotic fervor of investing in America, caused the corporate giving rate to
Community Chests--constant since 1921--to rise.

Zurcher comments on the still-strong tendency of foundations to isolate themselves rather than to collaborate with other foundations which have similar missions. Though he admits that this is slowly fading, he attributes it to the several federal investigations of foundations that took place in the early and mid 20th century. He argues that the most formative investigation was that conducted by Congress in 1912. The Walsh Committee’s final report “suggested that, if foundations acted in concert even in minor issues, they might be accused of being a ‘money trust’ and of using their economic power in ways that would be detrimental to the public interest.” Moreover, Zurcher contends that more recent investigations such as that of the Patman Committee in 1962 maintained, at least on the hinting level, that they agreed with the threats made 50 years earlier by Walsh.

The abuse of foundation status came under attack as early as 1948 when Senator Charles Tobey began an inquiry of corporate foundations. These kinds of probes continue today with charges that foundations exceed their non-partisan and political limits. The Filer Commission examined all aspects of the nonprofit sector, but before that several Congressional committees scrutinized the activities of one of the most controversial aspects, foundations. After the Walsh Committee’s 1912 investigation, the next major investigation came in 1948, with Senator Charles Tobey’s committee. Next came the Select Committee of the House of Representatives, called the Cox Committee after its chair. The Cox Committee scrutinized the business of many of America’s larger foundations and its findings were generally favorable, though pointing to a few abuses of foundation status. However, Representative B. Carroll Reece, dissatisfied with the findings, asked for and received permission in 1954 to continue the investigation in the
Special Committee to Investigate Tax Exempt Foundations.\textsuperscript{27} Reece’s Committee eventually reported its finding “that foundations, educational institutions, and research organizations were involved in a ‘diabolical conspiracy’ to foist socialism on the American people.”\textsuperscript{28} However, the Committee was unpopular in the media, which along with negative editorials publicized that two members of the committee had written a minority opinion referring to the committee’s work as “an ugly stain’ on the record of the House of Representatives.”\textsuperscript{29} Additionally, that the committee carried out its tasks concurrent with Senator McCarthy’s censuring lessened its credibility.\textsuperscript{30}

Despite that the two investigations of the 1950’s did little to hurt foundations, the foundations were not out of danger yet. Less than eight years after the Reece Committee’s Report was published, Texas congressman Wright Patman began the third investigation of foundations be Congress in a decade. Beginning in 1961 Patman concentrated his efforts on national foundations which he accused of dodging taxes, helping an elitist few to maintain their wealth and power and being able to operate with public officials exercising only “lax and sporadic control.”\textsuperscript{31} Hall suggests that Patman, a staunch Southerner, was at least partially motivated by his opposition to the support many national foundations gave to the civil rights movement.\textsuperscript{32} Whatever the motivation, Patman found much more public support than Reece had, especially once his conclusions were written up in \textit{The Rich and the Super Rich}, a 1968 best-seller by Ferdinand Lundberg.\textsuperscript{33}

The work of Patman’s committee was a primary cause of the IRS’s 1963 decision to implement a thorough system for auditing foundations. However, this was not the sum of the consequences. “Giving Better, Giving Smarter,” a report issued by The National Commission on Philanthropy and Civic Renewal, suggests that the Committee’s work was
also the major reason for the Tax Reform Act of 1969. Dislike of foundations continued to grow, with the government doing little to end the problems. They would pass laws that were vague or might not be followed. Thus, by the Tax Reform Act of 1969, foundations were viewed with such distaste that the proposals for part of the Act were quite extreme. One went so far as to insist that no foundation should be allowed to exist for more than 40 years.\(^3^4\) However, although the forty-year provision was not put into the final form of the bill, there were still many implications for the foundations of America. The Act’s two main goals were to limit the ability of foundations to benefit those who directly controlled them (self-dealing). The second was to limit the rights of foundations to operate in those arenas that were “politically sensitive.”\(^3^5\) The importance of this in the Act was encouraged by the criticisms of the 1960’s that foundations were engaged in extremist (leftist) activities. “The criticism consisted of charges that foundation money supported extremist causes, especially of the left; that indirectly, if not directly, it influenced the fate of issues at the polls and before legislative assemblies and administrative bodies; that sometimes it directly aided candidates for public office; and that it financed research the results of which were politically slanted or, in any case, of no social worth.”\(^3^6\) “Giving Better” outlines some of the changes in the 1969 Act as follows:

That law instituted a 4 percent annual excise tax on foundations’ net investment income (later reduced to 2 percent, and 1 percent in certain situations), prohibitions against self-dealing by foundation officials, an annual payout of 6 percent of assets (later reduced to 5 percent), a 25 percent limit on the ownership of a corporation, and various public disclosure requirements.\(^3^7\)

The 1969 act also included bans on spending money on political lobbying or advocacy with stiff fines on the foundation that engages in such activities, and upon
whomever at the foundation who approved such expenditures. An important catalyst for these changes was the strongly accusatory tone of the Reece report. “Our conclusion is that there is no true public accountability under the present laws. What is the penalty if, by chance, serious malfeasance is proved—perhaps by substantial grant, for subversive purposes or for active political propaganda? The mere loss of the income tax exemption. That is the sole penalty, other than the loss of the right of future donors to take gift or estate tax exemption on their donations. The capital of the foundation may still be used for a malevolent purpose. The trustees are not subjected to any personal penalty. The fund merely suffers by, thereafter, having to pay income tax on its earnings.”

In 1950, F. Emerson Andrews wrote, “The vast expansion of government services in the past two decades has changed conditions and vitally affected needs in nearly every field of voluntary philanthropy. The ration between government and voluntary spending for welfare purposes will differ with definitions of “welfare purposes,” but it is estimated that government expenditure (including federal, state, and local) is now about nine times voluntary giving for purposes which a generation or two ago would have been deemed to lie wholly within the field of private “charity.”

The second major expansion of the interrelationship between society’s three sectors was due to Johnson’s Economic Opportunity Act of 1964 which created the Office of Economic Opportunity and began the War on Poverty. The undertaking of the War on Poverty was a demonstration of the new conception of poverty which had taken root in the 1960’s. Previously, the majority had thought of poverty as the fault of the poor, thought that character defects in the poor were the cause of their destitution. However, two major scholarly works in the 1960’s helped to change that view of the poor. The first,
Michael Harrington’s *The Other America* took the notion of a “culture of poverty” introduced in world anthropological literature in 1959 by Oscar Lewis and made the case that it applied to the United States. Because of the culture of poverty, Harrington argued, destitution was not a choice or the result of a flawed character but rather the inevitable outcome of a person’s being reared in a community lacking money, traditional values and stable role models.42

Harrington’s book has often been cited as the source of America’s reintroduction to poverty, a topic which since the 1930’s had been largely ignored.43 His book soon found itself on the best-seller list and in the hands of President Kennedy and others influential in shaping America’s domestic policy. Many seemed to believe that Harrington’s “rediscovery” of the poor was the sole driving force behind Johnson’s War on Poverty. However, in his *Unraveling of America* Allen Matusow argued, “The government did not undertake a War on Poverty because Michael Harrington wrote a book. A constituency both aggrieved and vocal had first to demand it. In the spring of 1963 the civil rights movement took a mass dimension, creating that constituency overnight.”44

No matter what the motivations were behind the War on Poverty it greatly affected the nonprofit sector. With the War on Poverty, Medicare and Medicaid were established in 1965 and the Great Society also provided funding for Head Start, Job Corps, VISTA, and Community Action Programs (CAPs). The CAPs, designed to procure the "maximum feasible participation"45 of the poor in the programs created for them, were thought to strike at the causes of poverty rather than at its symptoms.46 The creation of CAPs in the 1960’s corresponded with the newly developing trend of creating nonprofit agencies that
addressed areas previously acted on by government alone. Smith and Lipsky write, “At times, government officials actually articulated the need and then created the organization in concert with interested social activists. Many current nonprofit programs for the poor, mentally ill and developmentally disabled fit this model.”

Government funding of applicable subsectors of the third sector (i.e., excluding foundations) has continued to increase since the 1960’s. The Independent Sector’s *Nonprofit Almanac* has reported a slow yet steady increase in the percentage of the third sector’s funding originating from the government.  

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount in 1996 Dollars</th>
<th>Share of Total Funding</th>
</tr>
</thead>
<tbody>
<tr>
<td>1977</td>
<td>29.5 B</td>
<td>26.6%</td>
</tr>
<tr>
<td>1982</td>
<td>59.5 B</td>
<td>28.1%</td>
</tr>
<tr>
<td>1987</td>
<td>88.5 B</td>
<td>27.9%</td>
</tr>
<tr>
<td>1992</td>
<td>159.4 B</td>
<td>31.3%</td>
</tr>
<tr>
<td>1996</td>
<td>196.8 B</td>
<td>31.7%</td>
</tr>
</tbody>
</table>

Even more dramatic, however, are the statistics showing the percentage of social and legal services organizations’ funding that comes from state, local or federal government.  

<table>
<thead>
<tr>
<th>Year</th>
<th>Amount in 1996 Dollars</th>
<th>Share of Total Funding</th>
</tr>
</thead>
<tbody>
<tr>
<td>1977</td>
<td>5.6 B</td>
<td>54.7%</td>
</tr>
<tr>
<td>1982</td>
<td>11.2 B</td>
<td>54.9%</td>
</tr>
<tr>
<td>1987</td>
<td>15.5 B</td>
<td>48.1%</td>
</tr>
<tr>
<td>1992</td>
<td>28.0 B</td>
<td>50.1%</td>
</tr>
<tr>
<td>1996</td>
<td>39.9 B</td>
<td>39.9%</td>
</tr>
</tbody>
</table>

From 1977 to 1996 real government increased by 34.3B in 1996 dollars. However, the percentages show the decreases in percentage revenue experienced by social service
organizations once the budget cuts of the 1980’s took effect.

With the government spending such great amounts of money on social welfare, some speculated that the private independent sector was no longer necessary. This was far from the truth. The American commitment to the diffusion rather than centralization of power meant that much of the government funding for social programs was distributed to private agencies to implement the initiatives. This mutually beneficial cooperation strengthened the relationship between the first and third sectors since the government depended on nonprofits to carry out its policies. The independent sector has continued to grow and expand from this early support.

That the money distributed went directly from the federal government into local programs was the root of public objection to the OEO’s programs. “OEO was encouraged to bypass local and state governments” as part of the way of insuring maximum feasible participation on the part of those they were serving. However, as Joseph Califano, Chief Domestic Advisor to President Johnson, remarked, “Part of the power of politics is your ability to hand out money and we were handing the money, and it wasn't going through the governor's office. And they didn't like that.”

Problems with the Office of Economic Opportunity and its programs were evident almost instantly. Though a main thrust of the OEO was the creation of CAPs, the agency did not have a clearly defined picture of its purpose. Its director later admitted, “It’s like we went down to Cape Kennedy and launched a half dozen rockets at once.” The widely-recognized lack of success of the Great Society programs caused a rethinking of how to best meet the needs of citizens and thus laid the foundation for significant redirecting of the government’s policies.
In “Nonprofit Organizations: The Lost Opportunity” Salamon maintains that the failure of past reforms (i.e., Johnson’s initiatives) helped to create the foundation upon which the Reagan administration’s initiatives concerning the sector were built. He argues that along with the “mediating structures project,” a decline in the health of the public-private partnership and slow declines in charitable giving, the dissatisfaction with the outcomes of the 1960’s and 1970’s governmental social-service programs created a viable atmosphere for significant changes in the government’s response to the third sector. The changes, however, Salamon characterizes as representing “a lost opportunity” for the government to make beneficial changes that would help the sector. He writes that “Insofar as the administration acted at all with specific regard for this sector, the actions...must be judged tepid at best and wrong-headed at worst.”

The many effects of the Reagan administration on the sector were the result of its three-pronged approach involving the manipulation of fiscal policies, the creation of “The Task Force on Private Sector Initiatives” and the change in approach towards dealing with various social service programs. However, by far the most influential were the administration’s tax and spending cuts. Though largely in response to the recession of the early 1980’s, these changes were also affected by the enduring debate concerning the appropriateness of various sources of third sector funding. Some critics had denounced the sector’s acceptance of governmental funding, arguing that such money comes with “strings attached.” One nonprofit director explained, “Truly voluntary associations are desperately needed for the revitalization of the democratic process, but they cannot be supported by government funds since governmental funding immediately contaminates their nature and is self-defeating.” The Reagan administration hoped that by reducing
governmental funding of the sector, it could eliminate the conceptualization of the sector’s being funded by “tainted money” and could thus revive America’s propensity to volunteer and/or to support independent sector organizations. It counted on this predicted increase in support for the sector to make up for the funding decreases which it caused.

However, the Reagan administration underestimated the negative effects its policies would have. Reagan’s use of supply-side economics included major tax cuts designed to stimulate the economy. These cuts doubly burdened the third sector. First, citizens who were motivated to charitable giving by tax benefits found that they need not donate as much money to meet their maximum deductions. At the same time, Reagan called for decreases in public spending on social needs. The administration seemed to expect the sector to operate with less revenue while making up for the government’s withdrawal of support from many public service programs. Thus, nonprofits found themselves faced with decreased revenue coupled with the expanding need for their services caused by the elimination of several federal programs for the less-fortunate.

A few years later, the 1986 Tax Reform Act was yet another federal action that resulted in a major revenue decrease for the third sector. The changes it produced in the tax code meant that citizens who filed non-itemized tax returns (approximately 75% of Americans) could no longer claim tax deductions for charitable donations. Although most citizens who engaged in charitable giving did not see tax benefits as their sole reason for donating, the tax law changes nonetheless decreased the economic benefits of philanthropy. Like the tax cuts earlier in the decade, the 1986 reform was a major setback for the sector.
The revenue decreases during the Reagan era caused the sector to work towards “collaboration and partnerships, partly in the hope that the other sectors could make up for what the public sector was no longer willing to provide... Today, collaboration and partnerships remain guiding principles.” The nineties have seen government spending restored in some cases but also a reordering of national priorities particularly on personal responsibility and fiscal health. Barring significant economic troubles, the country will simultaneously enter the new century and achieve the longest economic expansion in its history. However, this financial improvement has not benefited the community sector in the fashion of the Keynesian multiplier. As the sector approaches the future, it still has many significant issues which must be resolved. The “sources of funding” debate is particularly important. As mentioned, many believe that governmental funding is innately wrong; at the same time, though, the sector has also come under fire for its increasing commercialization. Caused by competition in typically-nonprofit realms by private corporations and by the pressure on independent-sector organizations to be self-sufficient, the commercialization of the sector has been marked by the entry of many third-sector organizations into for-profit markets and the increasing tendency towards fee-for-service policies. Nonprofit organizations have taken such approaches in order to generate more revenue to apply towards their primary foci. However, the question arises whether such profit-generating endeavors that are unrelated to the organizations primary mission should be protected from taxes under 501(c)(3)

As second and more primary debate has also begun over whether “the independent sector” actually exists outside of the tax code. Critics and practitioners recognize the sector’s numerous diverse subsectors and some argue that the “independent sector” is only
a legal construct. In order to move forward successfully, practitioners and scholars will need to address these issues; the sector cannot move forward without knowing where it now stands.

2 Couto, Chapter 2.
3 De Tocqueville in O’Connell 54-55.
4 Bremner. p. 163-164
5 Andrews. p 230
6 Andrews. p 231
7 Bremner. 164
8 The Foundation Directory, New York, 1964, p. 9 quoted in Zurcher, p.6
9 Reeves, p. 4
10 Zurcher, P11
11 Hall in Powell, p. 17
12 Zurcher, p. 145
13 Reeves, P. 6
14 Zurcher, P1
15 Reeves, P. 7
16 Zurcher, P1
17 Reeves, P 7
18 Reeves, P. 8.
19 Zurcher, P. 9 .
20 Kerrine, 1980, quoted in Couto.
21 Couto.
22 Hall in Powell, 18
23 Couto.
24 Salamon in Powell, p. 109
25 Zurcher P9
26 Zurcher, P10
27 Hall in Powell, p. 19
28 Bremner, p. 167.
29 Bremner, p. 171
30 Hall in Powell, p. 19
31 Bremner, p.181
32 Hall in Powell, 20
33 Hall in Powell, 20.
34 Zurcher, p. 146
35 Zurcher, p. 147
36 Zurcher, p. 148
38 Zurcher, p. 149
40 Andrews, P43
41 Hanson.
42 Hanson.
43 Patterson. 99
44 Quoted in Gareth Davies, p 45
45 http://www.ark.edu/depts/hesweb/rsweb/nimley.html
46 ??
47 Smith and Lipsky.
49 Hall, 18.
50 DiNitto, Diane. Social Welfare. p 284
52 Patterson.
53 Salamon, in The Reagan Response. p 271
55 Wallis, 254
56 Salamon in The Reagan Response.
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