Challenges in the Icelandic Non-Profit Sector

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Abstract
Non-profit organizations have been key actors in providing welfare services in Iceland. The recent economic crisis in Iceland, described as the most serious since its independence in 1944, will create new and extensive demands for welfare services. This paper describes the new challenges non-profit organizations face as a result of growing demands and the financial uncertainty following the collapse of the banking system in the fall of 2008 and how the economic situation is expected to influence their capacity and managerial strategies. Three types of non-profit organizations were analyzed: service provision organizations, mutual support societies and campaigning associations. The paper is based on preliminary findings from a current study on non-profit organizations in Iceland.

Introduction
The importance of the third sector in providing public and quasi-public goods in a market economy has been well documented. Its existence has been explained by its ability to respond to “demand heterogeneity”, an unmet need for goods not provided by the government (Weisbrod, 1977), being trustworthy agents as their incentive is not distributing profit to owners (“nondistribution constraint”, Hansmann 1980) and having an important entrepreneurial role for promoting social value and innovation (Anheier 2005).
In recent decades the third sector has become a more influential actor in public service provision and policy making – not least in welfare services (Smith and Lipsky 1993) in addition to the traditional role as social entrepreneurs and active participants of civil society (Herrington 2006). Because of this increasingly important role it is a demanding question how the global economic crisis will affect the third sector as it faces shrinking budgets and increasing demands. This paper describes the challenges the nonprofit organizations (NPO) in the welfare sector in Iceland face as a result of growing demands and financial uncertainty and how the economic downturn is expected to influence their roles, operational capability and managerial strategies.

This paper is based on preliminary findings from a national case study the authors are currently conducting. The study is based on qualitative data, both historical documents and semi-structured interviews with six general managers of nonprofit organizations, two of each category discussed in the paper, and six senior officials, three working for the central government in Iceland and three for local governments, all of whom interact with NPOs to some degree. In addition the data are based on documents describing the operation of twelve nonprofit organizations in Iceland (Kristmundsson, Hrafnsdóttir 2008).

Prospective changes in the operation of nonprofits were analyzed according to: a) demand for activities offered, measured in changes in the number of users, buyers, clients, members, etc.; b) the operational activities they undertake, measured by the increase or decrease in services, programs, changes in human and financial resources; c) prospective managerial strategies dealing with the changes; and d) relationships with governments (central and local). The last variable is analyzed according to Young’s taxonomy (2000). Different theoretical frameworks have been used to describe the relations between nonprofits and governments. Young describes three types of relations. According to Young *complementary relations* reflect collaboration between government and the third sector that carries with it mutual benefits; one party provides necessary resources, the other services or support. Due to nonprofits’ incentives and non-distributional constraints, the negative effects of information asymmetry between government and nonprofits should be minimal when compared to profit-making companies, thus promoting nonprofits as ‘trustworthy’ agents. *Supplementary relations* reflect the situation when nonprofits simply are responding to
unmet demands for public goods not fulfilled by the government. The important incentive of NPOs of establishing new welfare programs in the early 20th century in Iceland is an example of this type (Kristmundsson 2008). The adversarial relations describe when the two entities can be seen as adversaries in policy-making and provision of public services. A divergence of nonprofits and government is reflected in the former’s attempt to influence the policy-making of the latter. Instead, government tries to regulate its operations and advocacy initiatives.

An essential independent variable in discussing the economic effects on the third sector and its reaction is its primary mission as it reflects its working environment and the nature of activities, resources, and stakeholders, among other factors. Several taxonomies have been used to classify different types of nonprofit organizations based on activity, main source of funds and function. Here is a classification that was originally put forward by Charles Handy (1990) and further elaborated by Mike Hudson (2002). According to the authors nonprofits can be divided into three categories based on their primary mission:

- Service provision organizations (e.g. organizations operating nursing homes, youth centers and shelters for the homeless).
- Mutual support organizations (e.g. Alcoholics Anonymous and other self-help associations)
- Campaigning organizations (e.g. Amnesty International, environmental associations).

NPOs frequently fall into more than one category, for example it is common that organizations broaden their functional scope as they develop. However, this taxonomy serves the purpose of the analysis, namely to define the basic elements affecting the operational environments of the organizations involved.

This paper describes characteristics of each type of NPO in Iceland, how the economic crisis is expected to influence their operations and their managerial strategies.

**Iceland and its economic situation**
Iceland is a Nordic welfare state with an advanced public health system, social security and free education. Consequently Iceland has had high levels of public consumption in relation to GDP (25%) and was the fastest growing of the OECD countries in the past decade (Hagstofa Íslands 2008). Despite this Iceland has a large nonprofit sector in terms of numbers of organizations involved in public programs in health and social services (Hrafnsdóttir 2008). Iceland has received considerable international attention, especially related to the global recession and banking collapse. In the winter of 2008-2009 the country experienced the beginning of the deepest economic crisis since the country’s independence in 1944, the nationalization of the leading banks followed the collapse of the banking system in Iceland. A huge volume of financial assets was lost, the exchange rate of the Icelandic currency took a dive at the same time as interest rates skyrocketed. The country became the first Western country to apply to the IMF for emergency financial aid since 1976. These events have seriously affected the financial resources of both central and local governments. Presently (May 2009) the unemployment rate in Iceland is 9% compared to within 1% a year ago, inflation stands at 12.7%, the highest in 19 years (Fjármálaráðuneytið 2009). The central government budget deficit is estimated at 12.6% of GDP in 2009. Local governments are expected to experience comparable deficits. The central government is currently working on an extensive cut-back strategy.

The economic outlook for Iceland is poor (Fjármálaráðuneytið 2009). The financial system is not fully functional, currency restrictions are in effect and some international financial obligations are unsettled. In 2009 the forecast predicts a decline in national expenditure by approx 21%. Prices in residential housing will continue to fall rapidly while price indexed mortgages are creating a serious financial situation for a large proportion of households in the country.

NPOs providing welfare services in Iceland, characteristics and development

This type of organizations has received extensive academic attention in recent decades (see e.g. recent work on the subject (Light 1999; Kettl 2000; Salamon and Elliott 2002; Guo and Acar 2005; Agranoff 2006). This is not surprising given the emphasis on contracting as a dominant tool for public service provision. The impact of contracting has been well documented in academic research and linked to a long list of theoretical concepts that fall
under the umbrella term of new public management (NPM), like government by proxy, new public service, collaborative public management, public private partnership (PPP), government networks and third party government.

This development has created a “contract culture”. Even though the approach originally evolved from neo-liberalism and privatization efforts in the 1970s-80s –it has become part of the moderate politics practiced in Europe, evolved as well in social democratic countries such as those in Scandinavia (Eikås 2002).

This has been the case in Iceland – it is safe to say that Iceland has been a dedicated follower of fashion since the forming of a new government in 1991. Thus, in the spirit of Osborne’s and Gaebler’s catch phrase, “Steer but not row” (1992), attempts were made to create a buyer-seller relationship between the public administration on the one hand, and private parties or quasi-public institutions on the other. The legislative framework for contracting and tendering was thus formed.

NPOs providing services had an important role in welfare service provision in Iceland long before the advent of NPM. As an indication of the scope of the services 31% of the 2009 budget of the Minister of Social Affairs and Social Security was transfer payments to nonprofits and local governments, primarily the former, in accordance with existing contracts (Fjármálaráðuneytið 2008). The Ministry of Health is expected to use 10% of its budget to finance health service providers outside the central government, also to large extent nonprofits.

There are particular areas of welfare services which have historically been dominated by nonprofits, providing trust goods in a heterogeneous society. Those are services initiated by the institutions themselves which eventually lead to government support and financing (Kristmundsson 2008). Nursing homes for the elderly have largely been run by nonprofit institutions. Various facilities for the mentally and physically handicapped have also been operated to a large extent by nonprofits. Thirdly, treatment centers and halfway houses for drug and alcohol treatment have predominantly been run by the third sector. Lastly, a
variety of social and health services is partly run by nonprofit institutions or in cooperation with the government.

This includes habilitation and rehabilitation centers, day care centers, nursing homes for the elderly, sheltered workshops for the mentally handicapped, operation of ambulance services, rescue services, prevention, rehabilitation centers for diseases, and other specialized social and health services.

As the list above indicates the nonprofit institutions responsible for the welfare services in Iceland differs in types and scope. However, some basic characteristics can be found which coincide with the general textbook definitions of service provision nonprofit institutions (see e.g. Hudson 2002). They are in operational terms large, have a formalized structure, have been in operation for some time, and have a relatively large proportion of staff compared to volunteers, in some cases even a very limited number of volunteers.

Evidently, the primary source of revenue for nonprofit service institutions is public funding, either in the form of grants or service contracts. The second most important source of income is either private fees for services or membership and/or private giving from individuals or cooperation, especially in relation to special fundraising campaigns. There are also examples of large amounts of income coming from independent revenue sources like lotteries and gaming machines. Examples of nonprofit institutions of this kind are: the Icelandic Red Cross, that runs ambulance services, nursing homes for the elderly, shelters for the mentally handicapped and homeless people; SAA, the National Center of addiction that runs a hospital and detoxification clinics.

Since October 2008 several nonprofits have experienced an increase in the demand for welfare services, in most cases indirectly related to changes in the economic condition. This is also the case in other countries that are experiencing economic downturn such as in the USA, Ireland and Germany (Hasenfeld, 2009, Anheier, 2009a, Prize and McGee, 2009). This should not come as a surprise because of the well-known relation between the economic well-being of a nation and its health and social problems (World Health Organization 2009). Nonprofit institutions like the Icelandic Church Aid organization have experienced a
considerable increase in aid requests. During the first four months of 2009 the institution received three times more the number of requests compared to the same period a year ago. The aid consists of food and other necessities and includes counseling and even school supplies so that young children can go to school. The beneficiaries are to a large extent unemployed people and their families. Based on the economic forecast, including trends in unemployment, this demand is expected to continue throughout 2009 and 2010. Another example is programs offered by the Red Cross. In the period from October 2008 to May 2009 there has been a 40% increase in help line calls compared to the same period a year ago. The Red Cross has also experienced an increase in requests for financial support and secondhand clothes. The shelters for people with mental disorders have seen an increase in attendance. Several other nonprofit organizations have reported the same trend.

The changes in demand call for increased resources, both financial and human. The fact that government payments are the single most important source of revenue for nonprofits, a complementary and often complex relationship has been created between the central government and nonprofits. There are no signs that the government will terminate long-term contracts, but requests for amendments or revisions can be anticipated. It should be expected that the government will request that individual programs not considered basic be left out of or struck from the contracts involved. There are already some examples of amendments of contracts for example, the Icelandic Cancer Association got less contribution from the government than they expected 2009 and the same applies to SAA.

In addition nonprofits will be prompted to operate in new areas that are politically sensitive and reflect complex social problems, areas that are especially difficult to tackle under tight budget conditions. Such expansion of nonprofits may imply that “something is being done”, solutions offered. Helmut Anheier, the prominent scholar in nonprofit theory, calls this “mellow weakness scenarios” where “nonprofits are the fig leaf for a political world unwilling to address social problems in a serious way” (2009b).

Based on information from selected nonprofit organizations, household contributions have not been reduced as measured in constant prices (rather than in real terms). This is
supported by historical evidence from previous research on the influence of economic downturns on charities (Mohan and Wilding, 2009). There are also indications of a growing interest in volunteering. This can be explained by changes in some basic values held by the nation and expressed in greater civic engagement. It is, however, too soon to say if this will be a long-term trend. Previous instances of serious disaster in Iceland have shown a significant but temporary increase in solidarity and empathy.

In the period from October 2008 to May 2009 contributions from the for-profit sector have fallen dramatically simply because of the bankruptcy of several corporations which previously operated on the basis of a corporate social responsibility (CSR) scheme. NPOs that had previously been supported largely by this scheme are experiencing serious financial troubles. There are indications that the companies that still exist have been cutting their donations and are more selective in their contributions. The emphasis has been on supporting their local community—and on balancing their own budgets. To support this, Icelandic NPOs’ that provide assistance in the developmental countries have experienced severe difficulties. The government is decreasing their contribution to humanitarian aid abroad and has been cutting down their contributions. Many of the NPOs’ have used their reserve funds to be able to continue their operations and maintain their obligations. Because of the weak Icelandic currency all aid abroad is more than double expensive than before the collapse. Some projects abroad have been put on ice because of this.

There is no available information on the proportion of NPO income as return on investment in fixed assets, stock, bonds or mutual funds. Money market mutual funds, which had become one of the most popular investment alternatives to traditional deposit accounts in Iceland, closed for business, or lost their assets by government takeover, following the collapse of the banks. Several nonprofits had invested in the funds, as had their counterparts in Europe. In the spring of 2009, 60-70% of the deposits were recovered (in constant prices) and paid to the owners.

In the interviews with selected organizations it was clear that they were unsure, how the future would be. However, all of them had in responded to the crisis. They thought it was difficult to engage in long-term planning at this moment, although they were actually in the
Some of them were engaging in strategy planning looking at their missions and values and how to tailor their programmes more toward this. All were looking at their revenue base and developing innovative measures in fundraising. They had adopted hiring freeze, cutting travel expenses and not engaging in new projects in some cases. These responses are quite similar to research findings from Ireland where it was indicated that staff numbers had to be reduced and working environment adapted and the organizations were trying to find new ways of fundraising (Prizeman and McGee, 2009).

When asked what support the government should give NPO’s at this difficult time, tax exemptions for provision of public benefits was mentioned. Unlike several European countries, the tax system in Iceland does not allow private donations to be deducted from the income tax base before computing the tax owed. However, corporation has this benefit. Allowing private donations to be deducted from the income tax base is expected to increase Non-Profits resources.

The managerial challenges that nonprofit organizations providing services face as a result of the developments call for both short-term and long-term strategies. Several well-known strategies can be expected to be chosen:

1. Write or rewrite the existing contingency strategy. Popular portfolio maps (product portfolio map and value return matrix) can help the NPOs to find a balance between mission fit and economic viability (Anheier 2005). The analysis can lead to changes in mission concentrating on programs critical for the nonprofit’s existence and/or are resource attractive, vis-à-vis cutting programs with limited value to its mission or are resource attractive. As part of this work the structure of the revenue base will need to be analyzed; for example more emphasis on fundraising with focus on households rather than seeking corporate donations or additional contributions from the government could be necessary.

2. Improving economy of scale and scope by creating strategic alliances, pooling of resources or consolidation. Nonprofits in Iceland have already in recent years made
some effort to increase their economy of scale and scope, for example by establishing service centers to provide specialized services to individual organizations. A growing number has become “multi-functional,” providing a variety of services, operating mutual support groups and campaigning. The development of strategic alliances has been limited – however a new society for nonprofits in Iceland just established last fall is an example. Pooling of resources has been growing in the field of fundraising, however. So far Iceland has not experienced any consolidation of nonprofits. New franchising models are an option that has not yet been adopted.

3. **Strategy towards a more diverse revenue base.** Because of cuts in public grants – more selective contracting by the government and rapidly falling corporate support – nonprofits need to establish a strategy towards a more diverse revenue base focusing more on household donations. NPOs will press for tax exemptions for provision of public benefits. Unlike several European countries, the tax system in Iceland does not allow private donations to be deducted from the income tax base before computing the tax owed. However, corporations do have this benefit. Allowing private donations to be deducted from the income tax base is expected to increase NPOs resources.

4. **Change in human resources.** The managerial focus will be on cutting expenses by a hiring freeze, an increase in the number of part-timers, and cutting overtime and travel expenses. At the same time there will be more effort on developing the membership base and expanding the number of volunteers.

5. **Strategy towards government.** It is considered essential to build dependable complementary long-term relations with government. For this purpose NPOs will pressure for long-term contracts with price index changes.

6. **Use allocation mechanisms purposively,** like sliding fees, waiting lists, product bundling.

**Mutual support organizations**

Member orientation is the primary function of this type of organization. Included are self-help groups, interest groups, friendly societies, professional associations and trade unions. In
the welfare sector the first two are of special interest. Self-help mutual aid or patient groups have been growing in number in the latter part of the 20th century in response to the advent of the welfare state (Katz 1986). In Iceland the number of new mutual-support organizations accelerated in the 1980s and ‘90s (Hrafnsdóttir 2008). The exact number presently operating is not available but it can be expected that of the three types of NPOs discussed in this paper, the largest number belong to this category, though not in terms of financial activities (Jónsson 2006).

This development has been explained by the emergent awareness of the limitations of the welfare state to deal with complex social and health problems, the negative effects of “helping and healing” professionalization, and the awareness of the efficacy of mutual support groups. The theoretical discussion of social capital and civil engagement coincides with the function of mutual-support organizations. According to Katz (1986) “[t]he common element in all these activities may be called empowerment, the raising of the participants’ sense of control and environmental mastery.” (p. 9). This heightens both their ability to understand and react to professional recommendations and policies.

Examples of mutual support associations are the informal fellowship of Alcoholics Anonymous (AA) and related support groups and more formal organizations where mutual support is the primary function, in addition to some other activities like lobbying, dissemination and professional counseling like the Icelandic Diabetics Association, the National Autistics Society, the Icelandic counseling and information center for survivors of sexual violence and the Icelandic Association of Heart Patients.

Organizations of this type are normally informal and small measured in terms of financial activities. The resources include primarily volunteers. They rely on in-kind donations and membership fees. In some instances, as in the case of AA, external grants are not accepted. Bearing in mind the well-known relationship between the economic downswing and the prevalence of health and social problems (World Health Organization 2009) the number and members of mutual support societies can be expected to grow. This has been the case in previous economical global crisis (Mohan and Wilding, 2009). Substantial growth in the member pool can therefore be expected. As this type of organization is primarily driven by
volunteers and membership donations economic recession should not limit their expected growth.

The relations with the government have primarily been supplemental, that is, mutual support societies are primarily responding to unmet needs for public goods not fulfilled by the government. Some of the well established mutual support associations have been involved in policy making in addition to submitting opinion to relevant parliamentary bills. It is a standard work procedure of standing committees of the Icelandic parliament to seek opinions from nonprofit organizations in order to include this type when discussing relevant parliamentary bills.

As indicated above mutual support organizations do generally not rely on financial contributions from government. Some have, however, received minor general grants on annual basis. It is assumed that the government will cut grants of this type. Some of the managerial strategies of service provision organizations can be used for mutual support organizations. It can be anticipated that mutual support organizations will rely more on service centers in lowering administrative costs and donor and volunteer management. It can also be expected that campaigning and service provision organizations will merge with mutual support organizations to some extent.

**Campaigning organizations in Iceland, development and strategies**

In this case the term “campaigning organizations” refers to social movements that “provide the organizational and political mechanism for translating private concerns into public issues” (Anheier 2005, p. 286). Using Weisbrod argument (1977) preferences of heterogeneous groups are not reflected in public policies. Accordingly, minorities will unite to meet their own needs and, in addition, force government to respond to them by establishing new public programs. The relations between campaigning organizations and the government can at the same time be seen as adversarial. A divergence of nonprofits and government is reflected in the former’s attempt to influence the policy-making of the latter. Instead, government tries to regulate its operations and advocacy initiatives. In their first stages of operation campaigning organizations are informal and unstructured but can develop over time into large formal organizations. Examples of this type of organizations include
Throskahjalp, the National Association of Intellectual Disabilities, Samtokin '78, the National Organization of Lesbians and Gay Men in Iceland, the Icelandic section of Amnesty International and the Icelandic human rights centre.

The first two are multifunctional, involved in campaigning, mutual support and counseling. The number of advocacy groups, human rights organization and some special interest groups in Iceland has been growing since the 1960’s and 1970’s, as elsewhere. Some of these associations have become highly influential in policy making in Iceland, such as in services for the disabled. Patients’ and other member-oriented associations have gradually formed an umbrella of organizations that have become a powerful voice demanding to be heard, and insisting on a role in the policy-making process in order to influence new legislation (Margeirs dóttir 2001). Health and social legislation has formally recognized some advocacy groups, like associations for the handicapped, as deserving to be able to influence public policy-making, and representatives from these associations have been included in some policy-making bodies within the government.

In the winter 2008-9 a new social movement originated as a result of a growing discontent among civilians in Iceland. The reasons were lack of government responsiveness, action and dissemination of information as well as extensive public debt caused by government deposit insurance following the collapse of the Icelandic banks in the UK and other European countries.

This eventually led to street protests. Only once before have such protests taken place, namely in 1949 when the country joined NATO. Behind the protest were loosely organized groups that have not led to the formation of a structured social movement, with the exception of a small new political party, the Citizens movement, that received 4 seats of 63 in parliament in the election this spring.

The operational size of campaigning organizations is generally small; there is a limited number of paid but professional staff, for example in public relations. Volunteers are used for individual campaigns. This type of organization relies on member donations and other household contributions. In some instances the organizations receive minor general grants
from the government. In the case of associations like Amnesty International financial contributions from the government are prohibited.

The serious financial situation of a large proportion of households in Iceland will most probably lead to ongoing protests and other civil disobedience in the latter half of 2009 and 2010.

Accordingly one can expect an increase in the number of members of social movements that advocate social and economic change. The same trend is expected in campaigning organizations that focus on the protection of minority groups like people with low income and disabilities.

As with other types of nonprofits, relying on membership fees as an important source of income, their revenues as measured in constant prices should be in balance or even increase with a growing number of members. Because of the high rate of inflation in 2008 and in the first part of 2009 the buying power of their funds will, however, continue to shrink.

Iceland has not experienced a fundamental change in the adversarial relationship between campaigning organizations and government in recent years. It is however important to differentiate between the older and more established organizations that have already been influential in policy making and are frequently consulted or involved when policy changes and the more recently established action groups that expressing general discontent with the government. Some of the managerial strategies used for service provision organizations can also be expected to be used by these newer groups. This includes pooling of resources and possible consolidation to improve economy of scale and scope. Strategies towards organizing a larger membership pool to increase human and financial resources can be expected, in addition to the use of service centers to lower administrative cost.

**Conclusion**

The global economic crisis has created new unprecedented challenges for the third sector. In this paper NPOs in the welfare sector in Iceland have been described, their managerial challenges as a result of changing working environment. Three different types of non-profits were analyzed: NPOs providing services, mutual support societies, and campaigning
associations. The preliminary research findings indicate that the economic recession will have diverse effects on different kind of organizations.

Since October 2008 the demand for welfare services provided by NPOs has increased, more or less in relation to the economic situation. There are indications of larger memberships in mutual support groups. The growing interest in social movements in the last eight months is a result of dissatisfaction with the government that can be expected to last.

The growing demands on all three types of NPOs call for more financial and human resources. In the case of service organizations providing welfare services the largest single revenue source is government payments based on contracts. Historically, NPOs have provided services in several welfare areas based on informal complementary relations. Following the advent of NPM in the 1990s formal contracts primarily with existing service providers were entered into. There are indications that governmental funding based on formal contracts will be maintained but revised on the basis of what can be considered essential services. It can be expected that the government will put up for bid new programs dealing with complex social or health problems. The NPOs will instead press for long-term contracts with price index changes. NPOs will move towards a more diverse revenue base. Instead of corporate donations the focus will be more on household contributions, a revenue source that is predicted to be unaffected despite of the crisis. Both because of limited liquid assets and reliable investment options income from investment will be limited.

In addition to changes in income strategy other responses will include revision of the existing contingency strategy, efforts to improve the economy of scale and scope, and putting constraints on paid human resources instead of focusing on a volunteer base. The mechanisms of allocation will be used more purposively.

As the mutual support organizations rely primarily on volunteers rather than financial resources for their operation, the expected cuts in annual general grants and the substantial increase in their membership will not create serious operational problems. Campaigning organizations experience a similar situation as they rely on membership fees and other household donations and volunteer input. The two types of organizations must lower administrative costs by pooling resources and using service centers. Other types of cooperation with other NPOs can also be expected.
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