Innovative IC Framework in the Non-Profit Sector

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ABSTRACT

The importance of the intellectual capital in non profit sector generates the need to measure its role in the value creation process. The purpose of the paper is to study the application of intellectual capital within the non profit sector, by turning attention to resources such as: knowledge, experience and skills. Organizations, which are able to increase the knowledge of their staff and to transform this knowledge into skills to improve services, can easily meet users’ needs and, thereby, become competitive. This contribution proposes to study how people’s knowledge can contribute to increasing social value, which is the aim of the non–profit organization. Furthermore, the goal is to demonstrate how collaboration between staff and volunteers is essential to a professional service. Finally, the research proposes a conceptual framework in which intellectual capital helps in defining the strategic issues, which non–profit organizations must tackle in order to achieve their social programs.

Keywords: Intellectual capital; Non-profit sector; Strategic management; IC framework; Value Creation; Performance

INTRODUCTION

In recent years, the importance of intangibles in the process of value creation has emerged with ever greater emphasis. Intangibles, as a resource without physical substance, are a key driver underpinning business competitiveness.

The definition of intangibles is still an open question (Zambon, 2004; Marr et al., 2004). We often speak about intangibles, intangible assets or, even, intellectual capital. The importance of intangible assets, including intellectual capital, i.e. the body of knowledge, organizational and interpersonal skills, has created the need for the non-profit organizations (NPOs) to assess their role in the process of value creation. In fact, in contrast to what happens in other sectors, where everything is measured quantitatively, in the non-profit sector the importance of communicating and demonstrating to stakeholders the quality of services provided, compared to the offer of other for-profit public or private subjects, is crucial to generate social value (Stewart, 1997; Benz, 2005; Drucker, 2006). "Social actions" have become really important, both in terms of efficiency and effectiveness. As for efficiency, reporting on the relationship between the achievement of results and the use of resources has become necessary to ensure the survival of the non-profit organization over time. Testing the effectiveness (i.e. the ratio between results and expected outcomes) is more complicated: effectiveness involves an evaluation of the quality of the organization’s work, and this is not achieved simply by considering the economic value of resources exploited (Baruch & Ramalho, 2006).

The services provided by NPOs are generally intangible and have a significant relational content (Fiorentini, 1997); they are characterized by close interaction with the final user and hence are difficult to standardize. Therefore, any reliable assessment of their quality must take account of the relational component and especially the close relationship between the provider (employee or volunteer) and the client (Cafferata, 2000). In many cases, in these relationships, the parties involved (users/volunteers/employees) do not interact in opposition, but in concert to achieve a common goal (Bennett & Barkensjo, 2005).

The quality of an NPO depends, above all, on the skills of its operators (in most cases volunteers), in particular on their ability to combine and exploit the experience and knowledge present in their organization. Knowledge becomes a major production factor (with land, job and capital), essential for any organization. (Azzariti & Mazzon, 2005).

Regardless of the sector it belongs to, every NPO must be able to develop, enhance and manage the knowledge resource, in other words the creation, exchange and sharing of ideas and values; knowledge, defined as such, becomes a key component of the NPOs competitive advantage (Hustinx & Lammertyn, 2000). The knowledge and skills possessed by the NPO and, therefore, by the NPOs representatives are of crucial importance and NPOs that can increase the knowledge of its collaborators and to turn this knowledge into skills, in terms of improved services, are in a better position to meet the needs of their users and, therefore, to become more competitive. In this sense, workers are increasingly seen as knowledge workers. The goal of knowledge management is actually practical: to improve organizational capabilities through better use of the organization’s individual and collective knowledge resources (Probst Gilbert, 1998).

This paper, through a conceptual framework, aims to study how knowledge resources help to provide the NPO with competitive advantages and, in particular, the role played by knowledge management in creating business value.

EVOLUTION OF THE THIRD SECTOR

The third sector includes the new model of Welfare State based on public service, but increasingly characterized by important private initiatives.
The term “third” (as well as “non-profit”, or “tertiary”) sector, actually houses a number of large and different realities that range from healthcare, to education, culture, charity, international cooperation, and so on (see Table 1 in the Appendix). The reference frame is therefore very broad and diverse and it is characterized, at least in part, by a fragmented legal framework whose only common denominator is the absence of the profit motive as a driving force (Cohen, 2007). The relegation of profit does not mean that a non-profit organization cannot make a profit, but it means that a limitation is imposed on it. In fact, an NPO cannot distribute revenues to shareholders, but rather re-invest any gains in social purposes.

One of the main reasons leading to the growth of the tertiary sector is undoubtedly linked to the crisis of the Welfare State (Malerba, 1994). In many Countries the central government, under the pressure of rising costs and financial problems, has not been able to provide citizens with assistance in key areas such as education, health and so on (Matacena, 2000). As a result, therefore, some important functions passed from the public to the private sector, albeit under the rules and guidelines imposed by the State through a system of incentives. The insufficiency, and in some cases, the inefficiency of some inadequate and obsolete public bodies led many people, for instance from the voluntary sector, to establish private organizations, pursuing goals of social solidarity, to fill the role the State was no longer able or willing to provide (Ozcelik & Kaynak, 2009).

The phenomenon of non-profit has grown not only because of the crisis of the Welfare State, but also because of a variety of factors, among which we can include:

- economic development which, in addition to rising incomes, increased spare time so that each individual has been able to undertake sports, cultural, recreational, and above all voluntary and charitable activities;
- the emergence of new needs and, therefore, the demand for new and different specific and more customized services;
- increasing attention of the government towards the development of the tertiary sector in order to support both employment and economic growth.

This situation has been favored by the spontaneity and good will of many citizens, who have joined together in groups (associations, cooperatives etc.) in order to provide answers to serious problems: diseases, social problems, unemployment, loneliness, etc. (Chaminade & Catasus, 2007).

The economic and financial inability of the State to respond to the growing social needs of the community, together with the inability of the profit-oriented organizations to combine economic objectives with accountability in the social field, created a gap between State and market, leaving an ample space to private initiative.

THE VALUE OF KNOWLEDGE FOR KNOWLEDGE–BASED ORGANIZATIONS

In the current economic context, companies, in order to address the needs expressed by the territory, have to accumulate specific knowledge to give consistent responses to the changing needs of the community.

In the knowledge-based organizations, the relationships with users are not guided by the market, but become a partnership in which the solutions are created together and knowledge flows in both directions (Minbaeva, 2007). Knowledge is destined to become the most important input and main output of the production process. We could say that the economy is the production of knowledge by means of knowledge.

In the knowledge economy, characterized by a demand for high quality human capital, subject to rapid change and new technologies, the skills possessed by individuals increase productivity, quality of life and, therefore, social welfare (Sveiby, 1997). This is especially true for NPOs, that work closely with users, and are closer to their needs.

Knowledge management becomes a key resource, perhaps the only source of NPOs’ competitive advantage. For this reason, more and more organizations are looking for new tools to increase this resource in the pursuit of excellence. It is through formalizing and sharing the available knowledge, that people connected with an NPO (either user, employee or volunteer) will be able to operate at their best, and to consciously exploit the experience and ideas gained hitherto by the entire community. The continuous exchange of ideas, information and knowledge contributes to an ongoing increase in the organization’s social value (Ammann, 2008).

Knowledge is a good with different characteristics from other economic goods. It affects the performance and competitiveness of companies and can lead to an increasing employment and, as a consequence, to economic growth. The use of knowledge as a resource contributes decisively to generate and secure new competitive advantages for for-profit organizations, while for the non-profit sector (the aforementioned third sector) it is reflected especially in the creation of social value for stakeholders.

THE DEVELOPMENT OF KNOWLEDGE MANAGEMENT IN THE NON-PROFIT SECTOR

The techniques of Knowledge Management (KM henceforth) have been applied, almost exclusively, to commercial organizations for a long time. Only recently the awareness that KM, if properly managed, can supplement the overall strategy of the NPOs, has been increasing among people.

As a result, the non-profit sector, far from being marginal and relegated to secondary activities, is becoming increasingly important as well, in ensuring the levels of Welfare the State fails to deliver and, on
the other hand, the private sector tends to overlook. NPOs have to combine ethical and cost criteria and have to be able, therefore, to cope with specific social needs, to plan operations and achieve results while pursuing the effectiveness, efficiency and ethical behaviours. The proper management of these factors would allow the organizations themselves to be more competitive and successful. In a context where competition is the main key to success for the NPOs, managing their intellectual assets is essential. In fact, due to the rapidly changing environment and excessive reduction of public funding, the NPOs have begun to look for new ways of gaining competitive advantage. One of these sources of competitive advantage is knowledge.

Knowledge becomes useful only when it loses its individual value to become, through sharing, collective heritage of the NPO. Knowledge provides a competitive advantage to the NPO only if it is shared by all members, or most of them, since it cannot be easily separated from the individuals possessing it (Blair, 2002).

In light of this, many NPOs are using their intellectual capacity and beginning to implement KM programs for the strategic management of knowledge. KM is the process through which the NPO collects, organizes, shares and analyzes knowledge in the form of documents, data, information, resources and personal skills. In other words, KM can be interpreted as a system of management practices designed to better manage the knowledge contained within an organization (Vitner et al., 2011). It takes into account both tangible (research and development, patents, customers and suppliers databases) and intangible assets (experience, skills), and guarantees their transfer and sharing among all members of the organization.

THE DETERMINANTS FOR THE DEVELOPMENT OF KNOWLEDGE MANAGEMENT IN THE NON-PROFIT SECTOR

To enable effective knowledge management dynamics, it is necessary to promote initiatives aimed at quickly and easily circulating data and information within NPOs. At the same time, the circulation and sharing of large amounts of information can facilitate the interaction of individuals, creating ongoing opportunities for exchanges and, more in general, new knowledge.

As knowledge cannot be separated from the individuals possessing it, each member of the community, whether volunteer or employee must provide the others with at least a part of its knowledge; only then will a two way exchange process be possible. Knowledge has a greater value when the members exchange it through interaction. What really counts for KM is people's willingness to consider the knowledge held as an asset to be shared within the organization or group they belong to. All this requires the attention of the people who manage the organization.

According to Teece (1998), sharing knowledge can often be the basis of competitiveness of each organization and the non-profit sector can use KM to be an active part in global competition.

Knowledge represents what is often identified as intellectual capital or knowledge capital of the company (Carlucci & Schiuma, 2006; Schiuma, 2009; Stewart, 2001; Roos et al., 1997; Nonaka & Takeuchi, 1995). It is not reasonable to think of a growth of the tertiary sector without making adequate investments in knowledge and, thus, in human capital. To this end, it is important to emphasize the diversity of the people employed in the NPOs. In addition to employees, there are volunteers, conscientious objectors, supporters and religious figures who share the values and purpose with the organization. In this context, the KM strategies fit with a specified aim. They promote the integration of different subjects and the creation of their strong sense of belonging to the community. The creation and maintenance of a given human capital allows the NPOs to develop new ideas, new knowledge and new innovations (Kong, 2008).

The heterogeneity of NPOs' human capital is a source of infinite creativity and value, despite its lack of formalization. Even in this case, it is necessary to implement appropriate KM strategies (Edvinsson, 2006). The objective of KM is to carry knowledge beyond the individuals’ perspective, in order to make it a collective heritage. When this is done, it will be easy to distribute the set of skills, individual and collective knowledge, both within and outside the community. Such this new knowledge, thus created, must be constantly enhanced to avoid becoming lost.

THEORETICAL AND OPERATIONAL INSTRUMENTS FOR THE MANAGEMENT OF KNOWLEDGE IN NPOs

Knowledge can be classified in many ways (Zack, 1999; Blackler, 2002), but the main distinction is the one between tacit and explicit knowledge. We define tacit knowledge as the one coming from and closely rooted in the experience of the individual subject; it is difficult to formalize because it has a strictly personal matrix. It is important that all NPOs deploy strategies to enhance the tacit knowledge, so that each individual feels encouraged to express it to others and, above all, to share it and thereby create value. Alternatively, we can speak of explicit knowledge with reference to the knowledge that can be easily stored, transmitted and shared, even outside the context where it was conceived. It is contained in formal documents such as, for example, simple instruction manuals, documents, daily practices. Unlike tacit knowledge, the explicit one needs to be constantly updated by the NPO in order to avoid becoming out of date.

The distinction between tacit and explicit knowledge, and the flow of knowledge among the members of an NPO, inevitably lead us to consider the model of knowledge management developed by Nonaka and Takeuchi, through which the continuous
interaction of knowledge creates new knowledge (Nonaka & Takeuchi, 1995). According to this interpretation, an NPO cannot create knowledge without individuals. Thus, it becomes important to support the knowledge that is inherent in the people who offer their services to the NPO.

KM has to take action to better exploit the knowledge contained within an organization in order to develop it in line with the needs expressed. Knowledge, whether tacit or explicit, becomes valuable when all members of the group can share it. In NPOs, given the multiplicity and diversity of the members of the community and the less formal environment, the circulation and communication of knowledge become an easy matter as the members themselves do not tend to hoard their knowledge, but they prefer to transfer it to others. In this context, the flow of knowledge can lead to improvements in performance through the creation of new ideas and new knowledge, thus enhancing the intellectual capital of the NPO (Sveiby, 1997).

Knowledge is part of the Intellectual Capital and an element of the so-called human capital, so it makes up a good part of structural capital (Curado & Bontis, 2000). The relational capital is excluded from the concept of knowledge, as long as the NPO is considered as an entity in itself. Instead, when the NPO is considered as part of a larger social reality, we comprise in it all those relationships that can provide an easy matter as the members themselves do not tend to hoard their knowledge, but they prefer to transfer it to others. In this context, the flow of knowledge can lead to improvements in performance through the creation of new ideas and new knowledge, thus enhancing the intellectual capital of the NPO (Sveiby, 1997).

INTELLECTUAL CAPITAL IN THE NON-PROFIT SECTOR

In recent years, the number of non-profit organizations that have interpreted the assessment of their intellectual capital as a management tool in order to improve decision-making and financial management.

Intellectual capital, defined as the intangible assets of an organization, is now recognized as a fundamental element from which value added derives. For this reason, it is important to analyze it carefully. In fact, the intellectual capital of the community built around a specific social problem is heterogeneous, distributed among various stakeholders, little formalized and volatile (because of the condition and the high turnover rates for volunteers). Creating a unique intellectual capital, formal and usable by each member of the community is one of the key challenges for NPOs. The adopted approach identifies a three-fold partition of intellectual capital into: human capital, relational capital and structural capital (Edvinsson & Malone, 1997).

As regards human capital, it is a very important feature for companies operating in the tertiary sector, which are characterized, in general, labor intensive. The management of human resources is a very delicate element to which managers should pay particular attention, because it strongly influences the proper functioning of the organization. In fact, NPOs’ human resources have unique characteristics not found in commercial ones. We can identify two different categories of workers: volunteers and paid staff. In order to make full use of these two categories, managers should be able to ensure that paid staff and volunteers work together (Bandini, 2003).

The second dimension of intellectual capital concerns: (i) structural capital, made up of all knowledge present within a company; (ii) the organizational structure, operating procedures and corporate databases, all of which have a significant importance also in not-profit organizations. In particular, the organizational structure and operating procedures represent the reference frame for the proper functioning of a company, since they define the subdivision of activities and the exact methodology to be used in the work performance (Joia, 2000). Databases are the information assets of a company, which managers have to pay particular attention to, by building a set of indicators to allow their measurement. Among available variables to assess structural capital are the corporate culture, the ability for change and innovation, the Internet and the network. (Davenport & Prusak, 1998).

The third component of intellectual capital is the relational capital, represented by all the relationships existing between the company and its stakeholders. A non-profit organization creates a competitive advantage when it focuses on creating value for the user, that is to say the ability to produce wealth for the user itself (Cavenago, 2004). In the non-profit organizations, relational capital covers, among other aspects, the communication system, client satisfaction, feedback and the corporate image (Andriesson, 2008). The communication system is important because the non-profit organizations must have a deep understanding of the users’ needs and, therefore, must create a relational and communication system that is able to perceive in real time the changes in demand (Bonacci & Tamburis, 2010); as a result, it will be able to create services and actions in order to build customers’ loyalty and to satisfy their needs.

IC FRAMEWORK FOR THE KNOWLEDGE TRANSFER AND VALUE CREATION IN NPOS

The introduced theoretical approach may be helpful to build a framework to demonstrate how the sharing of knowledge provides high competitive advantages, improves performance through the creation of new ideas and new knowledge, enhances the intellectual capital and contributes to value creation (Teece, 1986). The human intensive nature of NPOs causes the growth and permanence with time of these organizations, which are increasingly based on intangible assets rather than on traditional ones (e.g., physical assets and financial capital). From this perspective, the skills and knowledge of the people who participate, in one way or another, in the NPO, are the key factors in which to invest.

Knowledge creates new knowledge when correctly managed; thus, it has to be recognized as a
strategic asset that can lead to success when it is disseminated through the organization and is incorporated into the products and/or services that it offers (Boisot, 1998; Bontis & Choo, 2002). The proper flow of knowledge creation and dissemination within an NPO engenders fresh opportunities for the creation of new knowledge (see Figure 1 in the Appendix). Knowledge management becomes the key resource and, perhaps, the only source of competitive advantage. For this reason, there is an increasing number of NPOs in search of new tools aimed at increasing and accumulating this resource. Knowledge comes from the combination and elaboration of experience, values, information, skills and feelings that, through a process of abstraction and generalization, can be applied even in different areas. To ensure an effective management of knowledge, information must circulate; in fact, what really matters is the willingness of people to consider the knowledge held as a resource to be shared, rather than individually improved.

In order to manage the knowledge resource in a strategic way, KM needs to support communication initiatives and collaboration among individuals. It promotes continuous opportunities for exchange and creates the necessary conditions so that each person, regardless of one’s role, can quickly and easily access previously unavailable data and information; at the same time, their use at various levels becomes possible. Sharing information flows becomes therefore essential both for the creation of new knowledge (Moore & Brown, 2000) and for the replacement of the obsolete one; hence, KM strategy must move in two directions: the revision (or elimination) and continuous updating of existing information, on the one hand; the acquisition and incorporation of new information, on the other hand.

Through the theoretical framework suggested in this paper the role of intellectual capital in the NPOs is analyzed. In fact, the interaction among the three IC components (HC, RC, SC) within the NPOs creates new knowledge which, once learned and shared inside and outside the organization, generates new external knowledge; this one, in turn, together with the maintenance of the internal knowledge (Moutrisen et al., 2005), provides sustainable competitive advantages and contributes to value creation. The interaction of the intellectual capital components allows the NPO to carry out its specific activities, and to marry strategic objectives and social mission. The framework also shows the importance of external knowledge (external input) and the loss of internal knowledge (internal input). It should also be noted that the latter is not only identifiable in the knowledge held by individuals who are part of the NPO, but it is also found in the manuals, documents, and everyday practices, i.e. in the organization itself.

As said before, both internal and external knowledge are often identified as intellectual capital or knowledge capital of the organization (Bontis, 2000; Edvinsson & Malone, 1997); the latter term, in particular, is used to set forth a somewhat wider concept; to this end, Figure 1 and Table 2 in the Appendix try to provide an original perspective about the interrelations of the three components which create new knowledge flows that, if shared, will ensure the best KM strategy, enabling therefore the organization to accomplish its mission.

As Figure 1 shows, in respect of the staff a higher level of human capital is often associated with greater productivity and higher incomes or compensation for employees (Wilson & Larson, 2002). Instead, as regards the external stakeholder, the human capital acts as a multiplying element that creates value for the organization by connecting all IC components with other external stakeholders (Ordóñez de Pablos, 2004). Finally, the non-human storehouse is an element that adds value to the NPO and constitutes the support structure for HC and RC.

CONCLUSIONS

The framework developed in this paper allows us to demonstrate the importance of the components of intellectual capital in the tertiary sector and, in particular, how the three components (human, social and relational capital) represent strategic assets. Furthermore, it is clear that each of these assets can also provide a potential way to achieve competitive advantages in terms of fundraising and expansion for organizations belonging to the third sector.

In conclusion, it should be noticed that a proper functioning of the framework requires a deep cultural change in each component of the structure; this is the only way to acquire awareness of the importance of sharing knowledge, and create new ideas which, in turn, will generate value. Obviously, this is only possible if there is a Knowledge Management system that treats each individual is as a knowledge worker.

Further developments of this research will address the practical application of what has been covered in this work and, in particular, provide empirical verification of value creation.

REFERENCES


ad governmental organizations. Journal non profit and voluntary sector quarterly, 29(1), 183-204.


Even if the work has been done together, paragraphs 1, 3, 5, 6 can be ascribed directly to Maurizio Rija; paragraphs 2, 4, 7, 8, 9 can be ascribed directly to Giovanni Bronzetti.
### Table 1: Percentage Distribution of Italian NPOs by field of activity

[Source: Our elaboration on 2001 ISTAT census data]

<table>
<thead>
<tr>
<th>Field of Activity</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Culture, sport and spare time</td>
<td>62.4</td>
</tr>
<tr>
<td>Education and Research</td>
<td>5.3</td>
</tr>
<tr>
<td>Health</td>
<td>4.4</td>
</tr>
<tr>
<td>Welfare</td>
<td>8.7</td>
</tr>
<tr>
<td>Environment</td>
<td>1.5</td>
</tr>
<tr>
<td>Economic development and social cohesion</td>
<td>2.0</td>
</tr>
<tr>
<td>Rights protection and political activity</td>
<td>3.1</td>
</tr>
<tr>
<td>Philanthropy and volunteering</td>
<td>0.6</td>
</tr>
<tr>
<td>International Cooperation and solidarity</td>
<td>0.6</td>
</tr>
<tr>
<td>Religion</td>
<td>2.7</td>
</tr>
<tr>
<td>Union relationships</td>
<td>7.1</td>
</tr>
<tr>
<td>Else</td>
<td>1.6</td>
</tr>
<tr>
<td><strong>TOT</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

### Figure 1: New Knowledge flow

[Source: Our elaboration]

<table>
<thead>
<tr>
<th>Abbreviation</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>MS</td>
<td>Staff Member</td>
</tr>
<tr>
<td>EX. SK.</td>
<td>External Stakeholders</td>
</tr>
<tr>
<td>NHS</td>
<td>Non–Human Storehouse</td>
</tr>
<tr>
<td>NKF</td>
<td>New Knowledge Flow</td>
</tr>
<tr>
<td>eka</td>
<td>External Knowledge Acquisition</td>
</tr>
<tr>
<td>lik</td>
<td>Loss of Internal Knowledge</td>
</tr>
<tr>
<td>Non-profit Staff Member</td>
<td>External stakeholder</td>
</tr>
<tr>
<td>-------------------------</td>
<td>----------------------</td>
</tr>
<tr>
<td>New staff and volunteers providing:</td>
<td></td>
</tr>
<tr>
<td>Attitudes</td>
<td>Experience</td>
</tr>
<tr>
<td>Skills</td>
<td>Capacity</td>
</tr>
<tr>
<td>Knowledge</td>
<td></td>
</tr>
<tr>
<td>Ability</td>
<td></td>
</tr>
<tr>
<td>Talent</td>
<td></td>
</tr>
</tbody>
</table>

Table n.2 Components of the Framework
[Source: Our elaboration]