

Lessons from *Doing Bad by Doing Good* for the Private Philanthropic Organization

*Jayme S. Lemke*¹

Abstract: Many donors and charitable organizations view philanthropy as more than an act of consumption. They consider themselves to be providing a valuable public good, or at least one they wish to see produced in excess of the quantity currently provided by the market. In this paper I adopt a means-ends approach in which the stated end of a network of philanthropic organizations is taken as given. I then employ the political economy of state-led humanitarian action developed by Christopher Coyne in *Doing Bad by Doing Good* in service of understanding the obstacles faced by the private philanthropic organization. After briefly discussing the critical differences between state-led humanitarian action and private philanthropy, I propose three lessons for the private philanthropic organization. First, philanthropy should be viewed without romance. Second, there is no formula for philanthropic success. Third, philanthropic redundancies need not be wasteful.

Keywords: Philanthropy, charity, public goods, polycentricity

Introduction

In *Doing Bad by Doing Good*, Chris Coyne raises a number of important challenges to the way humanitarians and economists alike think about charitably intentioned action. The greatest of these is his assertion that practitioners and scholars should cease to ask what *should* be done to aid those less fortunate in an ideal world and instead ask what *can* be done for the poor, hungry, and besieged in this world as it actually exists (Coyne 2013: 12)

Coyne's response to his own challenge is to bring to bear two analytically distinct but empirically inseparable sets of considerations: knowledge problems and incentive problems. Knowledge problems arise because humanitarian agencies operate in a complex world with incomplete information about the consequences of their actions. Consequently they have no way of calculating the best course of action, or even of knowing if their existence is beneficial or harmful. Incentive problems arise because decision makers, such as bureaucrats and humanitarian aid workers, face motivations other than the welfare of those they seek to help. These range from the commonplace distractions and misalignments present in all principal-agent relationships to the unique malignancies found in the darker corners of the aid business.

"The man of the humanitarian system" is a compelling archetype who suffers from ignorance of both. This unfortunate soul "holds that human suffering can be removed or prevented, that human welfare can be improved as desired, provided that the right people are in charge... that improving the human condition is a purely technological problem akin to sending a man to the moon" (Coyne 2013: 16). Through careful study of many variations on the man of the humanitarian system, real and hypothetical, Coyne develops a powerful lens through which to evaluate state-led humanitarian action.

In this paper, I borrow that lens to discuss the private philanthropic organization. Many donors and charitable organizations view philanthropy as more than an act of consumption. They consider themselves to be providing a valuable public good, or at least one they wish to see produced in excess of the quantity currently provided by the market. In this paper I adopt a means-ends approach in which the stated end of a network of philanthropic organizations, i.e. its philanthropic mission, is taken as given. I then employ the political economy of humanitarian action as developed by Christopher Coyne in *Doing Bad by Doing Good* in order to better understand the unique obstacles faced by the private philanthropic organization.

In section two of this paper, I briefly discuss the differences between state-led humanitarian action and private philanthropy. In the third section of this paper, I draw on Coyne (2013) and the logic of public goods provision within a polycentric order to propose three lessons for the private

philanthropic organization. First, philanthropy should be viewed without romance. The same axioms of self-interest that apply to market and political behavior also apply to private acts of philanthropy. Second, there is no formula for philanthropic success. Private charities are still nonmarket organizations operating within a heavily bureaucratic environment, and they will have no easier time planning grand social, economic, or political reforms than their public counterparts. Third, philanthropic redundancies need not be wasteful. On the contrary, duplication of efforts by many organizations with unique perspectives and skill sets can enhance the efficiency of a network of like-minded nonprofit organizations.

Private versus State-Led Humanitarian Action

In *Doing Bad by Doing Good*, Coyne focuses on *state-led* humanitarian action, coming to the general conclusion—as the title might suggest—that it can often do more harm than good. He defines state-led actions as those where “a government or group of governments plays a leading role as the agenda-setter in designing, implementing, funding, or overseeing the humanitarian effort” (Coyne 2013: 19). One explanation he offers for this choice of focus is that state involvement in humanitarian action has increased to the point where few humanitarian endeavors are free from government intervention.

There is no doubt that empirically disentangling private from public philanthropy would be a mighty feat.² In the United States of the 19th century it was not uncommon for health care, education, and other artistic and cultural endeavors to be managed by for-profit corporations, but by the turn of the century many of these functions began to be assumed by the non-profit sector (Hall 2006). Regulation was a key motivator of this shift in operating structure. The Tariff Act of 1894 was the first to explicitly mention that particular organizations were not required to pay taxes, and the tax-exempt status of qualifying nonprofits was formalized in the income tax code of 1917 (Arnsberger, et al. 2008: 106). Ever since, most philanthropic organizations have registered as tax-exempt nonprofits and as such have been subject to regulation by the IRS.

It is even difficult to disentangle which philanthropic projects should be considered privately directed and which should be considered state-led. Coyne cites a number of studies finding that the government has dramatically increased the extent to which it directly funds nonprofit organizations (Coyne 2013: 49-50). Public giving—government funding of nonprofit organizations—was estimated at \$483 billion in 2011. Private donations, including gifts by individuals, foundations, and corporations, totaled \$298 billion in the same year (Blackwood, Roeger, and Pettijohn 2012: 1, 3). These figures imply that the

average nonprofit receives \$1.62 from the government for every privately donated dollar, and this ratio likely underestimates the extent of public influence given that many private donations go to public charities. Further, private foundations are eligible to apply for and receive public funds. Braving this muddle to isolate the public from the private dollar hardly seems worthwhile.

Further, even if the private projects could be isolated from the state-led, both would still be managed by bureaucratic organizations operating without profit and loss in a generally non-priced environment. Coyne (2013: 61) asks, “Do humanitarians possess the ability to coordinate the often disparate plans and goals of many people (tens of thousands, hundreds of thousands, or even millions) to achieve the goal of promoting economic progress?” Throughout the book Coyne makes a compelling argument that the answer is no—coordination on such a scale is not possible in non-market contexts and cannot lead to genuine institutional change. The core of this argument would seem to apply equally well to private philanthropy and state-led humanitarian action, as I will discuss further in the subsequent section. However, there are some important distinctions between privately directed and state-led humanitarian action that should be mentioned first.

The primary difference between privately directed and state-led charities is that private charity is a consumption good for the donor. Individuals who donate to charitable causes without subsidization or other coercive motivation have done so because the benefits to them—emotional, psychic, or otherwise—outweigh the financial costs. The humanitarian act may be less than fully efficient or may even generate negative externalities, but at least this one aspect of the transaction is guaranteed to be welfare enhancing. The directors of state-led humanitarian action, on the other hand, are incurring costs on the behalf of others. When a public charity receives government funds, those funds are collected through taxation. The potential alternative uses of those funds are unknown, and consequently cost-benefit calculation is not possible.

Second, there is a difference in the scope and scale of state-led versus private activity. The difference in scale is somewhat obvious. Publicly directed charities dominate private efforts by any kind of financial accounting, as discussed above. In terms of numbers of organizations, the National Center for Charitable Statistics reports that public charities outnumber private foundations 10:1. More important than scale, however, is the difference in scope. Governments possess a coercive power that the private sector lacks. This is most obviously present in the use of the military as an instrument of humanitarian action. For example, the 2011 air strikes in Libya were humanitarian actions intended to improve the quality of life of Libyan citizens by removing Muammar Gaddafi from power (Coyne 2013: 143-145). A

privately led humanitarian action would not have been permitted to exercise violence in such a capacity. Whether this limitation is for better or worse depends on the expected probability assigned to the ultimate success of the intervention.

Lessons from *Doing Bad By Doing Good* for the Private Philanthropist

At its core the economic analysis of philanthropy is straightforward. A donor views the world and sees a problem he wishes to remedy. Perhaps this problem is an individual experiencing hunger, exposure, or illness, or living in a conflict-prone area. Perhaps it is a person who has had difficulty finding a job for lack of education or credentials. The problem the donor seeks to remedy could also be something less pleasant to the liberal ear, such as people reading the wrong books or believing in the wrong gods. The content of the problem actually does not matter. So long as the donated money, pamphlet, or box of canned goods is accepted voluntarily, human welfare is improved by the exchange. A gift freely given and received is a Pareto improvement.

However, many donors and charitable organizations view philanthropy as more than an act of consumption. They consider themselves to be providing a valuable public good. And some philanthropic organizations do focus on producing goods commonly considered to be public or quasi-public in nature, such as education, vaccination against communicable diseases, or the cessation of violence. However, many of the outputs of philanthropy are not public goods in the sense of being non-rivalrous and non-excludable—food and housing, for example.³

Whether or not the output of the charitable organization merits categorization as a public good, the founders, donors, and employees of the charity still ostensibly wish to produce a quantity greater than that which is currently provided by the market.⁴ More likely than not, this goal will overlap with the objectives of many other organizations. These organizations may differ in many ways—strategy, internal regulations, size, culture, degree of independence from other organizations, etc.—but no matter how many differences there are, their shared goal will bind them together in a common network.

The diverse individuals involved with this hodge-podge of organizations will have a common interest in identifying how best to achieve their shared goal, whatever that goal may be. In that spirit, the remainder of this section is conducted from a means-ends perspective. I take the philanthropic organization's stated goal of public good (or at least extra-market) provision as

given and as genuine. I then employ the political economy lens developed by Coyne (2013) for the evaluation of humanitarian action in order to better understand the obstacles faced by the private philanthropic organization.

I also draw upon the theory of public goods provision in a polycentric order. Networks of humanitarian organizations are an example of a polycentric order—many apparently independent organizations with different overall missions, strategies, and levels of authority with respect to other organizations that interact within a framework of shared rules. In this case those shared rules include not only the laws that govern nonprofit organizations but also a commitment to a common cause.

View philanthropy without romance. James M. Buchanan used the phrase “politics without romance” to describe the analytical tenets of public choice economics. He argued that politicians are no more wise or beneficent than other men, and that analyzing their behavior accordingly will advance our understanding of political institutions (Buchanan 1979). This is equally true for actors in the philanthropic sector.

Philanthropic organizations produce outside the realm of economic calculation. This is a point Coyne emphasizes at several points in his discussion of humanitarian aid (see for example Coyne 2013: 66-70). Because they operate in a non-priced environment, decision makers in philanthropic contexts are not guided by profit and loss. An entrepreneur in the market must transform the resources at her command into a configuration that makes them more valuable to others than they were before. Otherwise, engaging in production will be costly rather than profitable, and either she must decide on her own to leave scarce resources in the hands of a more capable individual or the market will decide for her by putting her out of business. In this way the market disciplines the entrepreneur.

The difference between an entrepreneur in the for-profit and nonprofit sectors is who they are seeking to serve. A nonprofit organization may consider their customer to be the individual they are seeking to aid or the cause they are aiming to advance, but more often than not the organization will never receive any direct feedback about their contribution to that end goal. Further, payment for goods produced or services rendered usually comes in the form of donations from third parties. The small set of high contribution donors that provide the bulk of the organization’s funding may very well provide the only feedback a nonprofit ever receives. To the extent that Tullock’s (1966) observation that most donors are indifferent between actual philanthropy and a successful façade of philanthropy is true, there is no reason to expect that this feedback will guide the organization in the direction of achieving its intended aims.

Further, private philanthropic organizations are subject to the problems of bureaucratic organization. Alone that statement means little, since all organization that takes place by conversation and committee rather than through market exchange is by definition bureaucratic. As such all organizations are in some sense bureaucracies. The difficulty faced by philanthropic organizations goes a step further though, because like state-led humanitarian organizations, the layers of bureaucracy are many and ultimate (Coyne 2013: 90-142). Unlike in a market context where the consumer serves as a final arbiter that constrains the bureaucratic system by forcing the most excessive out of business, the value of a nonprofit organization is judged only by other bureaucracies. Consequently, the employees of nonprofits receive paychecks not because they have contributed to an organization that has passed some kind of market test, but because they have convinced a donor that what they do is worthwhile.

There is no formula for philanthropic success. The mentality that social change can be orchestrated is at the core of American philanthropy. Andrew Carnegie, one of the founders of modern philanthropy, proposed a graduated inheritance tax that would encourage people to direct their giving while alive rather than donating posthumously, suggesting that:

Under its sway we shall have an ideal state, in which the surplus wealth of the few will become, in the best sense the property of the many, because administered for the common good, and this wealth, passing through the hands of the few, can be made a much more potent force for the elevation of our race than if it had been distributed in small sums to the people themselves. Even the poorest can be made to see this, and to agree that great sums gathered by some of their fellow-citizens and spent for public purposes, from which the masses reap the principal benefit, are more valuable to them than if scattered among them through the course of many years in trifling amounts (Carnegie 1889: 660).

Undergirding this statement is the belief that being wealthy and successful can enable you to transcend the unpredictability associated with acting in a complex system under limited information.

However, to borrow a phrase from Coyne, “The Planner’s Problem is Ubiquitous” (Coyne 2013: 85). This is true whether the planner is acting under the auspices of a government or not. To illustrate the systematic nature of the difficulties associated with attempting to serve the needs of strangers in the absence of market coordination, consider the case of in-kind donations. Aid workers have long been dealing with the problem of private individuals sending ill-timed or useless donations-in-kind to regions in crisis. Juanita Rilling, an aid

worker in Honduras at the time of a devastating hurricane, recalls having to turn away a cargo plane full of medical supplies because planes filled with useless consumer goods donated by well-meaning but misinformed people had overcrowded the tarmac (Fessler 2013).⁵ The fact that hundreds of thousands of individuals persist in committing this error over and over again demonstrates that even decentralized philanthropic activity can be impeded by the incomplete knowledge of donors.

Coyne notes when discussing the planner's problem that philanthropic organizations often believe they can mimic economic calculation through a process of experimentation (Coyne 2013: 71-89). This is evidenced by the increased popularity of randomized controlled trials and the trend towards transparency and measurement of the outcomes of particular projects. Central to both of these strategies is the belief that social change can be identified by watching a particular number—classroom hours, incidences of malaria, bowls of soup served—rise or fall. However, it is never possible to guarantee a connection between an output number and the attainment of an intangible goal. Even if there was a single output or a small set of outputs that, if altered, would make a dramatic difference for good, the formula could not be known in advance or even proven after the fact because of the sheer complexity of the context within which action takes place.

Duplication need not be wasteful. Ostrom, Tiebout, and Warren (1961) advanced the hypothesis that consolidating a network of overlapping local public goods providers would not necessarily make it more efficient. What appears to be needless duplication can be optimal if agencies are in reality providing “similar but differentiated services which impinge upon diverse communities of interest” (Ostrom 1972: 1). In the context of philanthropic organizations, this can be interpreted as proposing that it need not be wasteful for multiple nonprofit organizations with the same or similar missions to function simultaneously so long as they are sufficiently autonomous to be able to differentiate their services.

Duplication can occur whenever multiple organizations are permitted to function autonomously, as within a polycentric order. Sometimes this duplication is costly. Coyne (2013: 128) illustrates this point with an example from Tanzania, where 1,300 different humanitarian projects active from 2000 to 2002 involved 2,000 donor meetings and nearly 20,000 donor reports over the two year period. In theory, greater centralization could have lowered administrative burdens on the part of both recipients and donors by eliminating duplication of reporting and monitoring functions. Further, Coyne (2013: 118) notes that a decentralized network of state-led humanitarian aid organizations can face “issues of continuity of vision, mission fulfillment, and effective communication across decentralized bureaus, resulting in problems of

fragmentation.” This suggests that there are, theoretically, benefits to consolidation of philanthropic activities.

However, there are also costs associated with consolidation (Coyne 2013: 128-131). Smaller, more specialized organizations will face fewer information and incentive problems than large bureaucracies due to shorter chains of command. In theory, this means that organizational leadership will be more directly accountable to donors and in a better position to ensure that the donor’s wishes are accurately communicated to staff. Furthermore, smaller agencies allow their employees greater flexibility and tend to be less regulated, meaning they often have lower administrative costs. The net effect of decentralization is, however, indeterminate. Although decentralization may help preserve what is known in nonprofit circles as donor intent, the donor is still subject to information and incentive problems of his own. The donors may get exactly what they want, but there is still no guarantee that what they want is an efficient use of funds.

In sum although a network of philanthropic organizations all working in service of the same mission may seem wasteful, duplication and decentralization can sometimes serve useful functions. The implication is that attempts to coordinate large networks of philanthropic organizations to take advantage of economies of scale should be undertaken with caution.

Conclusion

In the preface to *Doing Bad by Doing Good*, Coyne warns that those looking for “a ‘how to’ guide for carrying out humanitarian action” might want to look elsewhere (Coyne 2013: xiii). Rather, it is precisely those individuals who are in search of easy answers and formulaic solutions who stand to benefit most from his sobering words. This includes not only those in the international humanitarian sector but also those involved domestically in private philanthropy.

This paper discussed only three of many implications that Coyne (2013) has for private philanthropic organizations. There is also a lesson to be taken from the fact that after full consideration of the constraints posed by dispersed information, systems complexity, special interests, and other political economy considerations, Coyne comes to the conclusion that the removal of barriers to innovation and exchange is the best way to improve standards of living in impoverished countries. The private philanthropist would do well to consider the possibility that they may be in an analogous situation, and that the most direct reform might not be the most obvious.

Notes

¹ Political Theory Project, Brown University. Providence, RI 02912. Jayme.Lemke@Brown.edu.

² See Coyne and Hall (2013) for a discussion of private philanthropy in the absence of the state.

³ Shughart (2011) discusses the non- public nature of many supposed public goods associated with disaster relief.

⁴ See Tullock (1966) for reasons to suspect this may not be the case.

⁵ The Center for International Disaster Information (CIDI) was created in 1988 in response to this problem (USAID 2012).

References

Arnsberger, Paul, Melissa Ludlum, Margaret Riley, and Mark Stanton. 2008. "A History of the Tax-

Exempt Sector: An SOI Perspective." *Statistics of Income Bulletin* 27(3): 105-135.

Blackwood, Amy S., Katie L. Roeger, and Sarah L. Pettijohn. 2012. "The Nonprofit Sector in Brief:

Public Charities, Volunteering, and Giving." Urban Institute Press. Available online at

<http://www.urban.org/publications/412674.html>.

Buchanan, James M. 1979. "Politics Without Romance: A Sketch of Positive Public Choice Theory

and Its Normative Implications." In *The Collected Works of James Buchanan, Volume 1: The*

Logical Foundations of Constitutional Liberty. Indianapolis, IN: Liberty Fund, 45-59.

Carnegie, Andrew. 1889. "Wealth." *The North American Review* 148 (391): 653-664.

Coyne, Christopher J. 2013. *Doing Bad by Doing Good*. Stanford, CA: Stanford University Press.

Coyne, Christopher J. and Abigail R. Hall. 2013. "Anarchy, Philanthropy, and the Provision of

Public Goods in a Free Society." Available at SSRN: <http://ssrn.com/abstract=2296021>

Fessler, Pam. "Thanks, But No Thanks: When Post-Disaster Donations Overwhelm." *NPR Around*

the Nation, January 09, 2013. <http://www.npr.org/2013/01/09/168946170/thanks-but-no->

[thinks-when-post-disaster-donations-overwhelm](http://www.npr.org/2013/01/09/168946170/thanks-but-no-thanks-when-post-disaster-donations-overwhelm)

-
- Hall, Peter Dobkin. 2006. "A Historical Overview of Philanthropy, Voluntary Associations, and Nonprofit Organizations in the United States, 1600-2000." Ed. Walter Powell and Richard Steinberg. *The Nonprofit Sector: A Research Handbook*, 2nd Ed. New Haven, CT: Yale University Press, 32-65.
- Ostrom, Vincent. 1972. "Polycentricity." Prepared for delivery at the 1972 Annual Meeting of the American Political Science Association, Retrieved from the Digital Library of the Commons, <http://dlc.dlib.indiana.edu/dlc/>.
- Ostrom, V., C.M. Tiebout and R. Warren. 1961. "The Organization of Government in Metropolitan Areas: A Theoretical Inquiry," *American Political Science Review* 55: 831-842.
- Shughart, W.F. 2011. "Disaster Relief as Bad Public Policy," *The Independent Review* 15(4): 519-539.
- Tullock, Gordon. 1966. "Information without Profit." *Papers on Non-Market Decision Making* 1: 141-159.
- "USAID Center for International Disaster Information Fact Sheet." 2012. Available online at www.cidi.org/wp-content/uploads/resources/toolkit/CIDI-Fact-Sheet-2012.docx.