

# **Accountability in Social Enterprises: An Analytical Framework**

## **I. Introduction**

Social enterprises, considered a form of organization that differs from traditional for-profit and non-for-profit organizations, has been broadly discussed and systematically encouraged among academic communities and practitioners since the 1990s (Perrini, 2006). Reflecting this trend, universities have created programs, offered courses, and built centers to systematically encourage social entrepreneurship (i.e. the Harvard Business School of Harvard University). Foundations are established to promote and incubate social entrepreneurship (i.e. The Skoll Foundations). Knowledge sharing networks (i.e. EMES European Research Network) have been also set up to facilitate dialogue with social enterprises. The emergence of social enterprises is a phenomenon that has not only occurred in the United States, but also many other OECD countries (Noya, 1999).

It is believed that the emergence of social enterprises in the United States is rooted in six historical forces (Boschee, 2006: 357): (1) depleted reserves caused by the recession in the late 1970s; (2) diminished support from the public sector; (3) reduced giving by individuals and corporations; (4) increased competition for grants and contributions; (5) increased people in need; and (6) a dangerously frayed reputation of the nonprofit sector. As a result, the emergence of social enterprises has reflected the increased desire for social change from the public, as well the need for non-profits to diversify financially.

Social enterprises are hybrid organizations that have mixed characteristics of philanthropic and commercial organizations (Dees, 1998). They are established to

respond to unmet social needs through business-like and innovative means. According to Alter (2006), social enterprises are driven by two forces: “first, the nature of the desired social change often benefits from an innovative, entrepreneurial, or enterprise-based solution. Second, the sustainability of the organization and its services requires diversification of its funding stream, often including the creation of earned income opportunities (p. 205).”

The hybrid nature of social enterprises makes their accountability different from that of traditional nonprofit organizations. As Imperatori & Ruta (2006:107) indicated, social enterprises obtain human and financial resources from both non-for-profit and market sectors which operate according to different rules, and are composed of multiple actors who have different knowledge and preferences about the resources allocation. Accountability is an information generation process in which actors “report to authorities and are held responsible for their actions (Edwards and Hulme, 1996: 967).” Connecting the characteristics of social enterprises and the nature of accountability, social enterprises are held responsible for both social and economic performance and are expected to report to multiple authorities who pursue different interests.

However, there are not many social enterprise researches address accountability issues. Although some studies (e.g., Romzek & Dubnick, 1987; Kearns, 1994) have proposed frameworks that can analyze accountability in nonprofit and public organizations, they do not emphasize on the interaction between the features of double bottom line and multiple stakeholders in social enterprises. This study proposes a framework to illustrate how different values and multiple stakeholders frame accountability issues in social enterprises. The framework incorporates the features, conflicted values and diverse stakeholders’ interests, into a matrix that can be used to analyze accountability in social enterprise. It is a two by two matrix that contains two dimensions: (1) sources of accountability (internal and external stakeholders) and (2) expected values (social and economic achievement).

This paper is organized into five distinct sections. The first section is the introduction. The second section defines the term social enterprise. The third section discusses the rationale for focusing on accountability in social enterprises. The fourth section describes the proposed analytical framework for the accountability in social enterprise. The fifth and final section discusses some of the issues that make it difficult to hold social enterprises accountable and the further researches which are needed.

## **II. Definitions of Social Enterprises**

Most definitions of social enterprise contain the notion of social purposes and business likeness. For instance, the UK-based Social Enterprise Coalition (2007) defines social enterprise as “dynamic businesses with a social purpose.” Virtue Venture (2007) provides a more specific definition: “a social enterprise is any business venture created for a social purpose – mitigating or reducing a social problem or a market failure – and to generate social value while operating with the financial discipline, innovation and determination of a private sector business.” These definitions suggest that social and financial achievements are equally concerned in social enterprises in which social values are generated through entrepreneurial, finance-sustainable, and innovative means.

There are two issues in identifying the notion of social enterprise. First is about the different perspectives on the institutional form of social enterprise. Some scholars see social enterprises as hybrid organizations that could either be nonprofit organizations engages in commercial activities, or for-profit firms pursue social responsibility. Recognizing this bend of commercial and non-commercial activity, Dees (1998) suggests that social enterprises are hybrid organizations that have mixed characteristics of philanthropic and commercial organization in several aspects, such as motives, methods, goals, and key stakeholders (p. 56-57). Building upon this perspective, Dees proposed the social enterprise spectrum (Figure 1), where pure forms of nonprofit and for-profit

organizations reside at opposite ends, and social enterprise, having characteristics of both, fall somewhere in between.

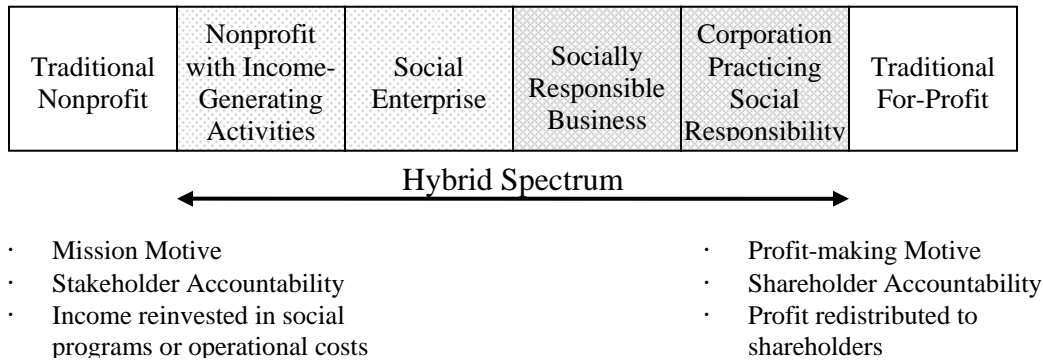
Figure 1 Social Enterprise Spectrum

		Purely philanthropic	←————→	Purely Commercial
	Motives Methods Goals	-Appeal to goodwill -Mission driven -Social value	-Mixed motives -Mission and market driven -Social and Economic value	-Appeal to self-interest -Market driven -Economic value
Key Stakeholders	Beneficiaries	Pay nothing	Subsidized rates, or mix of full payers and those who pay nothing	Market-rate prices
	Capital	Donations and grants	Below-market capital, or mix of donations and market-rate capital	Market-rate capital
	Workforces	Volunteers	Below-market wages, or mix of volunteers and fully paid staff	Market-rate compensation
	Suppliers	Make in-kind donations	Special discounts, or mix of in-kind and full-price donations	Market-rate prices

Source: Dees, 1998: 60.

While Dees identifies social enterprises as hybrid organizations having characteristics of both nonprofit and for-profit form organizations, other scholars limit their discussions of social enterprise to the field of nonprofit management (Alter, 2004, 2006; Dart, 2004; Young & Salamon, 2002). Alter (2004) develops the hybrid spectrum to identify social enterprises. On the spectrum, hybrid organizations are organized by degree of activity as it relates to: motive, accountability, and use of income (p. 7). This enables the spectrum to be organized into four categories of hybrid organizations: (1) nonprofits with income-generating activities, (2) social enterprises, (3) socially responsible businesses, and (4) corporations practicing social responsibility (see Figure 2). Alter's hybrid spectrum clearly identifies social enterprises as a form of non-for-profit organizations that differ from the nonprofits that engage in income generating activities.

Figure 2 Hybrid Spectrum



Source: Alter, 2006: 7.

The second issue in identifying the notion of social enterprise is about: what has made non-for-profit-formed social enterprises distinctive from the nonprofits that engage in income generating activities. Scholars have different viewpoints about the essential elements that make social enterprises distinctive. From Alter’s (2006) perspective, business activities in social enterprise are either motivated by mission or driven by profit. Hence, in terms of mission orientation, social enterprises may engage in business activities which are in the form of mission centric, mission related or unrelated to mission. However, some scholars emphasize that business activities in social enterprises should be mission related. Boschee and McClurg (2003) claim that social enterprises are different from traditional nonprofit organizations because social enterprises’ earned income strategies are directly tied to their social mission. The business activities like employ the disadvantaged or sell mission-driven services and products can have direct impact on the social programs.

This study acknowledges that social enterprises could exist in either non-for-profit or for-profit form and there are various viewpoints on the distinction between social enterprises and traditional nonprofit organizations. In terms of institutional forms,

different institutional forms may lead to different natures and characteristics of accountability system and mechanisms. For analytical purpose, this study chooses to focus on the nonprofit-based social enterprises. Regarding the distinction between “Nonprofit’s earned Income Activity” and “Social Enterprise”, this paper agrees with Boschee & Jim McClurg’s viewpoint that the business oriented strategies which social enterprises adopt are usually directly tied to their social mission. After all, nonprofit organizations earning income is not a new phenomenon (see Bielefeld, 2006), this paper believe that it is the mission-related business strategy makes social enterprises distinctive from nonprofit organizations. In sum, the term, social enterprise, used in this paper is referred to the non-for-profit formed institution that creates social values through adopting entrepreneurial, mission related, and business-like activities.

### **III. Rationale for Focusing on Accountability in Social Enterprise**

There are multiple perspectives on what accountability is in organizations. The narrow perspective suggests that an organization is accountable to the extent that its activities can pass financial scrutiny. A broader perspective suggests that an organization is accountable to the extent that its activities can meet the public’s expectation of social responsibility, which means that the organization is not just spending money properly, but doing so in a way that has a positive social impact.

Edwards and Hulme (1996: 967) describe accountability as “the means by which individuals and organizations report to a recognized authority (or authorities) and are held responsible for their actions”. Fox and Brown (1998: 12) also emphasize accountability as “the process of holding actors responsible for actions.” These definitions indicate that accountability is an information reporting process in which actors answer higher authorities and are held responsible for actions. However, these definitions do not address the sources of accountability and what the actors are held accountable for.

There are literatures that address the limitation. Ebrahim defines accountability as “the means through which individuals and organizations are held externally to account for their actions and as the means by which they take internal responsibility for continuously shaping and scrutinizing organizational mission, goals, and performance (p. 23).” The definition shows that accountability can be externally driven and be internally generated. Furthermore, actors are held accountable for certain expected values such as their mission, goals and desired performance.

Several researchers believe that demands for accountability information come from multiple sources which usually can be categorized as the internal and external sources of accountability (Cutt & Murray, 2000; Ebrahim, 2003; Romzek and Dubnick, 1987). Cutt and Murray (2000) classify sources of accountability into two groups based on the information use: internal information users and external information users. Romzek and Dubnick (1987) propose a framework which indicates that there are four types of accountability in democratic system which may be driven by external forces like political pressure and legal regulations, or be internally initiated in the hierarchy and professional communities.

Jos and Tompkins (1994) further provide seven sources of demands for accountability. These include (1) market exchange: properly functioning markets allow buyers and sellers to exchange goods and services to ensure accountability through an invisible hand (supply and demand); (2) legal accountability: it is required by public managers and fulfilled by following laws and regulations; (3) political accountability: it emphasizes how public organizations achieve their missions to serve the public; (4) managerial authority: leaders and managers in organizations use formal and informal mechanism or techniques to enforce accountability needs; (5) professional control: it is enforced through certifications, norms, ethic codes, and standards maintained by trade associations and occupational communities; (6) informal networks: personal ties, professional affiliations, and network relationships affect employees’ attitude and belief

toward accountability system, and (7) personal values: values are important to have influences on making accountable actions and decisions. We can group the former three items (market exchange, legal accountability, and political accountability) as external sources, and group the latter four items (managerial authority, professional control, informal networks, and personal values) as internal sources.

In sum, the notion of accountability can be considered as an information generation process that has at least two essential elements. One is the entities that have higher authority to hold actors at lower position accountable. This is the element about sources of accountability. Another element is the value that actors are accountable for. This is about what is the desired performance that the entities with higher authority expect actors to achieve.

Examining with the two essential elements, accountability in social enterprises may be different from it in traditional public organizations in terms of the sources of accountability and the values that social enterprises are expected to achieve. In terms of the sources of accountability, social enterprises have mixed stakeholders from traditional nonprofits and commercial organizations; in terms of the expected values, social enterprises are driven by the double bottom line: financial success and social mission achievement. The following paragraphs further discuss the accountability as it applies to social enterprises.

### ***Sources of Accountability: Mixed Stakeholders***

Accountability is a process of fulfilling information demands from higher authorities (Kearns, 1996: 7). Nonprofit organizations have responsibility for reporting accountability information to their stakeholders. Different stakeholders have different interests, demands and expectations on organizational performance. Kanter & Summers (1987) propose that there is the need for a multiple-constituency approach of accountability. To understand the accountability system of social enterprises, we need to

review the diverse stakeholder community and its demand for information and expectation of organizational performance.

Social enterprises have mixed stakeholders from traditional nonprofits and commercial organizations (Dees, 1998). For instance, in traditional nonprofit organizations, beneficiaries may receive services without paying. However, in social enterprises, beneficiaries may be seen as consumers who pay for receiving services. In addition, traditional nonprofits rely on charitable donations, but social enterprises may receive funding from investors who request return of investment.

Mixed stakeholders in social enterprises may incur conflicting accountability relations. As engaging in business-oriented activities, social enterprises may play a role of supplier in the market. Social enterprises build accountability relationships with consumers on the basis of economic exchanges. Consumers aim to maximize utilities and have freedom of making choices from different products. In business world, ventures can always adjust prices and features of products as well as withdraw the goods or services from market in order to maximize their revenue. However, on the other side, social enterprises also have responsibility to their clients who have relied on social enterprises provide services without charge. Social enterprises may commit to provide free services to a group of disabilities who would expect stable and continuous services instead of social enterprises' risky innovation.

### ***Expected Performance: Double Bottom Line***

It is not just the mixture of stakeholders that makes the accountability of social enterprises different from traditional non-profit and commercial organizations. They are also different in terms of their expected performance. Social enterprises are established to create social value and to solve social problems that governments and markets fail to address. Social enterprises do so by operating in the area between traditional non-profits and traditional for-profit organizations. Therefore, unlike these traditional organizations,

social enterprises are driven by the double bottom line: the need for financial success and the need to achieve its social mission. The problem with this is that the goals of creating social and economic values do not always coexist without conflict (Foster and Bradach, 2005). Bielefeld (2006: 17) also indicates that there are tensions and a need of trade-off between nonprofit missions and economic profit in social enterprises.

There is a concern about the engagement in commercial activities that may drive social enterprises drift away from their social mission. Foster & Bradach (2005) discuss mission drift as the phenomenon that nonprofit organizations engage in commercial ventures not directly related to their core missions. Engaging commercial activities may cause social enterprises drift away from the mission statement. When social enterprises engage in commercial activities, its leaders and staff will increase the time they spend on commercial business, which diverts their time and energy away from the organization's primary mission. Moreover, engaging in commercial activities might attract business-oriented managers whose managerial talents can divert the organizational focus away from the original mission (Tuckman & Chang, 2006: 634).

#### **IV. The Analytical Framework for Social Enterprises**

As the previous sections discuss, accountability is an information generation process that contains two essential elements: 1) the sources of accountability (internal vs. external); and 2) the expected values (economic vs. social) that an actor is held accountable for. In terms of the sources of accountability, there are both external and internal stakeholders who demand accountability information of social enterprises. Internal stakeholders of social enterprises include the executive, board members, staff and volunteers who involved in the process of decision making, and goods and services producing activities in social enterprise. External stakeholders of social enterprises include the government, donors, clients, potential investors, customers and the public

who own the authority or resources that may have influence on social enterprises' operation. In terms of the expected values that actors are held accountable for, social and economic values are equally concerned and expected by various stakeholders in social enterprises. Internal and external stakeholders expect social enterprises to not only create social impact but also maintain their financial sustainability.

In sum, accountability in social enterprises is distinctive in two aspects: mixed stakeholders and double bottom line. Combining these two dimensions yields a two by two matrix with four cells as illustrated in Figure 3. The description of each cell in the matrix is followed.

Figure 3 The Matrix of Accountability in Social Enterprise

		Expected Values	
		Social	Economic
Sources of accountability	Internal	Mission (1)	Financial sufficiency (2)
	External	Legitimacy (3)	Market forces(4)

Cell 1: Accountability for mission

As several researchers have emphasized, the mission is the soul of the social enterprise (Alter, 2006; Dees, 1998, 2003; Foster & Bradach, 2005). It is serving social needs makes social enterprises different from business ventures. Social enterprises consist of the actors, including executives, board members, staff and volunteers, who are sharing the same vision and mission. Members in social enterprises are motivated by mission. The shared belief influences individuals on making accountable actions and decisions that lead the organization generate social impacts.

The accountability information associated with managerial processes is required. As accountability information users, internal stakeholders, including board members, executives, staff, and volunteers need the information about whether and how the projects and activities contribute to desired social change.

#### Cell 2: Accountability for financial sufficiency

Social enterprises are expected to be financially self-sufficient by generating adequate income to cover their operating and social programs costs without continued reliance on donor funding. Social enterprises are encouraged to diversify income sources and adopt business-oriented resource management skills to ensure they will be financially sufficient.

Cell 2 demonstrates that the accountability information about generating economic values is important to the internal stakeholders in social enterprises. In order to maintain financial sufficiency, internal stakeholders have the need of information for finance management purposes. For example, internal stakeholders such as board members and executives need the information about portfolio management, and information about how a commercial activity creates financial sufficiency for their organization.

#### Cell 3: Accountability for legitimacy

Recently, stakeholders increasingly expect nonprofit organizations to achieve larger-scale social impacts. Social enterprises are established to “strengthen, expand, or enhance their missions by creating more meaningful social impact, by reaching new client markets, or by diversifying their social services (Alter, 2006: 206).” Although it is the pro-business and pro-market values that makes social enterprise a preferred institutional form, generating social change is still the core value of social enterprises. As

Dees (2003) emphasized, “it is a social venture only if social considerations are integrated into its objectives and management.”

Edwards (1999) defines NGO legitimacy as “...having the right to be and do something in society -- a sense that an organization is lawful, proper, admissible, and justified in doing what it does, and saying what it says, and that it continues to enjoy the support of an identifiable constituency (p. 258).” The legitimacy of social enterprises is granted by external stakeholders. Cell 3 refers that social enterprises obtain their legitimacy by carrying out social impacts and fulfilling the expectations of external stakeholders effectively. Therefore, external stakeholders, including clients, donors, and the public, need the accountability information about whether and how social enterprises generate positive social impacts to the society. Besides, social enterprises set in the non-for-profit form should follow the legal regulation and rules to maintain their tax exemption status. Therefore, the government’s legal regulation is one of the sources of legitimacy accountability.

#### Cell 4: Accountability as market forces

Cell 4 refers that social enterprises are held accountable through market mechanism. Generating income through business-oriented activities is a common strategy that social enterprises adopt to diversify funding sources and maintain financial stability. Hence, social enterprises also play a role as a supplier. The properly functioning markets can hold social enterprises accountable. Social enterprises provide quality services with competitive price to successfully attract customers, or they would be eliminated through market competition.

Furthermore, a feasible and profitable business model can help social enterprises attract the funding from potential investors. Investors are the audience of social enterprises’ business plan for the purpose of obtaining financing. However, from the

moment potential investors decide to invest, their role shifts from external stakeholders to the internal stakeholders who have influence on the social enterprise' decision making.

In sum, this matrix is proposed as an analytical framework that can be applied to social enterprises for examining what kind of accountability information should be generated and for whom. Social enterprises are expected to achieve their mission, and be self-sufficient financially. They also maintain legitimacy by generating social impacts as their external stakeholders expected. Social enterprises also need to fulfill their external stakeholders' expectation on the market performance.

However, the matrix should not be merely understood and interpreted as four individual cells. The dotted line in the matrix represents the interrelationship between social and economic values in the accountability system. The major challenge social enterprises facing is to make a logical connection between creating social impacts and generating revenue activities. Alter (2006) describes the relationship between social and economic goals are intertwined like DNA in social enterprises:

“The crux of the individual social enterprise lies in the specifics of its dual objectives – depth and breadth of social impact to be realized, and amount of money to be earned. Mission drives social value creation, which is generated through not-for-profit programs. Financial need and market opportunities drive economic values creation, which is delivered through business models. As a result, money and mission are intertwined like DNA in the social enterprise...” (p. 206)

From internal stakeholders' perspective, leaders and managers in social enterprises do not carry out social and economic goals separately. From external stakeholders' perspective, consumers may be willing to consume social enterprises' services and goods with higher price, because they don't see the transaction as a pure business but a kind of charity. Therefore, the social-related and economic-related information should not be treated as disjointed pieces that are generated merely for serving different accountability purposes respectively. It is more important to bridge the two types of information to hold social enterprises accountable.

Furthermore, there might be tensions between different expected values and between different stakeholders. For example, social enterprises who receive charity donations from general public may be expected to open all organizational activities to public. However, investors may request recipient organizations to keep certain business secrets in order to maintain competitiveness and profitability.

## **V. Discussions**

One of the challenges of holding social enterprises accountable is to identify the proper balances between different values and interests among stakeholders. First of all, the balance is not a fixed standard, but rather a dynamic condition in the changing environments. As Imperatori & Ruta (2006) indicate, social enterprises operate in a changing environment in which “elements and context conditions can change over time and modify the social impact and economic results (p. 107).” Moreover, the standard of expected performance is dynamic as well. As Kearns (1996) indicated, the standard of accountability is a “moving target”. This is because “while the standards of accountability are often formally codified in laws and regulations, they also are defined by implicit expectations of taxpayers, clients, donors and other stakeholders.” If the expectations change, so do the standards of accountability. Third, it’s hard to measure both financial and social impacts performance in short time frames. One could not manage social enterprises’ performance without measuring it. Although one can measure social enterprises’ financial performance annually, it may take several years to make social impacts observable.

The difficulties of balancing the social and economic values in social enterprises associate with the concern of mission drift issue. With double bottom line, social enterprises are expected to create social as well as economic values. Stakeholders want to make sure their money was not wasted, the programs have been implemented in effective

way, and finally, organizations' efforts have successfully produced both social and financial return of investment. The nature of dynamic between social and economic values increases challenges of detecting whether social enterprises are drifting away from their social mission (Bielefeld, 2006: 17).

The difficult of measuring social impact is one of factors that makes it is challenging to manage the balance of social and economic values in social enterprises. It is relatively easy to measure the tangible financial performance than to evaluate the social impact generated by social enterprises. With the traditional logic model of organizational performance, we may infer organizational impacts by measuring the input of resources, process of activities and the outputs (Wei-Skillern et al., 2007: 326). In other words, we assume that, logically, there is a strong positive correlation between social impacts and sufficient inputs, effective program implementation, and desirable outputs. However, in practice, there are several technical and psycho-social limitations to make such interferences (See Cutt & Murray, 2000: 29-41).

In practice, the primary accountability issue facing social enterprises is the lack of enforcing mechanisms. Currently, there is no independent agency to enhance social enterprises accountability. In a recent Aspen Institute roundtable, participants discussed the use of new legal forms and tax structures to promote and regulate social enterprises organizations (Billitteri, 2007). For instance, social enterprises can be incorporated as limited liability companies (LLC); therefore, they can achieve social missions but at the same time, maintains their flexibility in attracting investment from individuals and financial institutions. Besides, there is no such watchdog institute to monitor and evaluate social enterprises' financial and social mission achievement.

The current accountability mechanism is limited in its analysis of knowledge sharing and technical support among social enterprises. For instance, the Social Enterprise Alliance is a membership organization that aims to advocate nonprofit organizations adapting earned income strategies by providing practitioners with learning

opportunities and technical assistances. The National Center on Nonprofit Enterprise is established to help nonprofit organizations doing business venturing by holding conferences, training and consulting.

The goals of accountability are not only to control and monitor an organization's performance but also to make an organization be learning and be improved. Ebrahim (2005) argued that an effective accountability system should be connected to organizational learning. His propositions suggested that organizational learning is more likely occur if organizations pay attention to the importance of evaluation, embrace errors as opportunities to improve, enhance responsiveness to environmental uncertainties, improve communication structures, provide incentives and training, build simple and flexible information systems, and strengthen relationships between mission and accountability.

The proposed analytical framework in this paper may help to classify the notion of accountability in social enterprises. Meanwhile, the framework provides a potential perspective for developing new logical model of performance management and designing proper accountability mechanisms. The matrix illustrates how different values and multiple information users frame the accountability issues in social enterprises. It also visualized the possible tensions between values and between stakeholders. The performance measurement of social enterprises may need a new logic model which can contain the performance information about both financial and social achievements and reveal the tension and balance between the two ends of goals.

The proposed framework also reveals that the importance of finding accountability mechanisms to hold social enterprises accountable and maintain their autonomy and flexibility as well. Social enterprises need to earn the public trust in order to maintain their legitimacy. According to Kearns (1996), accountability is “the obligation of public and nonprofit organizations to serve a higher authority – the public trust – which is the ultimate source of their mandate, their authority and their legitimacy.”

Meanwhile, social enterprises still need to have the autonomy and flexibility in running business. Accountability is always a mix of internal and external controls. As McCambridge analyzed, “there are many highly regulated situations where the culture is to beat the regulations or to drift to the lowest allowable compliance level. On the other hand, to have no regulations or monitoring where other people’s money is being used in trust is absurd. There are simply too many entrepreneurial souls out there looking for the right niche for their next scam (2005: 5).” Further researches is needed to identify the accountability mechanisms that can properly regulate social enterprise from ruining public trust, while still allowing them the flexibility and autonomy needed to generate social value.

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