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## **COORDINATION AND INDICATIVE PLANNING IN THIRD SECTOR: SOME BRIEF CONSIDERATIONS**

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*Discussion paper*

In this brief talk regarding Third sector I have stressed the usefulness of broadening the scope of the independent Authority responsible for this sector in order to establish general regulation through indicative planning, allowing for large firm autonomy and using mathematical models.

**1.** - The analysis of non-profit firms clarifies many theoretical problems according to the nature of the goods and services produced and to their specific and important role in the Welfare economy.

It must underline the prevailing nature of the “merit goods and services” produced by these firms.

**2.** – During the 1960s and 1970s economist of different orientation disputed the nature of economic planning in a market economy and its application in Italy. One aspect of the debate was the role of analysis of private and public consumption. Some economist assigned much importance to this in order to improve income distribution; satisfy the “merit goods and services” demand not satisfied by the market and achieve a higher goal, for example, public Education and scientific research.

The economic planning debate has not analyzed the non- profit firm role in the satisfaction of social consumption carefully enough. In the past non-profit firms were not as significant as they are today.

**3.** – The true problem is not choosing the right balance between public and private consumption, giving more weight to the former, but assuring the best social needs satisfaction through an increase in production by non-profit firms and a decrease in State “merit goods and services production”.

In the developed Countries, during the 1970s and 1980s there were two conflicting objectives: to satisfy higher social needs demand by public expenditure and to lower are increasing public debt, without rising taxation to follow a development policy.

This contradiction can be overcome by increasing non-profit firm production of “merit goods and services” and at the same time lowering the public production of such goods and services. In this way the Government can increasingly finance non-profit firm production in order to satisfy social need.

This situation calls for a serious social revolutionary transformation that could become ever more important in the near future.

I think that this economic evolution requires revision of traditional economic categories: for example the inclusion of altruistic individual preferences and not only self-serving ones.

4. – As well the complexity of the economic mechanism also means that the range of human motivation and behavior is very broad: it is therefore not possible to consider only selfish individual preference in economic models.

According to Musgrave<sup>1</sup>, for some community members we can replace individualistic preferences with “community preferences” that permeate through the commonly accepted values of these members throughout history.

I can, for instance, give a voluntary contribution to set up a cultural event, like a classical music concert even if I prefer another type of music.

This preference type is particularly related to cultural goods, education, environmental protection and so on.

Musgrave, in talking about the voluntary donations for relief destination, refers to the related preference type as “paternalism in the distribution”: indeed there is an “imposition” of tranferentes preferences upon the receives. On the contrary when there is money transfer their preference can be satisfied according to their tastes.

According to Musgrave the “paternalism in the distribution” is also more important when a majority decision, in order to set up a State financed project, must be taken. The majority of voters “paternalistically” imposes the public project execution. The Harsany distinction between ethical and subjective preferences is also very valuable. Specifically the former express the human point of view about what must be done, according general interest and personal interpretation. On the other hand, the latter express individualistic selfish preferences.

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<sup>1</sup> Musgrave R.A. “Merit Goods” in “The New Palgrave’s Dictionary of Economics”, 1987.

In conclusion, with reference to the non selfish preferences I should like to point out the distinction – following J. Brennan and L. Lomasky<sup>2</sup> - among market preference (m- preferences) and preferences regarding a vote situation. The former are a form of selfish utility and have a specific opportunity-cost: if I purchase a given commodities combination and spend the whole budget, I cannot buy another combination. The latter are general-interest based and do not have a well defined opportunity-cost.

5. – The above considered non selfish preferences are particularly valuable in relationship to the so called “merit goods and services” regarding mainly Health services, social services, Education and Environmental protection, all very valuable from a social point of view. Such goods and services are produced mainly by non-profit firms.

In order to undertake a systematic analysis of non-profit firms, I must consider the non selfish preferences.

The meaning of “Third sector” depends on its intermediate position between the public and private “for profit” sectors.

Generally speaking the opportunities for the Third sector are two fold.

The first motivation is set in relationship to well known “market failures” depending upon various factors such as the insufficient reductivity of some goods production; as, also, the existence of information asymmetries. There are, also, the “State failures” regarding the inefficiency of the public management; its tendency to meet the demand of the median elector, in the statistical meaning of this word, with consequent dissatisfaction of the electors that prefer a superior or inferior public production level; and finally for the low differentiation in the quality of public goods and services produced.

The second motivation moves more from historically-sociological considerations than by theoretical-efficient explanations.

It considers the importance of the general value of solidarity and of other ethical-social finalities in the working of non-profit firms belonging to Third sector: they develops, therefore, an autonomous role, highly positive, not supplementary in comparison with the other two sectors.

I should like to make some general considerations about the historical roots of Third sector.

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<sup>2</sup> Brennans-Lomasky L. “Institutional Aspect of Merit Goods Analysis” in “Finanzarchiv”, vol. 41, n. 2, pp. 183-206, 1983.

6. – Following Velo<sup>3</sup>, before the industrial revolution, the main society values was the solidarity and the “reciprocity principle” in the exchange so formulated: “I give you today, and you shall give me in the future”.

The economic principles of that society was very similar to the motivations and values of Third sector today.

After the industrial revolution, with the development of market economy, the area of solidarism and reciprocity tend to reduce: the new economic system stimulates and valorized the selfish individualism that is in every man.

The solidaristic attitude was transformed in a generic attitude to collaboration and to mutual trust.

The new age, incoming in England in the XIX century and, after many decades, in the most important European Countries.

The most important consequence of the industrial revolution was the prevalence of economic relationship upon other social relationship.

But the solidaristic attitude do non vanish: the strong income inequalities, generated by the new productive reality, stimulates solidaristic answer through the foundation of new institution related to Social Assistance.

After some time, according to the high social demand of goods and services, was founded other Institution in Education, Health and so on. Therefore born Third sector in order to satisfy the increasing social needs.

Historically the development process of Third sector was stimulated by the keynesian model crisis, in the 1960's. Indeed this crisis was a reaction against the excessive statalism of the preceding period.

There is a general development of the “subsidiary principle”, that European Union sets has adopted as the main principle in the Union organization.

This principle has regulated the relationship between the State and non-profit firm and has been a growth factor of Third sector high relevant.

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<sup>3</sup> Velo D. “Terzo Settore, Nuova Statualità e Sussidiarietà” in “Ecoomia e Diritto del Terziario”, n. 3, 2001.

7.- Third sector development must be considered from a more general point of view. In fact the “Third Industrial Revolution” progressively being carried out in relation to the new technological paradigm (microelectronics, information theory, telecommunications, new material production, biotechnology and so on), increases technological unemployment especially in the short and medium run. This unemployment, can sometimes be reduced, in the long run, in accordance with a general settling down of the economic system.

At the same time, growing social needs must be satisfied through “merit goods and services” production.

In many developed economic Countries, given the high public debt, the State cannot satisfy these social needs directly, with its own production.

In the meantime the “for profit” firms are attracted by other more profitable, production sectors.

Therefore, in developed economic systems, there is simultaneously high unemployment and a growing, unsatisfied demand for social goods and services. Thus a new unemployment equilibrium modality (very different in comparison to the Keynesian model) is required since the market system cannot satisfy these conflicting objectives by itself.

To overcome this state of affairs, the development of Third sector, in the production of social goods and services, is the best solution, also from the perspective labour occupation.

In relation to this latter point we must note that, even if there is not an automatic and self regulatory mechanism for overcoming the problem of technological unemployment, certainly increased development of Third sector can substantially lower this kind of unemployment.

Indeed, in the 1986, in the United States of America<sup>4</sup>, about 7.700.000 workers were employed in Third sector, correspond to 7,14 per cent of the total workforce. In the last seven years the employment growth rate in Third sector has increased by 3,17 per cent, per annum; in the meantime total employment has increased by only 2,34 per cent.

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<sup>4</sup> Hodgkinson U.A.- Weitzman M.S. “Dimension of the Independent Sector Statistical Profile”, Independent Sector Publications, New York, 1988.

In the other developed economic Countries, following a recent statistical research<sup>5</sup>, based on a unified definition of non-profit sector, the employment in Third sector is, in USA 6,8% of the total; in France 4,2%; in England 4%; in German 3,7%; in Italy 1,8%. The Eurostat statistics say that in E.U.<sup>6</sup> there is a percentage of 2,8%.

In Countries, like Italy, with a less developed Third sector, the employment rate has been growing very fast in the last ten years.

**8.-** I should like to make some general comments about the Social market related to Third sector.

Initially I shall consider only the three main subsectors belonging to this sector: Social Assistance, Health Services (especially drug-addiction and other social diseases) and some special forms of Education.

These three subsectors are very different from the point of view of non-profit firms: they have different types of public and private financing; moreover in the first subsector there are generally no prices. The price is paid only if the State provides a voucher or a proxy-shopping service to potential consumers. Sometimes there are normal-income consumers who pay a positive price.

In the other two sectors, however, the price can vary in terms of the personal income of the consumers: the highest price, paid by higher income consumers, is normally a full cost price; the lower price, paid by low income consumers, is equal to zero.

The State subsidizes Third sector primarily in order to satisfy growing social needs; secondarily because employment in this sector reduces unemployment in the whole economic system.

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<sup>5</sup> Eurostat, "A Statistical Profile of the Cooperative, Mutual and Non-profit Sector and its Organisation in the European Community. Preliminary Issue" in "Services and Transport", Supplement 2, 1993.

<sup>6</sup> Anheier H. K.- Salamon L. M. "The emerging Sector. An Overview", The John Hopkins University, Baltimore, 1995.

In order to best fulfill the latter aim, the Government must estimate the technical labour coefficients in each of these three subsectors, considering the different circumstances of the firms belonging to these subsectors. By considering the technical labour coefficients and the employment goal, Government divides the financial resources between sectors and firms.

But this distribution must also consider the social services goals that the Government would like to achieve.

These two different goals, employment and social services production can conflict with each other: for example a firm can have high quality production in some social services but employ few workers.

Therefore there is a normal conflict between these two goals. To resolve this trade-off, some multiobjective programming using mathematical methodology may be useful.

The Government, when distributing resources, must also distinguish between various non-profit firms from a legal and institutional point of view: for example in the same subsector we find IPAB, Foundations, Social cooperatives, etc.

A last remark: in order to stimulate private firm contributions, the Government can give a supplementary contribution to each firm in proportion to the received private contribution: otherwise the private contributors will not be interested in supplementing the State contribution if they think that the Government is giving the necessary contribution to each firm.

**9.-** The Authority regarding Third sector, recently founded in our Country, in my opinion could enlarge his scope: it could put in practice an indicative economic planning, leaving a large autonomy to the firms, but to supplement the relative lack of true market mechanism.

The main finality of such an indicative economic planning in the best use of economic resources in Third sector. For example this Authority could detect the opportunity to satisfy new social needs: it could stimulates new and old non-profit firms to undertake a new production of goods and services to satisfy the new social demand.

The Authority could analyse the best distribution of the State financial fund to the firm, in accord with government authorities, and to check the correct firms use of these financial support.



In order to fit this planning problem, avoiding a bureaucratic model, could be useful to apply some mathematical model. Could be worthwhile consider the “mechanism of resource allocation” proposed by Hurwicz<sup>7</sup> and by other authoritative researchers.

I think that, in order to determine the optimal division of State financial fund among the firms, these must calculate the “shadow price” of the financial resource. In equilibrium the “shadow prices” calculated by each firm, must be equal. Each “shadow price” represent an index of the marginal value of the financial fund assigned to that firm.

**10.-** I must point out that the application of a mathematical model to the problems that I have indicated earlier is not a panacea: for example it is very difficult for firms to provide all the information necessary to implement the analytical procedures.

Generally the founded mathematical solution is only a useful reference point for further elaboration. The real complexities of economic life make it impossible to apply simplistic models. The reality is beyond these hypotheses.

Nevertheless the mathematical models applied to economic problems can highlight the logical nature of these problems and help in finding not necessary the optimal solution, but perhaps a “satisfying solution” in the sense of H. Simon.

The financing scheme I have considered only concerns the State budget.

The regions and the municipalities can also finance non-profit firms.

I thinks that State financing is the main form of fund distribution to Third sector firms and that other public financing has only a supplementary function.

In this brief talk I have proposed to broaden the scope of the independent Authority regarding Third sector. I have also proposed the application of mathematical models to Third sector economic analysis.

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<sup>7</sup> Hurwicz L. Walker M. “On the Generic Non-optimal of Dominant-Strategy Allocation Mechanisms with an Application to pure exchange Economics”Mimeo, University of Minnesota, 1983.