

# LEGAL REGULATION and NONPROFIT DEVELOPMENT: A Supply and Demand Approach

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## BACKGROUND: Legal Regulation of Nonprofits

- Legal regulation of nonprofits a neglected area of study
- Literature generally assumes regulation is always harmful to nonprofits
- But, systematic empirical studies scarce
- No coherent analytical framework exists.

## TOWARDS A CONCEPTUAL FRAMEWORK: I

- “New institutionalism” theory offers a possible solution
- Focus on concept of “**transaction costs**,” the costs of creating and operating institutions
- **The higher the transaction costs, the less likely particular institutions are to form.**

## TOWARDS A CONCEPTUAL FRAMEWORK: II

- **Most discussion of nonprofit regulation focuses on the “SUPPLY SIDE”**
- **But transaction costs also operate on the “DEMAND SIDE”**

## TOWARDS A CONCEPTUAL FRAMEWORK: III

- Viewed through this lens, it becomes possible to rank and measure regulations:
  - Demand-side regulations can be positive—e.g., by promoting trust
  - Supply-side regulations can be more or less harmful.

# Factors Affecting Demand For Nonprofit Services: BUILDING TRUST

LEGAL PROVISION	EXAMPLES
<b>Non-distribution Provisions</b>	<ul style="list-style-type: none"> <li>• Prohibition on distribution of profits</li> <li>• Personal benefit restrictions</li> <li>• Capital lock</li> <li>• Conflict of interest restrictions</li> </ul>
<b>Transparency Requirements</b>	<ul style="list-style-type: none"> <li>• Reporting requirements</li> <li>• Public access to information</li> </ul>
<b>Governance Requirements</b>	<ul style="list-style-type: none"> <li>• Responsible agent</li> <li>• Participation requirements</li> <li>• Fiduciary responsibilities</li> </ul>
<b>Fundraising Restrictions</b>	<ul style="list-style-type: none"> <li>• Registration or permit requirements</li> <li>• Substantive restrictions (e.g., fundraising costs)</li> <li>• Truth in advertising provisions</li> </ul>

## Factors Affecting Supply of Nonprofit Organizations: ATTRACTING NP ENTREPRENEURS

- Organizations come into existence when the benefits of creating them exceed the costs
- Three broad sets of legal provisions affect these costs:
  - ✓ General legal posture
  - ✓ Establishment rules
  - ✓ Financing provisions

# Supply: GENERAL LEGAL STRUCTURE

- **Right to associate**
- **Allowable purposes:**
  - ✓ General vs. narrow
  - ✓ Common law vs. civil law
  - ✓ Appeal procedures
- **Allowable political activities:**
  - ✓ Advocacy
  - ✓ Lobbying
  - ✓ Electoral activity

## Supply: ESTABLISHMENT

- Incorporation procedures
- Membership requirements
- Capital requirements
- Government permission and/or involvement on boards
- Government discretion in granting legal status
- Appeal procedures

## CONCLUSION

- Regulation can stimulate NPs, not just constrain them.
- But a conceptual framework needed to assess this.
- New institutionalism and concept of transaction costs could help.