FLYPAPER NONPROFITS: CROWDING IN AND CROWDING OUT EFFECTS OF GRANTS ON NONPROFIT FINANCE

Orkhan ISMAYILOV
Department of Public Administration, University of North Texas, (940) 565- 2165
Orkhan.Ismayilov@unt.edu

Abstract

The flypaper effect is a concept most commonly used by economists to study effect of funding by the federal government on state and local government finance. The argument is that funds allocated by a larger institution to smaller institutions changes policies and revenue base of fund receiving institutions. Similar concept is used to study the effect of government grants on nonprofit finance. The argument is that grant money pushes aside private donations that nonprofit organizations receive. However, the literature on the flypaper effect on grant money varies based on disciplines. The literature on the flypaper effect comes from three main disciplines, such as Economics, Business, and Public Administration. Additionally, the literature also highlights that grant money creates crowding in and out effects. The purpose of this paper is analyze and highlight the literature from three main disciplines, and discuss advantages and disadvantages of crowding in and out effects of grant funding. Findings indicate that grants have an effect on organizational revenue, policies, mission, public support, and service effectiveness.

Keywords:
JEL classification:

Introduction

The flypaper effect is a concept derived from the flypaper theory that argues that funds allocated from the federal government to state governments increases expenditure in state governments (Turnbull, 1998). According to the flypaper theory, the tax burden of the tax sticks where it lands, as if a fly would stick to a flypaper (Barnett, 1985). That is to say, the flypaper theory is a concept in the field of economics, which argues that the burden of taxation sticks directly to those who are taxed, instead of spreading through the economy (Barnett, 1985; Wyckoff, 1988). However, the flypaper effect is not only applied to local governments, but to nonprofits as well (Payne, 2011). The flypaper effect in nonprofits has been studied mostly by scholars in the economics literature, but the concept is also applied to the public administration and management literature. One of the important aspects of the flypaper effect in nonprofit finance is its relation to federal grants.

Other concepts that are usually associated with the flypaper effect are crowding *out* and crowding *in* effects. It is argued that when nonprofit organizations receive grants, the grants crowd out private donations, which makes nonprofit organizations dependent on the government (Friedman, 1979). There are advantages and disadvantages with the crowding out effects, but the most important factor is decrease of funding from other financial resources and decrease of support from the public (Brooks, 2003). The crowding in effect, on the other hand, suggests that increase of grant funds increases private donations and public interest (Payne, 1998). However, whether it is crowding out or crowding in effect, according to Heutel (2009) nonprofit organizations act strategically with grant funds to limit the number of stakeholders and customers.

Moreover, if grant money crowds in private donations then the effect has a positive consequence for nonprofit organizations. In order to understand the positive and negative effects, it is essential to explain the difference. The economics literature argues that crowding out effect is a situation where government increases spending for certain programs in the private sector or increases interest rate, which reduces private sector spending and ability to compete with high interest rates (Payne, 1998). For instance, if the federal government increases spending for Medicaid then private insurance companies will face decrease in the

number of customers. To summarize, crowding out takes place when government enters the market, which essentially increases prices and rates (Rozella and Zanola, 2003). Crowding in effect, on the other hand, is a situation where the government reduces spending for certain programs and services, which leads to an increase of private investments (Thornton, 2012).

While the literature discusses negative and positive flypaper effect of crowding in and out situations in nonprofits, this paper finds that there are mainly two conflicting theories used to explain the flypaper effect. Crowding out has a negative effect on nonprofit organization revenue and private donations. A study conducted by Payne (2011) finds that for every $1000 in grant funds received from government, donations from private donors decreased by $772. In addition, the study highlights that fundraising spending of nonprofit organizations decreases by $137. On average, for every thousand dollars received from the government, there is $410 net gain. Theoretically, crowding out creates a situation whereby nonprofits do not rely on private donations. On the other hand, scholars argue that flypaper effect creates a window of opportunity whereby nonprofits are no longer dependent on private donations and do not have to survive solely based on donations (Simmons and Rosemarie, 2004). Theoretically, crowding out effect creates a positive environment for nonprofit organizations to concentrate more on delivering services instead of fundraising efforts (Horne, 2005).

This paper provides an understanding of two seemingly separate concepts; [1] the flypaper effect, and [2] the crowding out and in effect of grant money. The objectives are to determine factors explaining the flypaper effect and how this concept is related to the crowding out and the crowding in effect in the nonprofit sector. This paper is guided by four questions: (1) What is meant by the flypaper effect and the evidence that suggests the effects are present in the public sector? (2) What is meant by crowding out and crowding in effects and how they are related to the flypaper effect? (3) What are the different approaches in explaining the crowding out and crowding in effects? (4) What are the advantages and disadvantages of crowding out and crowding in effects?

What is meant by the flypaper effect and the evidence that suggests the effects are present in the public sector?

Economists argue that when local governments receive grants from the federal government, grant money increases local government spending. Gramlich and Rubinfield (1982) introduced the concept of the flypaper effect and provided empirical results that support the concept. Researchers in different fields have looked at the role of public officials and management. It is argued that politicians are "single minded seekers of re-election" (Mayhew, 1974), and therefore public officials do not disclose the information and ask voters to approve greater funding (Thornton, 2012). The flypaper effect occurs when residents are not aware of true budget constraints. With regards to politics, the flypaper effect is treated as an independent variable, whereby political institutions and politicians use grants for political purposes (Inman, 2008). The approach adopted by political institutions is solely based on self-interest.

Organizational behavioral approach suggests that the behavior of organizations depends on the type of grants (Hines and Thaler, 1995). Generally, behavior of an organization differs based on the allocation of resources to services. Meaning that organization's behavior changes when certain programs and services need funding. Organizations are able to reduce fees and dues if governmental funding is available for services, however spending does not decrease over time (Dahlby, 2010). Additionally, organizations become interested in spending more resources and getting in debt to make sure the flow of grant money from the government does not decrease overtime. Levaggi and Zanola (2003) finds that grant money received by healthcare organizations in fact pressures organizations to increase spending of own resources. On the contrary, Lalvani (2002) suggests that during recession period, organizations restructure their revenue base by adopting fundraiser and donation friendly image. The literature highlights that the behavior of organizations changes and adapts in order to raise revenue (Bailey and Connolly, 1998).

While research on the flypaper effect of grants on nonprofit expenditure has not been studied thoroughly, the existing literature suggests that the effect varies based on the grant types (Brooks, 2003). Thornton (2012) examines grants given by the Federal Assistance Award Data System (FAADS) by analyzing the structural characteristics of grants. The

empirical results show that conditional grants stimulate fund raising activities in nonprofits. Similarly, researchers have looked at the effect of grants on nonprofit expenditure and find that nonprofits tend to decrease money saving efforts when they have source of funding such as support from the government (Thronton, 2012). It is also noted that if nonprofits choose to not spend money, then government perceives it as lack of need for future funding (Andreoni *et al.,* 2011). Hence, similar to public organizations, nonprofit organizations spend money in order to guarantee support from the government.

Moreover, the literature on the flypaper effect argues that there is an advantage of the flypaper effect in public and nonprofit organizations could also be perceived as a disadvantage. Meaning, depending on the type of an organization, the flypaper effect may provide a window of opportunity for stable and continuous revenue for an organization in form of grants. On the other hand, nonprofit organization face decline in the number of donors and donations overtime. Additionally, another negative effect is decline in fundraising efforts of nonprofits. For instance, a report conducted by Andreoni and Payne (2011) argues that for every $1000 given to a nonprofit, the amount of private donations falls by $757. Theoretically, the flypaper effect has a positive but a minor marginal effect of 24 percent of grant money on nonprofit finance, compared to private donations. However, the Andreoni and Payne (2011) also find that nonprofits save $385 on fundraising expenses for every $1000 received in grants. This effect is also known as crowding out effect, whereby private donations are pushed aside by government grants.

What is meant by crowding out and crowding in effects and how they are related to the flypaper effect?

The crowding out effect is a concept that is derived from the flypaper effect that explains how private donations will be crowded out. In other words, pushed aside by governmental grants (Bekkers and DeWit, 2014). While there are many theoretical arguments for positive and negative consequences of the crowding effect in nonprofit organizations, only few have provided empirical evidence in the public administration literature. The economics literature, on the other hand, provides positive and negative arguments and evidence for crowding out effects in nonprofit organizations (Wu, 2013). The important factors a researcher must consider in empirical research of the crowding out effects are the type of (1) methodology used, (2) sample selection, (3) types of nonprofits, and (4) historical period. The important factors a researcher needs to take into account with regard to donors are motivation for donation, education and income level, and social value of a donor (Simmons and Emanuele, 2004). In fact, Bekkers and DeWit (2014) find that no matter how effective governmental grants are for nonprofit organizations, once the amount of a grant decreases, then support from private donations increases. It is argued that nonprofit funding is cyclical. When grant money decreases, private donations increase. However, the cycle is never permanent.

Scholars argue that the crowding out effect differs based on the type of an organization (Andreoni and Payne, 2011). Theoretically, the crowding out effect in nonprofit organizations has two outcomes. The first outcome is when nonprofits choose governmental grants over private donations, whereby grants crowd out private donors. The second outcome is when the nonprofit chooses to reduce fund raising efforts, whereby grants affect decision making and crowds out fundraising (Eckel *et al.,* 2004). An analysis of over 8000 nonprofit organizations conducted by Andreoni and Payne (2011) highlights that crowding out of donations is around 30 percent, while crowding out of fundraising is 70 to 100 percent. It is argued that governments dictate rules to nonprofit organization and are able to utilize organizations for personal gains through grants. Additionally, Irvin and Carr (2005) suggest that private donations have always been a minor but significant source of income for organizations, yet when other financial sources are available then organizations in fact reduce fundraising efforts.

While the number of nonprofit organizations has grown in the last thirty years, the controversy and the debate over the crowding out effect has been ongoing since 1970s (Horne *et al.,* 2005). Although there are no theoretical findings in the study conducted by Carlson and Spencer (1975), the findings highlight importance of understanding and researching nominal and real crowding out effects. Nominal crowding out does not account for effects such as inflation, while the real crowding out factors in effects that are necessary for to determine true

impact of grants on private donations. In addition, scholars note that the existing literature does not provide in depth analysis of indirect and direct crowd outs (Hughes *et al.,* 2014). The direct crowd out is measured by short term money loss or gains from private donations after receiving grant money. While the indirect crowd out is measured by long term changes nonprofit organizations make after receiving a grant (Eckel *et al.,* 2014).

Whether crowding out has positive or negative effects, knowing how to combat crowding is essential. Public administration scholars find that to combat indirect crowd out, a nonprofit organization must emphasize on the grant design, while combatting direct crowd out requires collective action theories (Hughes *et al.,* 2014). One common way to combat the crowding out effect is by requiring nonprofit organizations to match governmental grants, whereby by gaining money from private donations, nonprofits would be able to reduce negative effects of crowding out (Andreoni and Payne, 2011).

Matching governmental grants, theoretically, has positive and negative effects on nonprofit finance (Brooks, 2000). For example, if nonprofit organizations are required to match grants, then nonprofits are forced to raise funds through private donations. The argument is that nonprofit organizations are able to withhold social value and purpose, which is to serve public and promote social values (Brooks, 2003; Peredo *et al.,* 2006). On the contrary, when nonprofits are solely reliant on grant funds, then organizations are less likely to retain the social values and more likely to become contracted out by serving purpose other than the public (Heutel, 2009). Scholars also argue that decrease in reliance on private donations helps organizations to rethink values and encourage social entrepreneurship behavior (Jones *et al.,* 1998; Roberts and Woods, 2005). Depending on the type of an organization and the mission of an organization, the findings indicate that crowd outs in fact have a positive impact of nonprofit finance (Andreoni *et al.,* 2011).

While the crowding out has positive and negative effects, although seldom, but crowding in effects too have positive effect on nonprofit finance (Bolton and Katok, 2008) (*see Table 1)*. It is argued that when government increases grant funding to nonprofits, then most organizations increase private donations as well (Heutel 2012; Schiff 1986). However, this pattern does not apply to all nonprofits. According to Heutel (2012), new nonprofit organizations benefit the most from grants, whereby a governmental grant attracts attention of private donors who then donate funds to the nonprofit. Hence, the new and developing nonprofit organizations take an advantage of the crowding in effect by raising funds through grants and donations (Hughes *et al.,* 2014). Scholars find that type of a grant and mission of a nonprofit organization is what decides occurrence of the crowding in effects (Schiff, 1986). In addition, the crowding in effect occurs when grants motivate the public to be involved in charitable organizations and contribute to organization's fund (Kakinak and Kotani, 2011).

What are the different approaches in explaining the crowding out and crowding in effects?

The crowding out and in effects have been examined by fields of sociology, economics, business, public administration, and etc. Although, the main focus has been the approaches used to examine the crowding out and crowding in effects on financial, policy, and strategy aspects of an organization. Three fields that are most present in the literature are economics, business, and public administration. The economics literature uses monetary policies and funds approach to examine whether the crowding has negative or positive effects. The business literature uses strategies used by organizations approach to study the crowding effects and how nonprofits financially react to grants. The public administration literature uses policies and value approach to study the crowding effects on nonprofit finance.

Scholars in economics literature are interested in growth of nonprofits after receiving grant money. Main findings show that grants in fact have an effect on organization finance (Knight, 2000; Steinberg, 1987; Connolly, 1997). In order for a nonprofit to accumulate funds from government and private donations, the nonprofit must provide quality service (Heutel, 2009). Depending on services provided by nonprofits, economics literature suggests that grants rarely crowd out private donations. According to Livingston (2010), for each additional dollar increase in governmental spending on charitable organizations, private donations decreased by 16 cents. However, the funds raised through donations fell only 5 cents for each additional dollar spent in government grants.

Yet, maximizing all revenue, whether grants or donations, nonprofit organizations are able to raise more funds (Brooks, 2000). In fact, Andreoni and Payne (2010) highlight that the crowding out effect, although present in nonprofit finance, occurs aggressively when nonprofits do not maximize all available resources. Similarly, Sokolowski (2012) highlights that the crowding in effect is significant in charitable organizations that become active in order to attract funds from government and private donations, however there is no net effect on nonprofit finance. On the contrary to Sokolowski's (2012) findings, Payne (1996) finds that human service and shelter nonprofits, as a result of the crowding out effect of government grants, on average, experience 50 cent decline for every dollar increase in grants. Hence, there are mixed empirical findings that contradict each other. Nonetheless, it is essential that the reader understands net effects of governmental grants on nonprofit finance (*see Table 1*).

While the economics literature examines the net effect of crowding on nonprofit finance, the business literature examines policies and strategies used by nonprofit organizations to raise financial resources. One theoretical argument highlights that charitable organizations, overtime, purposefully adopt policies that attract private donations (Sokolowski, 2012; Heutel, 2012). For example, if government increases spending on healthcare, then charitable organizations are likely to change strategies and policies to become more healthcare friendly in order to receive grants. However, charitable organizations also adapt to societal changes and change mission to receive public support.

According to Borgonovi (2006) the relationship between level of public support and crowding effect takes U shape, whereby funds generated from private donations increase due to an increase in support for charitable organizations. Change in strategy and mission could potentially sway governmental grants and increase private donations (Schiff, 1985). Heutel (2010) finds that large amount of private donations crowds out governmental grants. According to Dokko (2009), when an organization faces reduction in grant funds, private donations increase by 50 to 60 cents for every 25 cents in spent in fundraising efforts. Thus, while charitable organizations value funding, changing strategies and mission, changes sources of funds and financial gains for nonprofits (*see Table 1*).

On the contrary to the economics and the business literature, the public administration literature uses policies and social value approach in examining the crowding effect of governmental grants. According to Brooks (2000), although small amount of the crowding out effect takes place in charitable nonprofits, the effect differs based on type and purpose of nonprofit organizations. For instance, nonprofits providing or championing for social and health services have higher crowding out effect (Brooks, 2000; Brooks, 2003; Payne, 1998). Moreover, Brooks (2003) concludes that due to the crowding out phase, the number of donors and supporters do not decrease, whereas the amount of private monetary donations in fact decreases significantly. The crowding out effects also affects donated time and volunteerism, whereby individuals decrease number of hours they volunteer due to higher grant funding (Simmons and Emanuele, 2004).

While the information on funds received from government for charitable organizations is open to public, the knowledge of available governmental funding to charitable organizations is limited among private donors (Horne *et al.,* 2005), highlighting that private donors are likely to continue donations due to limited knowledge of availability of grant funds to nonprofits. However, the behavior of a private donor is not based on limited knowledge alone. The crowding out effect also affects the structure on nonprofits, whereby nonprofits incline to hiring staff that writes grants to increase governmental funding (Kearns 2012). Hence, the paper finds that the crowding out effects do not only affect private donations, rather the crowding out affects nonprofit strategies and management (*see Table 1*).

Table 1 Approaches to studying the flypaper effect

Economics Literature	Business Literature	Public Administration and Nonprofit Literature

- The flypaper effect affects nonprofits positively, whereby nonprofits gain funds	- The positive or negative results of the flypaper effect depend on nonprofit policies	- Private donors depend on mission and social value of nonprofit organizations
- There is little empirical evidence that suggests the flypaper effects funds gained through private donations	- Nonprofits strategically adopt strategies to increase grant funding	- Although nonprofits disclose information to public, private donors rarely know about external nonprofit findings
- The evidence that suggests decrease of private donations highlights that for every grant dollar, private donations decrease by 25 cents	- The flypaper effect does have significant effect on nonprofit finance, although the evidence cannot be generalized to all charitable organizations	- Nonprofits adopt public friendly policies and mission to increase funding through grants and private donations
- The net effect of the flypaper effect depends on the types of grants		- The flypaper effects has a positive impact on nonprofit finance

What are the advantages and disadvantages of crowding out and crowding in effects?

Although positive and negative effects of crowding vary among nonprofit organizations, the debate over the displacement of philanthropy or encouragement continues among scholars (Brooks, 2000). Theoretical arguments suggest that nonprofits are likely to crowd out private donations, however empirically not many scholars have been able to prove this notion (Schief, 1985). Therefore, the literature on effects of crowding is divided into two sections. The first section argues that grants crowd out private donations, whereby nonprofits whether intentionally or unintentionally diminish fundraising efforts. The second section, on the other hand, argues that grants crowd in private donations, whereby after receiving grants, nonprofit organizations draw more attention from private donors and increase funding through donations (Brooks, 2000). However, Shief (1985) argues that this behavior depends on the type of an organization, while Hughes *et al.* (2014) argue that it solely depends on the private donors.

The advantages of the crowding out effect is creation of stable source of funds, clear mission, less political environment, greater monetary support, less expenditure on staff, and etc. In order to function and provide services, nonprofit organizations must have funds to operate. Yet, not all organizations are able to have stable sources of revenue to operate and continue providing services. For example, an organization that relies on private donations to operate, faces decrease in the amount of donations during economic recessions, which usually forces organizations to decrease number of employees and restructure the budget. Hence, the crowding out effect in fact creates an environment whereby nonprofit organizations are able to continue operations without any disruption due to bad economy or low donations (Silvesind and Selle, 2009). Additionally, by crowding out private donations, nonprofits are able to establish politics free environment, whereby nonprofit management would not be forced to please donors individually to gain support and financial resources (Horne *et al.,* 2005).

In addition, the crowding out effect also allows nonprofits to have clear mission and create reputation for providing particular services. For example, by crowding out private donors, a nonprofit gets rid of majority stakeholders, and is able to build a reputation for providing particular services with approval of the major stakeholder, which is the government. Nonprofits are not assured to gain minimum amount of financial resources every year from private donors. Receiving grants is more assuring and stable for nonprofits (Andreoni and Payne, 2011). Stable yearly financial resources help nonprofit organizations to master and excel at providing services (Andreoni *et al.,* 2011). Moreover, by crowding out private

donations, nonprofits are able to cut administrative and fundraising costs (Payne, 1998). Instead of increasing number of employees to increase funds through fundraising, nonprofits instead hire fewer number of employees for grant writing purposes. Hence, as a result of the crowding out effect, nonprofits are able to decrease costs associated with operating nonprofits. The findings highlights that there is minor decrease in administrative costs (Thornton, 2012).

The disadvantages of the crowding out effects on nonprofits are decrease of public support, decrease in financial resources, increase on governmental influence, and decrease of accountability by stakeholders. Although, the goal of nonprofit organizations is to value social change and provide services where government fails to act (Paredo and McLean, 2006), the crowding out effect creates an environment where public support for nonprofits decreases due to an increase in government grants, which is associated with distrust generated by the public (Payne, 2011). Decrease of public support then results in decrease in private donations (Andreoni and Payne, 2011). Although nonprofit organizations are able to maintain operations even when private donations decrease, the main issue then becomes the number of customers and stakeholders. Where governments are accountable to many stakeholders and serve large pool of customers (Austin *et al.,* 2006), nonprofit organizations are accountable to limited number of customers and stakeholders (Roberts and Woods, 2005). Not only the government becomes the largest stakeholder after proving grants, but it also increases influence over mission and operations of nonprofit organizations (Thonrton, 2014). To summarize, crowding out private donations reshapes purpose and values of having charitable nonprofit organizations (*see Table 2*).

The advantages of the crowding in effect are increase of private donations, increase of public support, increase in the number of stakeholders and customers, and increase of competition among nonprofit organizations. Studies show that governmental grants, in fact, increase private donations, yet the results show that this behavior is attributed to new nonprofits (Heutel, 2012; Hughes *et al.,* 2014). Similarly, the behavior of the public changes towards nonprofit organizations that receive large governmental grants, by increasing support for organizations (Friendman, 1979). An increase of support, whether it is monetary support or simply volunteerism, increases the number of stakeholders in nonprofits, which makes nonprofits more accountable to the public (Horne *et al.,* 2005). Yet, the biggest advantage of the crowding in effect is an increase of competition among nonprofit organizations (Ashley, 2014). Nonprofits that do not rely solely on grants, and by increasing private donations and increasing support of donors helps maintain providing services. Moreover, this creates a competition among nonprofit organizations, whereby organizations not only increase fundraising efforts through private donations, but through attracting supporters from competing nonprofits as well (Sokolowski, 2012; Horne *et al.,* 2005). To summarize, crowding in effect boosts competition among nonprofit organizations and increases quality of services provided (*see Table 2*).

There are few disadvantages of the crowding in effect of grants for nonprofit organizations, yet the most important factor is an increase in the number of stakeholders. Nonprofits, like politicians, are accountable to customers and stakeholders. Yet, just like politicians, nonprofits would rather have one major stakeholder to report to instead of many. That is, if a nonprofit accepts equal amount of financial resources from grants and private donations, then organizations are to report to many stakeholders (Siversind and Selle, 2009). Although significant, according to Heutel (2009) the impact of crowding in funds from other sources does little impact on nonprofit management and accountability. However, the important factor is that nonprofits in fact act strategically and choose whether to crowd in or crowd out (Bailey and Connolly, 1997).

Table 2 Advantages and Disadvantages of Crowding in and out Effects

	Advantages	**Disadvantages**
Crowding out	- Larger monetary gains - Decrease in fundraising efforts	- Decline in number of staff members - Decrease of social value and purpose

	- Decrease of customer and stakeholder pressure - Decrease in administrative costs	of an organization - Decrease of donor accountability - Decline of public support - Increase in governmental and influence
Crowding in	- Increase of monetary funds through donations and grants - Increase of donor and public accountability - Increase in public support - Decrease of governmental influence - Increase of service effectiveness	- Nonprofit competition for funding - Increase of the number of stakeholders

Conclusion

The purpose this paper is to critically evaluate and examine the literature on the flypaper effect in nonprofit organizations. In order to clearly understand the flypaper effect, this paper asks series of questions. The first question asks whether the flypaper effect is present in nonprofit finance and to what extend it effects private donations. The findings highlight that the flypaper effect becomes present in nonprofits when organizations receive grant money. The literature shows that the flypaper effect, mostly, has a negative effect on private donations and on other sources of revenue for nonprofits. Yet, conflicting literature argues that the flypaper effect, although significant, does no harm private donations. Additionally, scholars provide theoretical argument of positive effect of the flypaper effect, whereby grants help increase donations and public support. Nonetheless, this paper concludes that strategies and policies adopted by nonprofit organizations, in fact, play major role on whether the flypaper effect produces positive or negative outcome.

The paper also discusses the approaches adopted by various fields in studying the flypaper effect. While examining the literature, the paper finds that three fields have analyzed and examined the flypaper effect in nonprofits. To clarify and distinguish the differences, this paper examines all three approaches individually. The findings highlight that scholars in the field of economics are interested in finding the net effect of grants on nonprofit finance. Yet, the findings suggest that depending on the type and purpose of a nonprofit, organizations react differently to the flypaper effect. To support this claim, the scholars in the business field investigate whether nonprofits adopt certain strategies and policies to promote the flypaper effect. The findings suggest that nonprofits adapt strategically based on grant requirements to attract funds. However, this behavior does not apply to all organizations. The nonprofit and public administration literature also supports findings of business scholars, while adding that private donors usually are unaware of the amount of funding nonprofits get through grants. Yet private donors continue donating time and resources if the mission and social values of nonprofit organizations do not change.

Moreover, the paper in depth discusses what the crowding in and out effects are, and whether the effects have positive or negative effect on nonprofit organizations. The summary of findings highlights that the crowding out effects in fact do not have major impact on nonprofit finance. The essential impact of the crowding out effect is change nonprofit behavior to retain grand money. On the other hand, the findings of the crowding in effect suggest that private donations do not diminish even when grant funds increase. Moreover, grant funding help nonprofit organizations to attract more private donors and other financial resources.

Therefore, the paper concludes that the flypaper effect varies based on the type of a nonprofit organization, educational and income level of donors, and most importantly the

amount of grant funding. The paper also notices the gap in the literature. The area that has not been examined is the relationship between nonprofit organizations and politics. Hence, this paper recommends to examine the flypaper effect of grants based on the providing agency, and more specifically to research question “Does the flypaper effect depend on the agency that provides grants?”.

References

[1] Andreoni, James, and A. Abigail Payne. "Is crowding out due entirely to fundraising? Evidence from a panel of charities." Journal of Public Economics95, no. 5 (2011): 334-343.

[2] Andreoni, James, and A. Abigail Payne. Crowding-out charitable contributions in Canada: new knowledge from the North. No. w17635. National Bureau of Economic Research, 2011.

[3] Andreoni, James, Abigail Payne, Justin D. Smith, and David Karp. Diversity and Donations: The Effect of Religious and Ethnic Diversity on Charitable Giving. No. w17618. National Bureau of Economic Research, 2011.

[4] Ashley, Shena. "The Impact of Government Funding on Competition in the Nonprofit Sector: An Integrative Model and Review of Empirical Research." InNonprofit Policy Forum, vol. 5, no. 2, pp. 289-305. 2014.

[5] Austin, James, Howard Stevenson, and Jane Wei‐Skillern. "Social and commercial entrepreneurship: same, different, or both?." Entrepreneurship theory and practice 30, no. 1 (2006): 1-22.

[6] Barnett, R. R. "On the flypaper theory of local government response to grants-in-aid." Environment and Planning C: Government and Policy 3, no. 3 (1985): 341-348.

[7] Bailey, Stephen J., and Stephen Connolly. "The flypaper effect: Identifying areas for further research." Public Choice 95, no. 3-4 (1998): 335-361.

[8] Bekkers, Rene, and Arjen DeWit. "Look Who’s Crowding-Out! Correlates Of Willingness To Substitute Declining Government Contributions To Charitable Organizations." 2014

[9] Bolton, Gary E., and Elena Katok. "An experimental test of the crowding out hypothesis: The nature of beneficent behavior." Journal of Economic Behavior & Organization 37, no. 3 (1998): 315-331.

[10] Borgonovi, Francesca. "Do public grants to American theatres crowd-out private donations?." Public Choice 126, no. 3-4 (2006): 429-451.

[11] Brooks, Arthur C. "Public subsidies and charitable giving: crowding out, crowding in, or both?." Journal of Policy Analysis and Management 19, no. 3 (2000): 451-464.

[12] Brooks, Arthur C. "Is There a Dark Side to Government Supportfor Nonprofits?." Public Administration Review 60, no. 3 (2000): 211-218.

[13] Brooks, Arthur C. "Do government subsidies to nonprofits crowd out donations or donors?." Public Finance Review 31, no. 2 (2003): 166-179.

[14] Carlson, Keith M., and Roger W. Spencer. "Crowding out and its critics."Federal Reserve Bank of St. Louis Review December 1975 (1975).

[15] Connolly, Laura S. "Does external funding of academic research crowd out institutional support?." Journal of public Economics 64, no. 3 (1997): 389-406.

[16] Dahlby, Bev. "The marginal cost of public funds and the flypaper effect."International Tax and Public Finance 18, no. 3 (2011): 304-321.

[17] Dokko, Jane. "Does the NEA crowd out private charitable contributions to the arts?." (2008).

[18] Eckel, Catherine C., Philip J. Grossman, and Rachel M. Johnston. "An experimental test of the crowding out hypothesis." Journal of Public Economics89, no. 8 (2005): 1543-1560.

[19] Friedman, Benjamin M. "Crowding out or crowding in? The economic consequences of financing government deficits." (1979).

[20] Heutel, Garth. "Crowding out and crowding in of private donations and government grants." Public Finance Review 42, no. 2 (2014): 143-175.

[21] Hines, James R., and Richard H. Thaler. "Anomalies: The flypaper effect." The Journal of Economic Perspectives (1995): 217-226.

[22] Horne, Christopher S., Janet L. Johnson, and David M. Van Slyke. "Do Charitable Donors Know Enough—and Care Enough—About Government Subsidies to Affect Private Giving to Nonprofit Organizations?." Nonprofit and Voluntary Sector Quarterly 34, no. 1 (2005): 136-149.

[23] Hughes, Patricia, William Luksetich, and Patrick Rooney. "Crowding‐Out and Fundraising Efforts." Nonprofit Management and Leadership (2014).

[24] Inman, Robert P. The flypaper effect. No. w14579. National Bureau of Economic Research, 2008.

[25] Irvin, Renée A., and Patrick Carr. "The role of philanthropy in local government finance." Public Budgeting & Finance 25, no. 3 (2005): 33-47.

[26] Jones, Philip R., John G. Cullis, and Alan Lewis. "Public Versus Private Provision of Altruism: Can Fiscal Policy Make Individuals 'Better'People?."Kyklos 51, no. 1 (1998): 3-24.

[27] Kakinaka, Makoto, and Koji Kotani. "An interplay between intrinsic and extrinsic motivations on voluntary contributions to a public good in a large economy." Public Choice 147, no. 1-2 (2011): 29-41.

[28] Kearns, Kevin P., David Bell, Bobbi Deem, and Lydia McShane. "How Nonprofit Leaders Evaluate Funding Sources: An Exploratory Study of Nonprofit Leaders." Nonprofit and Voluntary Sector Quarterly (2012): 0899764012458038.

[29] Knight, Brian G. "The flypaper effect unstuck: evidence on endogenous grants from the Federal Highway Aid Program." Finance and Economics Discussion Series 49 (2000).

[30] Lalvani, Mala. "The flypaper effect: evidence from India." Public Budgeting & Finance 22, no. 3 (2002): 67-88.

[31] Livingston, Brendan. "Nontraditional Crowding Out: Spending and Endowment Decisions By Nonprofit Managers." (2010).

[32] Levaggi, Rosella, and Roberto Zanola. "Flypaper effect and sluggishness: evidence from regional health expenditure in Italy." International Tax and Public Finance 10, no. 5 (2003): 535-547.

[33] Mayhew, David R. Congress: The electoral connection. Yale University Press, 1974.

[34] Peredo, Ana Maria, and Murdith McLean. "Social entrepreneurship: A critical review of the concept." Journal of world business 41, no. 1 (2006): 56-65.

[35] Payne, A. Abigail. "Does the government crowd-out private donations? New evidence from a sample of non-profit firms." Journal of Public Economics 69, no. 3 (1998): 323-345.

[36] Roberts, Dave, and Christine Woods. "Changing the world on a shoestring: The concept of social entrepreneurship." University of Auckland Business Review7, no. 1 (2005): 45-51.

[37] Schiff, Jerald. "Does government spending crowd out charitable contributions?." National Tax Journal (1985): 535-546.

[38] Sivesind, Karl Henrik, and Per Selle. "Does public spending “crowd out” nonprofit welfare?." Comparative social research 26 (2009): 105-134.

[39] Simmons, Walter O., and Rosemarie Emanuele. "Does government spending crowd out donations of time and money?." Public Finance Review 32, no. 5 (2004): 498-511.

[40] Sokolowski, S. Wojciech. "Effects of government support of nonprofit institutions on aggregate private philanthropy: evidence from 40 countries."VOLUNTAS: International Journal of Voluntary and Nonprofit Organizations 24, no. 2 (2013): 359-381.

[41] Steinberg, Richard. "Voluntary donations and public expenditures in a federalist system." The American Economic Review (1987): 24-36.

[42] Thornton, Jeremy P. "Flypaper Nonprofits: The Impact of Federal Grant Structure on Nonprofit Expenditure Decisions." Public Finance Review (2012): 1091142112446845.

[43] Turnbull, Geoffrey K. "The overspending and flypaper effects of fiscal illusion: theory and empirical evidence." Journal of Urban Economics 44, no. 1 (1998): 1-26.

[44] Wu, Shih-Ying. "Margin of Victory and Crowding Out of Intergovernmental Grants–Evidence from Taiwan’s Lottery Grants." 2013

[45] Wyckoff, Paul Gary. "A bureaucratic theory of flypaper effects." Journal of Urban Economics 23, no. 1 (1988): 115-129.