

# Challenges in the Distinction and Reporting of Business Activities of Non-Profit Legal Entities

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**Abstract.** In the contemporary economic environment, non-profit legal entities (NPOs) are increasingly challenged to secure sustainable financial resources to fulfil their public benefit objectives. The limited access to funding through donations, subsidies, and grants leads to the growing necessity of engaging in business activities as an additional source of revenue. This situation brings forth numerous challenges regarding financial reporting, regulatory compliance, and the taxation of income generated through such activities. The article examines the key challenges faced by NPOs when distinguishing and accounting for business activities. Based on the applicable regulatory framework and current practices, potential approaches to enhancing the accountability and transparency of such activities are discussed.

**Key words:** non-profit activities, business activities, non-profit legal entities (NPOs).

*Received:* 15.06.2025

*Revised:* 21.12.2025

*Accepted:* 26.12.2025

*Published:* 31.12.2025

## 1. Introduction

In the contemporary economic environment, non-profit legal entities (NPOs) play a significant role in the development of social, cultural, and educational initiatives that contribute to the public good. The primary financial resources of these organizations have traditionally been secured through donations, subsidies, and grants. In addition, NPOs often engage in ancillary economic activities aimed at generating supplementary income, ensuring financial sustainability, and enhancing the effectiveness of their mission delivery (Anheier, 2014, p. 103).

The pursuit of economic activities by non-profit legal entities gives rise to substantial accounting, tax, and regulatory challenges, particularly with regard to the delineation between their economic and non-economic (public benefit) activities.

The absence of unified criteria for classifying revenues and expenses creates considerable uncertainty regarding their accounting treatment and tax implications (Cordery & Baskerville, 2011, p. 3). Additional difficulties arise in the recognition and allocation of so-called „non-allocable expenses” - those that cannot be directly attributed to a specific type of activity - particularly in the absence of a standardized and consolidated methodology (Breen, Ford & Morgan, 2018, p. 614).

Certain limitations in the legal framework, coupled with the lack of commonly accepted methodological approaches, lead to uncertainty not only for NPOs themselves but also for donors, regulatory and tax authorities, partners, and beneficiaries, all of whom depend on clarity, comparability, and transparency in financial reporting (Breen, Ford & Morgan, 2016).

In this context, the provision of high-quality, reliable, and structured information becomes particularly important, as it enables a proper assessment of both the effectiveness and the public value of NPO activities.

Accurate and consistent differentiation between economic and non-economic activities within non-profit legal entities is a fundamental prerequisite for achieving such reporting clarity. This distinction directly impacts the accounting treatment of revenues and expenses, the organization's tax obligations, and the trust of external stakeholders.

Despite the significance of the issue, the existing body of literature remains limited. Most publications consist of general legal commentaries, lacking practically applicable methodological solutions for differentiating economic and non-economic activities in the financial reporting of NPOs.

The relevance of this topic is further heightened by the fact that over 30,000 non-profit legal entities are registered in Bulgaria, many of which engage in both types of activities in practice (Bulgarian Center for Not-for-Profit Law, 2024, p. 5). This underscores the need for a comprehensive and systematic examination of the issue.

**The present study aims to analyze the criteria for differentiating between economic and non-economic activities of non-profit legal entities, to identify the key challenges in their accounting treatment, to examine the scale, dynamics, and profitability of economic activities, and to assess the extent to which existing models of organizational and financial separation ensure the necessary level of reporting transparency and compliance with the regulatory framework.**

## 2. Theoretical and Regulatory Aspects of the Distinction Between Business and Non-Profit Activities in Non-Profit Legal Entities

The business activities of non-profit legal entities encompass a wide range of forms — including the sale of souvenirs, books, handmade goods, promotional materials, as well as the provision of paid services such as trainings, seminars, consultations, or the leasing of property, among others.

This diversity gives rise to a number of practical and regulatory challenges related to **the distinction between business and non-profit activities**, their classification, accounting treatment, and tax implications. In this context, **a clear regulatory framework, applicable accounting standards, and robust organizational models** are key prerequisites for ensuring high-quality and reliable reporting, comparability, and a high level of transparency when both types of activities are combined within a single legal entity. In order to prevent deviations from the public mission of non-profit legal entities, the legislator has established specific restrictions and conditions concerning the conduct of business activities.

The main piece of legislation in this area is the **Non-Profit Legal Entities Act**. According to Article 3, paragraph 3 of the Act, *“Non-profit legal entities may carry out additional business activities only if they are related to the subject of the main activity and if the income is used to achieve the goals set forth in the statute or founding act”* (Zakon za yuridicheskite litsa s nestopanska tsel, izm. i dop., Darzhaven vestnik, br. 25 ot 2023 g.).

According to the clarifications provided by D. Georgieva, the **complementary nature of business activities** is justified by the requirement that the majority of an organization’s resources be directed toward achieving its non-profit objectives, rather than toward conducting commercial transactions (Georgieva, 2018, p. 86). In this regard, complementarity is assessed not only based on the nature of the activity, but also on **how the organization’s resources are allocated**. If the greater part of human, financial, and organizational resources is directed toward business activity, that activity ceases to be regarded as additional.

The absence of a legal definition and statutory criteria, as well as the lack of **quantitative or functional indicators of “complementarity”** in the law, makes the application of Article 3, paragraph 3 of the Non-Profit Legal Entities Act difficult, creating conditions for inconsistent interpretation, regulatory uncertainty, and a heterogeneous approach among organizations.

Such legal wording gives the impression that the “complementarity” requirement refers solely to the volume of revenue from business activities. In practice, however, the complementary nature should be interpreted **functionally - as a subordinate role of the business activity in relation to the organization’s core non-profit objective - rather than solely in quantitative terms**.

The key provision in Article 3, paragraph 3 of the Non-Profit Legal Entities Act, which allows for additional business activity only if it is related to the organization’s main non-profit purpose, remains legally undefined and abstract. The law does not provide a specific definition of what constitutes “related to the subject of the main activity”, leading to subjective interpretations by both organizations and regulatory authorities (Dimitrova, 2011, p. 140; Georgieva, 2019, p. 112). In practice, difficulties often arise when assessing the connection between business activity and the non-profit purpose, particularly in the absence of objective assessment criteria. For example, an environmental NPO offering computer literacy or language courses may raise questions about the relevance of such activities to its declared non-profit mission.

A fundamental requirement set forth in the law is the prohibition on the distribution of profit among founders, members, or third parties. Any profit generated from additional business activities must be used exclusively for the purposes outlined in the organization’s founding act or statute.

The distinction between business and non-profit activities is not only a legal requirement but also a fundamental prerequisite for establishing a reliable accounting policy. It determines the **structuring of the entity’s chart of accounts**, the development of internal rules for classification and analytical reporting, the proper allocation of revenues and expenses, as well as the preparation of financial statements in compliance with applicable accounting standards.

A clear separation between the two types of activities ensures compliance with the regulatory framework, a high degree of accountability, and traceability of financial flows. Non-profit legal entities are required to apply the provisions of **National Accounting Standard 9 (NAS 9)** "*Presentation of Financial Statements of Non-Profit Enterprises*", which mandates **separate presentation of revenues and expenses for each type of activity** (NAS 9, 2006, para. 1.3).

A clear distinction between business and non-profit activities is also required in order to ensure the proper allocation of so-called "**non-allocable expenses**" - costs that cannot be directly attributed to a specific activity.

Non-profit legal entities are required to prepare and present **two separate income and expenditure statements** - one for non-profit activities and another for business activities. The statement for non-profit activities also includes information on the result of business activities as a component of the overall reporting outcome. At the same time, the income and expenditure statement for business activities must be prepared in accordance with **National Accounting Standard 1 (NAS 1)** and must reflect the outcomes of commercial transactions in line with general accounting principles. The purpose is to ensure **reporting transparency, comparability, and the possibility of analytical control**.

From an accounting perspective, the result of business activities is reported separately and is subject to taxation under the **Corporate Income Tax Act (Zakon za korporativnoto podohodno obligane – ZKPO)**. After adjustment in accordance with tax regulations, the **net result is transferred to the non-profit activity** and must be disclosed in the income and expenditure statement for non-profit activities as a separate line item, in accordance with the requirements of **NAS 9**.

All of the above aspects highlight the need for the development and implementation of an **accounting policy and analytical reporting system** that ensures both the traceability of operations and compliance with the organization's statutory objectives.

Incorrect or incomplete differentiation of revenues and expenses may lead to **distorted financial results** and, consequently, to incorrect taxation. Moreover, there is a risk of creating a **misleading impression of the profitability of business activities**, which could result in inadequate management decisions and/or a loss of trust from donors, partners, and the general public.

Nevertheless, **NAS 9** does not provide specific criteria for classifying an activity as either business or non-profit. This opens the door to **subjectivity, inconsistent application, and practical difficulties** (Dimitrova, 2011, p. 140).

The financial reporting obligations of non-profit legal entities are also linked to the requirements of the **Value Added Tax Act (Zakona za danak varhu dobavenata stoynost (ZDDS))**. Organizations must register for VAT when they generate **taxable turnover exceeding the statutory threshold for their business activity** (ZDDS, izm. i dop., DV br. 96 ot 2023, chl. 96, al. 1).

According to Article 3, paragraph 1 of the law, when a non-profit legal entity provides a service in exchange for remuneration, this is treated as an **economic activity subject to taxation**, even in the absence of a positive financial result (art. 3, para. 1 **Zakon za danak varhu dobavenata stoynost (ZDDS)**).

In this context, the same event - for example, a **charity concert with a fixed ticket price**, where the proceeds do not cover the incurred expenses - is classified as a business activity due to the presence of consideration. Similarly, **monthly training sessions conducted for a fee**, even if consistently unprofitable, fall within the scope of taxable activities due to their market nature and recurring character.

What matters fundamentally is **not whether a profit has been realized**, but whether the service is provided **for consideration, according to market principles, and with a certain degree of regularity**.

This interpretation is also confirmed in the practice of the **National Revenue Agency (Natsionalna agentsiya za prihodite – NAP)**. In opinion No. 96-00-31 of 2018, it is stated that "*the provision of a paid service involving consideration falls within the scope of taxable supplies, regardless of whether a profit has been generated*" (NAP, 2018, p. 2).

Such interpretations create **regulatory uncertainty for organizations**, particularly in cases where an activity is closely aligned with their statutory objectives but, based on formal criteria, is classified as a business activity.

In addition to the requirements under the **Zakon za danak varhu dobavenata stoynost (ZDDS)**, the proper application of the **Corporate Income Tax Act (Zakon za korporativnoto podohodno obligane – ZKPO)** is of critical importance for non-profit legal entities. This act further emphasizes the necessity of a **clear distinction between business and non-profit activities**, as the tax treatment of revenues and expenses depends directly on such differentiation.

When non-profit entities generate income from commercial transactions, they are regarded as **taxable persons** within the meaning of the ZKPO and are subject to taxation under the general corporate income tax regime. The **positive financial result** generated from business-related transactions is taxable, whereas the **positive**

**result from non-profit activities** is not subject to corporate income tax (art. 1, item 2, **ZKPO**, izm. i dop., Darzhaven vestnik, br. 104 ot 2022 g.).

Tax implications for non-profit entities arise not only in relation to revenues but also with respect to certain expenses - such as **representative expenses, in-kind social benefits, and vehicle operating costs** (arts. 204 - 209 ZKPO) - when they are associated with business activity. This necessitates **precise identification and separate accounting** of revenues, expenses, and the respective activities that give rise to tax liabilities.

An analysis of the current legal framework reveals that the regulations applicable to non-profit legal entities are **dispersed across several legislative acts**, and that significant uncertainties arise in practice when applying them.

Although the existing statutes address different aspects of NPO operations - **legal, accounting, and tax-related** - they do not provide **explicit criteria for clearly distinguishing between business and non-profit activities**.

As a result, organizations are often forced to rely on their own interpretations when classifying activities, which leads to **uncertainty and inconsistency in accounting and tax practices**.

In light of these challenges, this study adopts an **analytical approach to summarizing the key distinguishing features** between business and non-profit activities. The following table systematizes the main criteria derived from the legal framework, accounting standards, and specialized literature:

**Table 1.**

Comparison Between Business and Non-Profit Activities in Non-Profit Legal Entities (NPOs)

<b>Criterion</b>	<b>Business Activity</b>	<b>Non-Profit Activity</b>
<b>Purpose of the activity</b>	Generating profit, which is not distributed but used for non-profit purposes	Achieving public benefit or private goals set forth in the statute or founding act of the NPO
<b>Mode of delivery</b>	Market-based, for a fee	Free of charge or for a symbolic amount
<b>Regularity</b>	Recurring, with planned or ongoing nature	Sporadic, project- or campaign-based
<b>Recipients</b>	The general public, market participants	Specific social group or cause; targeted or vulnerable communities
<b>Applicable legal acts</b>	<i>Zakon za korporativnoto podohodno oblagane (ZKPO), Zakon za danak varhu dobavenata stoynost (ZDDS), Zakon za yuridicheskite litsa s nestopanska tsel (ZYLNTs), NAS 1, NAS 9, and other applicable standards</i>	<i>NAS 9 and ZYLNTs</i>
<b>Corporate income tax (ZKPO)</b>	Subject to corporate income tax on the positive financial result	Not subject to corporate income tax on the positive result from non-profit activities
<b>Value-added tax (ZDDS)</b>	Taxable if the registration threshold is met or through voluntary registration; the general VAT regime applies	Not taxable unless it contains a commercial element; registration under art. 97 ZDDS may be required (e.g. cross-border services or intra-community acquisitions)
<b>Expense tax (ZKPO)</b>	Payable on representative expenses, in-kind social benefits, vehicle operating costs, if related to business activity	Not payable on representative expenses related to non-profit activity; social expenses may be taxable even under non-profit activity
<b>Typical sources of income</b>	Revenues from sales of products, goods, and services; rental of long-term assets; sale of materials; other market-oriented activities	Revenues from regulated activities; membership fees; program-based funding (conditional); government programs; unrestricted donations
<b>Typical expense directions</b>	Expenses for production and services, salaries and remuneration, marketing, procurement, rent, logistics, external services	Expenses for donations; provision of social services, campaigns, training, materials, project-based remuneration, administrative support
<b>Examples</b>	Sale of calendars, books; fee-based training; property/venue rental; consultancy; paid publications and events;	Free training, volunteering, humanitarian aid, charity campaigns, free consultations, social services, public lectures, awareness

	advertising contracts; sale of handmade goods	campaigns, free events, dissemination of materials
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Source: Author's compilation based on the applicable legal framework and relevant literature.

The presented table does not claim to be exhaustive but offers a structured overview of the key differences between business and non-profit activities that are essential for the **financial management and reporting of NPOs**. It may serve as a reference point for assessing hybrid activities, developing analytical accounting systems, and supporting management decisions related to activity planning and expansion.

In pursuit of more effective differentiation and risk minimization, **many NPOs adopt the approach of separating business activities through the establishment of a separate commercial entity**. This model provides greater reporting clarity, potential for market expansion, and separate legal liability. However, it also entails **higher administrative burden and requires strong managerial capacity**.

The choice between conducting business activities **within the organization itself** or through a **separate commercial entity** should be based on an analysis of **profitability, associated risks, and the administrative burden** of each option. In this context, the profitability of business activities should not be viewed solely in terms of profit generation, but rather evaluated as a **tool for achieving financial sustainability**, aligned with the organization's mission.

The following section of this study presents an **empirical analysis of selected Bulgarian non-profit legal entities**, examining specific models of structuring, reporting, and managing business activities. Through a **comparative approach**, the study explores the variations in how NPOs engage in business activities.

### 3. Empirical Analysis of Reporting and Differentiation Models for Business Activities in Non-Profit Legal Entities

The business activities of non-profit legal entities and their role in **financial sustainability, accountability, and strategic management** have been extensively studied in the international academic literature. Scholars such as Salamon (2003), Anheier (2014), Frumkin (2002), Tuckman & Chang (1991), and Toepler (2004) have examined the processes of "**commercialization**" within NPOs, focusing primarily on the reasons behind the development of business activities, their impact on the social mission, organizational identity, and resource management.

Only a limited number of studies—such as those by Cordery & Baskerville (2011) and Toepler (2004)—offer **methodological approaches for measuring the degree of commercialization and the profitability of business activities**.

For the purposes of this study, the methodology proposed by the aforementioned authors has been adopted, as it enables an assessment of the **relative significance of business activities in the overall operations of non-profit legal entities**.

The analysis is based on two primary indicators, which were calculated in advance and outside the scope of this article, and are used as the foundation for interpreting the results.

**The relative share of net sales revenue from business activities (RSNSR)** in relation to the total revenue of the organization, serving as an indicator of the degree of commercialization (Toepler, 2004; Cordery & Baskerville, 2011). Total revenue is understood as the sum of revenue from non-profit activities, net sales revenue, and all other relevant income reported in the income and expenditure statement for the respective year.

This method allows for tracking the dynamics of revenue structure and the extent to which business activities contribute to the organization's overall operations. The indicator is **crucial for evaluating the sustainability and strategic relevance of business activities within the NPO itself**.

**Return on Equity (ROE)** and **Net Profit Margin (NPM)** of the Subsidiary Companies of NPOs

The first indicator - **Return on Equity (ROE)** - is calculated as the ratio of **net profit to the average value of equity** over the analyzed period. It measures the return generated on the equity invested, indicating **how many units of net profit are earned for every unit of equity**. This indicator is essential for assessing the profitability of subsidiary entities and their contribution to the **sustainable financing of the NPO's non-profit activities**.

The second indicator - **Net Profit Margin (NPM)** - is defined as the ratio of **net profit to net sales revenue**. It shows what portion of the revenue remains as net profit after all expenses have been deducted. This ratio provides an evaluation of the **efficiency of the core business activity** of the subsidiaries and its significance for the **financial sustainability** of the organization.

The values of both indicators are presented as percentages, with the results multiplied by 100.

Profitability was calculated **only for the subsidiary companies**. This approach is justified by recommendations in the literature (Cordery & Sim, 2018), which suggest that calculating profitability at the NPO

level is **inappropriate in the absence of analytically separated financial data** for business activities, as it would result in a **mixing of business and non-business revenues and expenses**.

By applying these methods, the study aims to determine:

- the **role and significance of business activities** in the revenue structure of NPOs;
- the **profitability of existing subsidiary commercial entities**;
- how the results from business activities relate to the **sustainability and strategic management** of the organizations.

Based on a **comparative analysis** and review of the annual financial statements and activity reports of **twelve Bulgarian non-profit legal entities for the period 2021–2023, the study identifies key patterns and challenges in the reporting of business activities**.

The empirical sample is drawn from an official list by the National Statistical Institute of the 100 NPOs with the highest non-profit revenue. Organizations established under special laws, including trade unions and employers' organizations, were excluded due to their specific legal status and distinct reporting and funding regimes. The remaining organizations were classified into four fields of activity: Humanitarian and Social Services, Environmental Protection, Education and Culture, and Sports.

The primary selection criterion was the presence of business activity conducted in addition to non-profit activities, either directly by the NPO or through a subsidiary commercial entity. To ensure balanced representation across fields, three organizations were selected from each category, resulting in a final sample of **twelve NPOs**. In one field (Education and Culture), for the year 2022, where the initial list did not provide a sufficient number of suitable cases, an additional smaller organization meeting the same selection criterion was included to ensure equal representation.

The analysis covers the period 2021–2023 and is based on publicly available financial statements and annual activity reports. The degree of commercialization is assessed using the Relative Share of Net Sales Revenue (RSNSR), while the financial performance of business activities carried out through subsidiary companies is evaluated using Return on Equity (ROE) and Net Profit Margin (NPM).

The results are summarized in the following table:

**Table 2.**  
Relative Share of Net Sales Revenue (RSNSR) in the Revenue Structure of the Analyzed NPOs (2021–2023)

No.	NPO	Category	RSNSR (%) 2021	RSNSR (%) 2022	RSNSR (%) 2023
1.	SOS Detski selishta Balgariya	Humanitarian and Social Services	1.41	1.68	1.54
2.	Sdruzhenie „Sayuz na slepите v Balgariya“	Humanitarian and Social Services	55.45	48.58	59.62
3.	SNTs „Ekvilibrium“	Humanitarian and Social Services	0.78	0.87	0.18
4.	Ekologichno sdruzhenie „Za Zemyata“	Environmental Protection	0.36	0.09	0.04
5.	Zeleni Balkani – Stara Zagora	Environmental Protection	1.87	1.14	0.57
6.	Sdruzhenie „Balgarsko druzhestvo za zashtita na ptitsite“	Environmental Protection	1.44	3.57	2.43
7.	Fondatsiya „Zaedno v chas“	Education and Culture	12.59	16.00	3.30
8.	Sdruzhenie „Fridrih Shiler“	Education and Culture	0.00	0.00	4.24
9.	Fondatsiya „Chudomir“	Education and Culture	9.68	25.37	59.36
10.	Balgarska federatsiya po voleybol	Sports	24.91	37.45	25.42

11.	Sayuz na balgarskite avtomobilisti	Sports	55.63	36.02	38.35
12.	Balgarski futbolen sayuz	Sports	21.11	15.26	21.04

Source: Author's analysis based on the annual financial statements and activity reports of the examined entities

The results reveal **distinct differences both across the various NPO categories and within individual organizations** during the 2021–2023 period.

Firstly, NPOs operating in the field of **humanitarian and social services**, such as *SOS Detski selishta Balgariya* and *SNTs "Ekvilibrium"*, show a **consistently low relative share of revenue from business activities—below 2%**. This confirms their focus on delivering free services and securing funding primarily through donations and grants.

Conversely, organizations such as *Sayuz na slepite v Balgariya*, *Sayuz na balgarskite avtomobilisti*, *Balgarska federatsiya po voleybol*, and *Balgarski futbolen sayuz* demonstrate a **substantially higher share of net sales revenue**, with some exceeding 50%. This reflects the presence of **well-established business operations**, and in these cases, business activity plays a significant role in **financially supporting their non-profit missions**.

Among educational and cultural organizations, **significant heterogeneity is observed**. While *Fondatsiya „Zaedno v chas“* and *Sdruzhenie „Fridrih Shiler“* generate only a **modest share of business-related revenue** (up to 16%), *Fondatsiya „Chudomir“* exhibits a **markedly increasing share**, reaching **59% in 2023**. This indicates a **shift in the funding model and structure**, with a stronger emphasis on **market-oriented activities**.

The environmental NPOs in the study—*Ekologichno sdruzhenie „Za Zemyata“*, *Zeleni Balkani – Stara Zagora*, and *Sdruzhenie „Balgarsko druzhestvo za zashtita na ptitsite“*—consistently maintain a **low share of revenue from business activities** (below 5%). These organizations rely primarily on **external funding and donations**, with business activities playing a **supplementary role**.

Temporal dynamics are also evident: some organizations exhibit **stability over time** (e.g., *Ekvilibrium* and *Za Zemyata*), while others show **fluctuations** related to changes in the **scope or intensity** of business operations (e.g., *Sayuz na balgarskite avtomobilisti* and *Fondatsiya „Chudomir“*).

The literature does not establish universally accepted or strictly defined thresholds for classifying the **degree of commercialization** of NPOs, which is attributed to the high degree of variability across sectors and types of non-profit organizations (Toepler, 2004; Cordery & Baskerville, 2011).

In this study, and in line with approaches commonly applied in the literature, three indicative categories were adopted—**low, moderate, and high degree of commercialization**.

Among the twelve NPOs analyzed, the following patterns were observed:

- **Organizations with a low degree of commercialization** (net business revenue share not exceeding 5% in 2023) include: *SOS Detski selishta Balgariya*, *SNTs "Ekvilibrium"*, *Ekologichno sdruzhenie "Za Zemyata"*, *Zeleni Balkani – Stara Zagora*, *Sdruzhenie "Balgarsko druzhestvo za zashtita na ptitsite"*, *Fondatsiya "Zaedno v chas"*, and *Sdruzhenie "Fridrih Shiler"*.
- **Organizations with a moderate degree of commercialization** (net business revenue share between 5% and 25% in 2023) include: *Balgarski futbolen sayuz* and *Balgarska federatsiya po voleybol*.
- **Organizations with a high degree of commercialization** (business revenues exceeding 25% of total revenues in 2023) include: *Sdruzhenie "Sayuz na slepite v Balgariya"*, *Sayuz na balgarskite avtomobilisti*, and *Fondatsiya "Chudomir"*.

This classification makes it possible to conclude that the **relative share of revenue from business activities is highly dependent on the field of activity and the strategic model of the organization**. While **social and environmental organizations** typically exhibit a low level of economic activity and a comparatively small share of business revenue, **sports and certain cultural NPOs** rely more heavily on income from commercial activities to support their non-profit missions.

These findings **reinforce and expand upon conclusions in the international literature** regarding the specific relationship between commercialization, sectoral context, and organizational strategy (Weisbrod, 1988; Salamon, 2003; Toepler, 2004).

The present analysis provides an **empirical foundation for the subsequent evaluation of the profitability of business activities** conducted through the **subsidiary commercial entities** of NPOs. In this context, the inclusion of subsidiaries in the study is justified by the need to gain a **comprehensive and analytical understanding of the structural characteristics and scale** of business operations within NPOs.

The key findings from the profitability analysis of business activities conducted through the organizations' subsidiaries are presented below.

**Table 3.**

Return on Equity (ROE) and Net Profit Margin (NPM) of Subsidiary Companies of the Analyzed NPOs  
(2022–2023)

Parent NPO	Subsidiary	ROE % 2022	ROE % 2023	NPM % 2022	NPM % 2023	Notes
SOS Detski selishta Bulgariya	ChDG Drenchta EOOD	–	–	75.00	-54.66	Newly established; negative equity in both years
Sayuz na slepите v Bulgariya	Uspeh Filtar SSB EOOD	15.27	4.32	30.52	10.87	
Sayuz na slepите v Bulgariya	Relaxtur – SSB EOOD	18.18	15.38	16.66	5.00	
Balgarski futbolen sayuz	Natsionalna futbolna baza EAD	0.00	1.01	0.00	0.53	Only other income/expenses in 2022– 2023; negative equity in 2021
Sayuz na balgarskite avtomobilisti	SUAB - SBA EOOD	6.03	7.54	1.08	1.35	
Sayuz na balgarskite avtomobilisti	SHIPKA - T.A. EOOD	–	6.66	–	–	Negative equity
Balgarska federatsiya po voleybol	Voley Promotion EOOD	–	–	3.92	7.00	Negative equity in 2022– 2023
Balgarsko druzhestvo za zashtita na ptitsite	BDZP EOOD	26.08	-8.96	14.48	-5.54	Positive equity in 2022; negative in 2023
Balgarsko druzhestvo za zashtita na ptitsite	Neofron EOOD	–	–	–	–	No activity in 2021; zero equity in 2023
Zaedno v chas	Zaedno 2011 EOOD	–	–	–	–	No activity after 2021
Zaedno v chas	Akademiya Nike EOOD	–	–	–	–	Deregistered legal entity

Source: Author's analysis based on annual financial statements and activity reports of the examined entities

The study covers **11 commercial subsidiaries** through which part of the analyzed NPOs conduct their business activities. The analysis reveals **significant heterogeneity in terms of profitability and financial condition**, with several key trends emerging:

1. **Negative or unstable equity** – Three companies - **ChDG Drenchta EOOD** (SOS Detski selishta Bulgariya), **Voley Promotion EOOD** (Balgarska federatsiya po voleybol), and **BDZP EOOD** (in 2023) - recorded **negative equity**, which raises concerns about their long-term sustainability. In these cases, the business activity fails to generate a **positive financial result**, which, in the context of NPOs, is a serious indicator that the **business strategy may require reassessment**. If negative outcomes persist, such subsidiaries should be either **restructured or discontinued**, as their losses may compromise the **overall financial stability of the parent organization**.
2. **Low profitability among some subsidiaries** - A number of the analyzed subsidiaries demonstrate **positive but low returns on equity (ROE) and net profit margins (NPM)**. These entities cannot be classified as highly efficient, but they nonetheless manage to maintain a **positive financial result and ensure financial sustainability**. Typical representatives of this group include: **SUAB – SBA EOOD** (*Sayuz na balgarskite avtomobilisti*), with a ROE of **6.03% in 2022** and **7.54% in 2023**, and an NPM of **1.08%** and **1.35%**, respectively. **Natsionalna futbolna baza EAD** (*Balgarski futbolen sayuz*), which recorded **low but positive values in 2023** – ROE = **1.01%**, NPM = **0.53%**. **Relaxtur**

- **SSB EOOD** (*Sayuz na slepite v Balgariya*), which maintains relatively stable profitability with a ROE of **18.18% (2022)** and **15.38% (2023)** and NPM of **16.66%** and **5.00%**, respectively. This performance is consistent with expectations for activities that are **capital-intensive** or where business operations are **subordinated to the non-profit goals** of the parent organization.
3. **Positive and stable profitability** - Among the analyzed companies, several stand out for demonstrating **relatively high and sustained profitability**, indicating **effective management and well-structured business operations**, regardless of the non-profit nature of the parent organization. Two subsidiaries of *Sayuz na slepite v Balgariya* - **Uspekh Filtar SSB EOOD** and **Relaxtur – SSB EOOD** - show **stable and positive profitability** throughout the analyzed period. In 2022, *Uspekh Filtar SSB* recorded a **ROE of 15.27%** and an **NPM of 30.52%**, meaning that each BGN 1 of equity generated over BGN 0.15 in net profit, and each BGN 1 of revenue resulted in BGN 0.30 in net income. In 2023, despite a decline, both indicators remained positive (**ROE = 4.32%**; **NPM = 10.87%**), placing the company among the **financially sustainable structures**. A similar pattern is observed in *Relaxtur - SSB EOOD*, which maintained **stable profitability in both years—ROE of 18.18% in 2022 and 15.38% in 2023**, with corresponding NPM values of **16.66% and 5.00%**. This means the company achieved BGN 0.16 and BGN 0.05 in net profit for every BGN 1 of revenue, while the invested equity generated returns of BGN 0.15 to BGN 0.18. Similar trends can be seen in other subsidiaries with **positive, though lower, profitability**, but **Uspeh Filtar SSB EOOD** and **Relaxtur - SSB EOOD** clearly stand out as **notable examples of sustainability and high profitability**.
4. **Inactive or dissolved subsidiaries** - In several cases, there is a **lack of activity or legal dissolution** of the commercial entity - *Neofron EOOD* (BDZP), *Zaedno 2011 EOOD*, and *Akademiya Nike EOOD* (Fondatsiya "Zaedno v chas"). This is a **common occurrence among NPOs** when business operations are either discontinued or have proven ineffective. The **subsidiaries of the analyzed NPOs vary significantly in terms of scale and intensity** of their business activity. Some demonstrate **high profitability**, while others engage in **minimal commercial operations**, resulting in **unstable or declining profitability**.

Out of the 12 analyzed NPOs, **7 conduct business activities through established subsidiary commercial companies**, while the remaining **5 operate without creating such entities**. The data indicate that **more than half of the examined organizations (58%)** prefer to separate their business from non-profit operations through a subsidiary. This reflects a **deliberate approach to ensuring clear differentiation** between the two types of activities in both reporting and management.

As an extension of the profitability analysis, the study includes a **comparison between the relative share of business revenue** within the parent NPOs and the **financial performance of their subsidiaries** for the year 2023. The aim is to assess the extent to which the **scale of business activity**, as measured by the **Relative Share of Net Sales Revenue (RSNSR)**, correlates with its **profitability**.

- **A significant share of business activity within the NPO does not necessarily imply profitability**  
For *Sayuz na slepite v Balgariya*, *Sayuz na balgarskite avtomobilisti*, and *Fondatsiya "Chudomir"*, business activities account for **38% to 60% of total revenue** - a substantial portion of the budget. However, the **profitability of their subsidiaries varies considerably** (ranging from moderate to low). This highlights that **managing business activities poses numerous challenges**, and a larger volume of operations **does not guarantee profitability**.
- **Risk and losses are "isolated" within subsidiaries**  
Organizations such as *SOS Detski selishta Balgariya* and *Balgarska federatsiya po voleybol* illustrate that with **low or moderate commercialization**, subsidiaries may accumulate losses without directly impacting the parent NPO's consolidated reports. If such losses were accounted for within the NPO itself, they would **negatively affect the result of non-profit activities** and potentially undermine the organization's standing with **donors, members, and regulatory bodies**.
- **Establishing commercial subsidiaries minimizes accounting and strategic risk**  
Even when business activities are important for revenue, **separating them into subsidiaries enables the NPO to manage them independently** - with separate capital, governance structures, and reporting. This ensures a **clear distinction between business operations and the public benefit mission**. When business activities are conducted directly within the NPO (as seen in some organizations without subsidiaries), **any inefficiency or loss directly worsens the overall result**, complicating the interpretation of financial reports.

The comparison between the **share of business activity within NPOs** and the **profitability of their subsidiaries** leads to several key conclusions:

- **Subsidiary commercial companies are not merely an organizational form**, but represent a **critical tool for risk management, enhanced accountability, and strategic flexibility** for NPOs.
- The **separation of business activity into an independent commercial entity** is often **not driven by expectations of higher profitability**, but rather by the **need to minimize risk to the parent organization** and to **preserve clarity in reporting and management**.
- This relationship highlights an important feature of NPO financial reporting: the **use of a subsidiary to isolate business activity**, frequently noted in the literature (Weisbrod, 1988; Salamon, 2003; Toepler, 2004; Cordery & Baskerville, 2011), serves as a **risk-limiting mechanism**. It allows the business function to be **managed and evaluated independently**, without directly affecting the outcomes of non-profit operations.
- The **comparison between the two levels of analysis** demonstrates that the implementation of such a reporting model ensures **greater transparency, clarity of financial information, improved risk and resource management**, and **protection of the public benefit mission** from the volatility and uncertainty inherent in business activity.

The analysis of the **reporting and structure of business activities** carried out by **non-profit legal entities (NPOs)** - whether directly or through subsidiary commercial companies - reveals **several systemic issues** that hinder both the **external assessment of performance** and the ability to evaluate the **sustainability and contribution of business operations** to the organizations' non-profit missions.

First, although financial statements typically include a **formal distinction between business and non-business activities** (through separate Income Statements in accordance with NAS 9), in the majority of cases, **no detailed information is disclosed** regarding the **nature, scale, or results** of business operations. This significantly limits the ability of **external users** to evaluate the data. There is **limited access to analytical summaries**, interpretation of the outcomes of commercial activities, comparison with the non-profit objectives, or **assessment of economic efficiency**.

The **statutory regulation of content requirements in the Non-Profit Legal Entities Act (ZYuLNTs)** does not ensure the necessary level of detail. This becomes particularly problematic in cases where the **share of business revenue is substantial**. Another significant issue is the **lack of publicly available summarized or consolidated information** regarding **group structures** in which NPOs hold subsidiary companies. Among the organizations analyzed, **only the Bulgarian Football Union has published a consolidated financial statement**, while the rest - despite owning subsidiaries - have presented **only individual reports with insufficient references or explanations** regarding intra-group interactions. This lack of disclosure **hinders the tracking of internal transfers**, the allocation of resources, and the overall picture of **financial sustainability**. It also poses a **risk of misinterpretation** by external users, including **donors, clients, partners, and regulatory authorities**.

Another serious issue identified in the analysis relates to the **maintenance of subsidiaries with low or irregular business activity**, where **no public justification is provided regarding their role or strategic significance** for the parent NPOs. Despite their continued existence, these entities **fail to contribute meaningfully to the financial performance** of the organizations.

#### 4. Conclusion

The conducted analysis made it possible to identify **key problem areas** related to the **structure, reporting, and profitability** of business activities undertaken by NPOs. The observed differences highlight the **heterogeneity of the third sector**, while also outlining specific **challenges in the internal and external representation** of business operations and their **significance for organizational sustainability**.

Based on the study, several important **recommendations can be formulated** to improve the **accountability, management, and public transparency** of business activities carried out by NPOs through subsidiary entities:

- **Organizations should enhance the quality of publicly disclosed information** regarding their business activities by including in their annual activity reports not only overall financial results, but also an **analysis of the operations carried out**, their **profitability, strategic purpose, and connection to the non-profit mission**. This approach would support **external stakeholders in understanding the role and significance** of business activity within the broader context of the NPO's operations.
- **NPOs maintaining subsidiaries with limited or inefficient activity** should conduct a **thorough internal assessment** of their **relevance, strategic role, and contribution** to the organization's overarching goals. Sustaining entities with **minimal activity or persistent losses** poses a risk of

**inefficient resource use** and may divert attention and capacity from the organization's **core non-profit mission**.

- **In NPOs with a mixed model** (business activity both at the NPO level and through a subsidiary), **internal rules and procedures should be implemented** to ensure clearer **segregation, documentation, and public presentation** of business results. This would contribute to both **greater transparency in reporting and improved management** of intra-group financial flows.
- **A review of legislative shortcomings should be initiated, and necessary legal amendments proposed**, with the aim of establishing a **clearer and more applicable regulatory framework** for business activity reporting and oversight within NPOs.

This study confirms the **need for more detailed presentation and analysis of business activities**, both in the **annual financial statements** and in the **mandatory annual activity reports** of public benefit NPOs. In this context, the importance of developing **methodological guidelines or examples of good practice** becomes evident - tools that can support both the **practical application** of reporting standards and their **comprehensibility for external stakeholders**.

The analysis highlights several **key directions for future research** and improvements in **accounting and governance practices** within the non-profit sector. It also confirms that the **issues related to the distinction and reporting of business activities** are **not the only challenges** faced by third-sector organizations. There are also **significant difficulties in the proper classification and presentation of revenue and expenses** from non-business activities, as well as in the **allocation of common and administrative costs** between the two types of operations.

While these questions lie **beyond the scope of this study**, they constitute a **crucial component of the broader accountability framework** for non-profit entities, which will be addressed in a **separate in-depth analysis as part of a dissertation project**. The author believes that **further research and practical action in this direction are essential** to promote good practices in reporting - ones that ensure the delivery of **useful, reliable, and comprehensive information** to all stakeholders, and that help **build trust in the so-called "third sector"**.

From an international perspective, the findings of the study confirm key patterns discussed in the literature on nonprofit commercialization. The observed variation in the degree of commercialization across sectors, the frequent use of subsidiary commercial entities to isolate financial risk, and the limited transparency in reporting business activities correspond to challenges identified in other national contexts. By providing detailed empirical evidence from Bulgaria, the study contributes to the international literature on nonprofit accounting and commercialization, demonstrating how hybrid operational models function in a regulatory environment that lacks detailed methodological guidance for mixed activities.

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