CONVERSATION 10

Rethinking Philanthropy and Business

David Ellerman

COMMENTS

Explaining the Scale of the Philanthropic Sector

David L. Prychitko

Out of Philanthropy and Into Social Enterprise? Probably Not

Roger A. Lohmann

Conversations on Philanthropy Volume VI:
Identity, Interests, & Philanthropic Commerce

CONTRIBUTORS

DAVID ELLERMAN works in the fields of economics and political economy, social theory and philosophy, and in mathematics. His undergraduate degree was in philosophy at M.I.T. ('65) and he has Masters degrees in Philosophy of Science ('67) and in Economics ('68), and a doctorate in Mathematics ('71) all from Boston University. He has been in and out of teaching in economics, mathematics, accounting, computer science, and operations research departments in various universities (1970-90), founded and managed a consulting firm in East Europe (1990-2), and worked in the World Bank from 1992-2003 where he was an economic advisor to the Chief Economist (Joseph Stiglitz and Nicholas Stern). Now he is a visiting scholar at the University of California in Riverside. He has published numerous articles in various fields (see Curriculum Vitae) and five books.

ROGER A. LOHMANN is Professor of Social Work and Benedum Distinguished Scholar at West Virginia University. He was editor of *Nonprofit Management and Leadership* from 2000-2008. He is the author of numerous journal articles and author of three books: *Breaking Even: Financial Management in Human Services* and *The Commons: New Perspectives on Nonprofit Organization*, *Voluntary Action and Philanthropy and Social Administration* (co-authored with Nancy Lohmann). He is also co-editor (with Nancy Lohmann) of *Rural Social Work Practice* and a forthcoming volume on public deliberation and sustained dialogue (co-edited with Jon Van Til). He was a pioneer of online intellectual discussion lists, founding ARNOVA-L (in 1990) and more than 30 other lists. He is the founder and chair of the board of the Nova Institute at West Virginia University and is currently engaged in developing an online graduate certificate program in nonprofit management and third sector studies and an update on his previous theoretical work on the commons theory of associations.

DAVID L. PRYCHITKO is a professor of economics at Northern Michigan University. He has published widely in economics, and is the co-author (with Paul Heyne and Peter Boettke) of *The Economic Way of Thinking*, an introductory textbook published by Prentice Hall.

RETHINKING PHILANTHROPY AND BUSINESS

David Ellerman

Introduction

Can philanthropy share the success of the business sector as a spontaneous order? Instead of directly addressing this question, I will analyze some of the presuppositions. Firstly, I argue that two logics run through human affairs: the logic of exit and the logic of commitment and voice. Secondly, the economy or business sector is composed of markets, natural sites for the logic of exit, and organizations which are natural sites for the logic of commitment. Economics, neoclassical or Austrian, focuses on exit-based markets, the main examples of spontaneous orders, while I argue along with Herbert Simon that organizations have an equal if not more important role in modern economies. How might people address their community's social and environmental problems to the extent that government is ineffective?

While people may have some associational life after-hours and on weekends, their principal involvement beyond the family in joint human activities is in their job in the organizations that have an increasingly important role in the economy. But the structure of most companies of any size—namely, securitized absentee ownership on the stock market—institutionalizes irresponsibility by disconnecting the far-flung shareholders from the social and environmental impact of their "corporate governance." Or viewed the other way around, that structure prevents the local managers and staff in widely held companies from using their principal outside-the-family organizational involvement to address local problems. That in turn increases the need for a stronger third sector, the philanthropic or non-profit sector, to address those problems. Then if we come back around to our original question, we see the answer may lie not in making philanthropy more like business (in some sense) but in finding forms of business that allow people to be more socially responsible directly through their principal associational involvement.

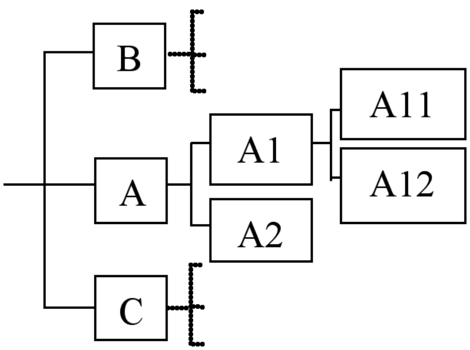
Ellerman, David. 2009. Rethinking Philanthropy and Business. *Conversations on Philanthropy VI:* 79-96.
ISSN 1552-9592

How might philanthropy (the nonprofit sector) be organized to share more of the vitality and efficiency of the market economy (the business sector) as a spontaneous order? Instead of trying to answer this question directly, I will analyze some of its presuppositions. That analysis, in turn, will suggest a different approach to the broader problem of harnessing the power of the business economy to address the social and environmental problems that are usually the target of philanthropic efforts.

The Two Logics: The Logic of Exit and the Logic of Commitment

Throughout human affairs and even in mathematics, science, and engineering, there are two logics that are, in a certain sense, "dual" to one another (Ellerman 2005). Albert Hirschman investigates them as the logic of exit and the logic of commitment, loyalty, and voice. The expressions "logic of exit" and "logic of commitment" are used by Tadao Kagono and Takao Kobayashi (1994) who develop the two logics of organizational design by contrasting the American-style firm and the Japanese-style firm. Jane Jacobs (1992) develops a variation of the theme with the contrast between the exit-oriented commercial syndrome and the commitment-oriented guardian syndrome.

The logic of exit and the logic of commitment can be illustrated rather abstractly by considering the ubiquitous human activity of searching over some tree of possibilities for the "answer" to some question or the "solution" to some problem.



Search tree for some "answer" or "solution"

Suppose that one starts the search at A but does not find the answer there. There are two contrasting "logics" or strategies of search, which illustrate the logics of exit or commitment.

1. The logic of exit would recommend breadth-first search: Since A is not the solution, exit that branch of the search tree altogether and try B or C. Only if none of the initial branches contained the answer would one proceed along any of the branches to a higher branch such as A1 or A2.
2. The logic of commitment would recommend depth-first search: Although A is not the solution, stay committed to that branch (for whatever reason) and continue to look for the answer in a higher branch such as A1 or A2. Only after exhausting the A branches would the logic of commitment recommend exiting the A branches to try B or C.

These two logics run throughout human affairs. We might consider one logic to be appropriate to one sphere and the other appropriate to another sphere without giving the matter a second thought.

For instance, for a consumer in a competitive marketplace, the logic of exit would be the natural assumption. If a company's product was found to be continually deficient, then one could follow the logic of commitment to write letters to the company or otherwise try to exercise what Hirschman called voice, to get the company to improve its product. But most consumers would follow the logic of exit and switch to a competitor's product. The logic of exit fits well into the marketplace.

There are other spheres of human affairs, however, such as the family, where the logic of commitment would be the presumed strategy. To take an extreme example, if a child's behavior is continually unsatisfactory, one would presumably not apply the logic of exit by dropping the child off at a foundling hospital or adoption agency and trying another child by birth or adoption. The presumption would be commitment to that "branch of the search tree," and one would explore further branches to improve the situation. Other examples suggested by Jane Jacobs' "guardian syndrome" (1992) are the police officers, military personnel, and public officials who are supposed to operate on the basis of the logic of commitment and loyalty rather than the logic of exit (for example, by selling their services to the highest bidder).

In many other situations there may be more of a real choice between the two logics. For instance, a person in an undeveloped country who is contemplating migration faces the basic choice: commit to making one's home better or exit to find a better home. In general, the choice is not simply "love it or leave it" but whether to change a loved place for the better or leave it to find a better place.

What determines which logic is best in a given situation? One key consideration seems to be the extent to which the person or persons can change a situation for the better. Does a voice have a decent chance of being effective, so that a commitment to improving the given situation will pay off, or is the unsatisfactory situation essentially "hopeless" in the sense that commitment and voice have little hope of success and thus exit is probably the best option? The search tree analogy may be misleading in the sense of presenting the branches as if they were already there and as if search were a rather passive activity of finding a preexisting "solution." A better understanding would emphasize that the higher branches in the "search tree" may have yet to be constructed. The key consideration, then, is this: Can better "branches" be constructed or changed through commitment and voice, or is that hopeless, leaving exit as the best option? Hirschman referred to the change-the-characteristics strategy as *voice*: "Voice is here defined as any attempt at all to change, rather than to escape from, an objectionable state of affairs" (1970, 30).

Economics, or the Logic of Exit as "the" Logic

Both neoclassical and Austrian economics focus almost exclusively on the logic of exit. The market operates largely on the basis of the logic of exit, and economics developed first as the theory of markets and market behavior, so economics tends to see the world through an exit-oriented lens. Hirschman wrote, "The economist tends naturally to think that his mechanism [exit] is far more efficient and is in fact the only one to be taken seriously" (1970, 16).

For instance, under the exit-oriented logic, all labor questions are "labor market" questions, while under the alternative commitment-oriented logic (as in a Japanese-style firm), a labor question is a "human relations" or "human resources" question. An amusing example of this is that the advice of the World Bank to developing countries about labor is in the "labor markets" topic area [see www.worldbank.org/sp]; there is no "human resources" topic area. But for its own staff within the World Bank, there is a Human Resources Vice President but no "Labor Market Vice President." Thus the World Bank looks outward through the exit-oriented lens (provided by the discipline of economics), and looks inward through a commitment-oriented lens.

Now we are in a better position to unpack one of the presuppositions in the original question about philanthropy partaking of the vitality and efficiency of the market economy as a spontaneous order. The basic presumption is that the principal institution in the successful industrialized economies is the market, and thus if the philanthropic sector is to share this success it needs to be reconceptualized in some sense as a spontaneous or emergent order like the marketplace. But if in fact the market is only a part, say, "half" the story in the advanced industrial economies, and if the logic of commitment naturally applies to the other "half," then the questions about philanthropy might be seen in quite a different light.

Modern Economy = *Markets* + **Organizations**

Of all the Nobel Prize winners in economics, Herbert Simon was perhaps the most interdisciplinary and the least committed to some of the conventional wisdom of the discipline. Late in his career he published a seminal paper, "Organizations and Markets" (1991), emphasizing the importance of organizations in understanding a modern economy and stressing the incompleteness of an economics that views the market and its logic as the center of a modern economy.

Simon imagines a visitor approaching Earth from Mars and viewing Earth through a special telescope that reveals different social structures with different colors. Organizations are colored green, and markets are red:

> No matter whether our visitor approached the United States or the Soviet Union, urban China or the European Community, the greater part of the space below it would be within the green areas, for almost all of the inhabitants would be employees, hence inside the firm boundaries. Organizations would be the dominant feature of the landscape. A message sent back home, describing the scene, would speak of "large green areas interconnected by red lines." It would not likely speak of "a network of red lines connecting green spots" (1991, 27).

When the visitor learns that the green masses are organizations and the red lines are market transactions, it might be surprised to find the economy described in both neoclassical and Austrian economics as a "market" economy: "The economies of modern industrialized society can more appropriately be labeled organizational economies than market economies. Thus, even market-driven capitalist economies need a theory of organizations as much as they need a theory of markets" (1991, 42).

The mischaracterization of a modern industrial economy as a market economy is not one of the issues that divides neoclassical and Austrian economics. If anything, Austrian economics pays even less attention to organizations than neoclassical theory (with the latter's "new institutional economics"). For instance, in Friedrich Hayek's juxtaposition (1973; 1989) of the unplanned spontaneous order of markets ("cosmos") to a planned social order ("taxis"), he takes government, and particularly socialist government, as the canonical examples of planned orders. Hayek, of course, recognizes the existence of organizations as examples of taxis or planned orders in the middle of the spontaneous order of the market (1973, 46-54; 1989, 37). But organizations are mentioned as an aside (in Simon's terms, only "green spots" rather than "large green areas") and cryptically as parts of an "even more comprehensive spontaneous order" (1989, 37). There is no recognition of their role as the principal actors in a modern industrial economy and little recognition that much of the spontaneous order theory about the market does not apply to organizations (taxis).

If market commerce is at best only "half" the story in the private-sector economy, then one might find a richer set of motives associated with the logic of commitment potentially at work in the private sector within organizations—which means one does not need to look to the philanthropic sector to find alternatives to the narrow self-interest usually taken as the model of market exchange.

Given the ubiquity of organizations in a modern economy, a basic problem arises because, as Simon writes,

> most producers are employees of firms, not owners. Viewed from the vantage point of classical theory, they have no reason to maximize the profits of firms, except to the extent that they can be controlled by owners. Moreover, profit-making firms, nonprofit organizations, and bureaucratic organizations all have exactly the same problem of inducing their employees to work toward organizational goals. There is no reason, a priori, why it should be easier (or harder) to produce this motivation in organizations aimed at maximizing profits than in organizations with different goals (1991, 28).

Insofar as conventional economics tries at all to explain organizational behavior—for example, in the "new institutional economics"—it falls back on the exit-oriented template of the market transaction but with the addition of "transactions costs" (Williamson 1985) and "asymmetric information" (Ross 1973; Stiglitz 1974). As Simon notes:

> A fundamental feature of the new institutional economics is that it retains the centrality of markets and exchanges. All phenomena are to be explained translating them into (or deriving them from) market transactions based upon negotiated contracts, for example, in which employers become

"principals" and employees become "agents" (1991, 26-7).

What are the motivations involved in organizational behavior that fall outside the market commerce paradigm? In many cases, employees (particularly those with high skills and professional education) are intrinsically motivated to do the work. They need the salary to live, but they are committed to the work itself, so their organizational involvement is not well-described simply as a market exchange of labor for salary. Some modern management theorists such as Douglas McGregor (1960) have probed the difference it makes if employees have or potentially have some intrinsic motivation on the job (Theory Y) instead of only the usual extrinsic pecuniary motivation (Theory X).

There is also the phenomenon of "identification," where, far from just being a seller of labor in a market transaction, the employee identifies with the organization that is the "employer" or with the organization's product:

> A department will be less likely to skimp on quality to cut costs if its members identify with the final product. In particular, identification becomes an important means for removing or reducing those inefficiencies that are labeled by the terms "moral hazard" and "opportunism" (Simon 1991, 41).

Intrinsic motivation and identification are two examples of the commitment-oriented factors that are important in a modern economy but which are either ignored or inadequately treated by an economics that sees through the exit-oriented lens of the marketplace:

> The attempts of the new institutional economics to explain organizational behavior solely in terms of agency, asymmetric information, transaction costs, opportunism, and other concepts drawn from neo-classical economics ignore key organizational mechanisms like authority, identification, and coordination, and hence are seriously incomplete (1991, 42).

Intrinsic motivation and identification are also not well-described in juxtapositions of self-interest versus altruism, or market transactions versus gift-giving (see, for example, Godbout 1998). Like an onion skin, the "self" has concentric layers of stronger and weaker identification that determine one's identity. Action in the interest of others in a family or a larger group with which one identifies need not be seen as altruistic in the sense of selfless action but could be seen as self-interested action in support of an expanded sense of self. In addition, intrinsic motivation is derived from the nature of the action, not from monetary rewards or any other *quid pro quo* given in exchange for the action. An understanding of how organizations work requires going beyond extrinsic, pecuniary self-interest as the paradigm of motivation, and yet the consideration of identification and intrinsic motivation are not well understood as "altruism" in contrast to self-interest.

Rethinking Philanthropy

Now we are in a better position to rethink our original question about philanthropy. The need for a philanthropic sector arises from the many social and environmental problems left unresolved by the public and private sectors, i.e., the government and the economy. While government-led social renewal is always possible, particularly in a vigorous democracy, our focus is on somehow extending the success of the economy to the tasks of philanthropy. To see how that might happen, we need to understand the principal factors in a modern economy.

We have argued that modern economies are composed of two principal parts: markets and organizations. Markets provide a natural setting for the logic of exit, and organizations may be seen as providing a natural setting for the logic of commitment. These are the two logics that might be applied, with the unsatisfactory situation being a community with accumulating social and environmental problems that a philanthropic sector might be called upon to face. The community could be a small town, a city, a regional state, or a country. Philanthropy here refers to one of the ways a community might try to resolve the problems left unresolved by its governmental and economic actors—not to charity or "do-gooderism" wherein the better-off think they can resolve the problems of those in very different circumstances.

If the causes of the community's problems are seen as unchangeable by means of the public or private tools at hand, then many people, particularly the most energetic and ambitious, will adopt the logic of exit. Since there seems to be little chance of making the community better, they will exit to find a better community. If communities operated like companies in a marketplace, exit could promote renewal or, failing that, lead to the complete demise of the community and the dispersal of its assets. But communities often do not operate like companies, particularly regarding the bankruptcy option. Instead of triggering a process of renewal, the exit of the most energetic and ambitious citizens makes renewal even more unlikely. The result of the logic of exit may be a vicious circle of ghettoization leading to a semi-permanent failed community (or failed state in the case of entire countries). That, in turn, leads to the call for more "philanthropic" intervention in the sense of charities alleviating the symptoms of community failure. On an international scale, the logic of exit leads to the flight of financial and human capital from underdeveloped countries which, in turn, calls for a strengthened response from international aid agencies to assist the ghettoized failing states.

It was the failure of the logic of exit in the case of Nigeria's railroads in the 1960s that prompted Hirschman to make his analysis of exit versus voice. The conventional economists' logic of exit predicted that the continual unsatisfactory performance of the Nigerian railroads could be addressed by promoting the trucking industry to provide competition, to provide an exit for some freight customers from the railroads to trucks. Indeed, the most discerning and time-sensitive customers did switch to trucking, but this did not lead to any renewal in the state-run railroads. There was then even less voice to prompt changes, so the railroad's performance got worse rather than better.

The key point is that the social choice of exit versus commitment depends in large part on the extent to which people are empowered in their own community to address their own social and environmental problems. Political participation and action is always a possibility, but the original problems may have arisen, in part, from those channels being blocked and ineffective. In addition, political action to unblock those channels is always difficult for the simple reason that most people have to devote their time to making a living and to their private family life. Their principal activity outside of family life is their work. That is what people typically "do all day long." Moreover, the workplace is where most people learn to work together to take effective collective actions to do what they couldn't do by themselves individually.

Economic Organizations: "Footloose" or Embedded in Communities?

The question of people being empowered in their community to address their local social problems raises the question of their role in the economic organizations of their community, the organizations that form "half" of a market economy and are the natural loci for the logic of commitment. That is where people spend their productive hours and where they have the skills for effective joint activities (in contrast, say, to individuals volunteering after hours for unskilled work in a charity). Why can't these economic modalities address the social and environmental problems that face the community?

The argument has thus taken a perhaps unexpected turn to look at the form of economic organizations. The line of argument began by looking at where people apply the logic of exit or the logic of commitment. In spite of advertisers' best efforts, most people do not "identify" with the products they consume, and thus they are willing to apply the logic of exit in the consumer marketplace. In contrast, almost all people apply the logic of commitment to their own family without a second thought. In spite of economists' best efforts to explain organizational behavior by using the logic of exit, it would seem that the logic of commitment based on identification with the company and its products plays a key role in modern economic organizations. The logic of commitment would also seem to be the natural default for most people's relation to the community where they live.

But as social problems accumulate, that commitment may be called into question if there are no channels for social action to address them. It may be that the commitment to one's family can be honored only by exit from a deteriorating and seemingly unchangeable local community. Since most people's primary time commitment outside their family is to their job, the question of economic organization thus comes to the forefront.

Is a company embedded in a community in the sense that the community members who work in the company (as managers and staff, for example) can see it as an instrumentality for their commitment to help address local social and environmental problems? Or is a company simply a footloose asset with only a contingent connection to the community and an externally imposed "purpose" unrelated to local concerns? Clearly both types of companies could exist. For instance, a longstanding family-owned company would be embedded in a community in a way that helping to address local problems would seem a natural response in view of the family's commitment to the community. But an absentee-owned subsidiary of a distant company would have no such embedding or commitment and would likely see any such efforts as a misuse of corporate resources for some unauthorized goal. Any local commitment would be a potential immobility retarding the efficient allocation of corporate assets to their highest-valued use wherever that might be.

Which form of organization predominates? If the latter sort of company predominates, then the for-profit business sector would have little commitment to using its successful modes of organization to address accumulating social and environmental problems. This is not "its purpose" (as determined by footloose absentee owners with no local commitment). In that situation, there would be the essential need for a third sector, a nonprofit sector, that could try to address the unresolved problems. And then our question would arise of how the philanthropic sector might share more of the success of the "market economy." But as the argument has unfolded, we now see that there is another path. The problem may lie not in the philanthropic sector but in the way most economic organizations are structured, which blocks direct social action and thus strengthens the need for a philanthropic sector.

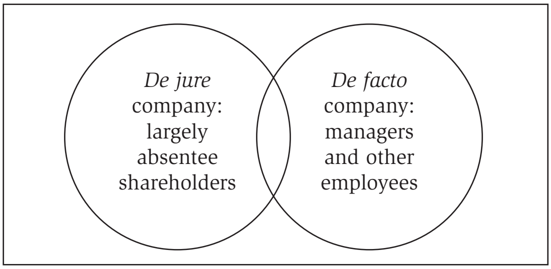
The American Model of the Widely Held Company

Since this line of argument leads to an understanding of the importance of the form of the economic companies, we will briefly review two stereotypical models: the American model of the widely held company as a footloose company unconnected to local communities, and the Japanese-style firm (or "J-firm" of Aoki 1988) as a model of the embedded company based on the logic of commitment.

If the exit logic fits markets and the commitment logic fits organizations, then what would an organization look like if it were based on the logic of exit? This brings us to the "model" of the widely held American corporation. To apply the exit logic, we must know who's in and who's out. Who are the members of the organization?

There are actually two "companies": the company as a legal entity and the company as a working group of human beings: "The human association which in fact produces and distributes wealth, the association of workmen, managers, technicians and directors, is not an association recognised by the law. The association which the law does recognise—the association of shareholders, creditors and directors—is incapable of production and is not expected by the law to perform these functions" (Percy 1944, 38, quoted in Goyder 1961, 57).

The legal entity, the legal or de jure company, has the shareholders as its members. But the members of the actual or de facto company are the managers and workers who actually carry out the company's business. In a small, closely held business, the de jure company and the de facto company are largely the same. But for the large, modern, publicly traded American corporation, there is very little overlap between the de jure company (shareholders) and the de facto company (employees including managers). Those who are actually inside the company (the staff) are from the legal viewpoint outside the firm and have only a contingent market relationship (employment) to the firm. Those who are legally inside the company (the legal members of the company) are the far-flung shareholders who typically have no business relationship with the company (not to mention its local community or environment) aside from the share of ownership, and who typically have well-diversified portfolios of shares.



The Two Companies in a Publicly Traded American Firm

The commitment-oriented logic of organizational design would be appropriate for a company, but the problem is that there are the two companies. The shareholders are seen as the insiders, principals, members, and owners of the (de jure) company. When things are not going well, the shareholders are legally empowered to change "their company" in accordance with the logic of commitment. And since the people who actually work in the company, the de facto company, are seen legally as having only a market relationship to the company (the employment relation), their role is legally modeled on an exit-based logic.

In the Anglo-American economies, starting from closely held firms (with little divergence between the de jure and de facto firms) the growth of the public market in equity shares has created these rather odd chimeras. And as the de jure firm ("ownership") diverged more and more from the actual firm, the legal theory broke down. The transaction costs for dissatisfied far-flung shareholders to organize and actually change things were very high. And the returns from organizing enough shareholders would be shared by all shareholders, so there was also a strong collective action problem. Thus the logic of voice and commitment did not work in practice in the American-style widely held company. Hence shareholders used the "Wall Street Rule": if you don't like the way things are going, exit by selling your shares.

Hence the people legally empowered to implement a commitment-based strategy (those who have the voice and vote to "change things") use an exit-based strategy (sell the shares). And the managers and workers who are de facto in a position to implement a commitment-oriented strategy of voice ("change things") are seen legally as being outsiders ("employees") on the other end of a market relationship with the company. They are not the principals or owners directly empowered by corporate law to change things, so in the eyes of the law their only option is to quit ("exit") if they are dissatisfied.

Any attempt of the workers, the members of the de facto firm, to formalize powers to directly "change things" is seen as infringing on the "management rights" exercised by the supposed agents of the far-flung shareholders who are the legal members of the company.

Of course, this bizarre structure does not actually work. Some insiders gladly grabbed the levers of actual control dropped by the shareholders. Those insiders are the top managers, and thus we arrive at what Adolf Berle and Gardner Means called the "separation of ownership and control" (1932, 89) and what is currently called the "corporate governance problem." The legal theory or "model" is shareholder capitalism; the underlying reality is managerial capitalism. Since there is no legal basis for the actual system of managerialism, the public relations machinery in the companies, in the business press, and in academia broadcasts the professed goal of "maximizing shareholder value" while the top managers reveal their actual goals in their salaries, bonuses, benefits, perquisites, (manipulated) stock options, and golden parachutes. The top managers have every interest in keeping the fantasy of "shareholder capitalism" alive as the cover story for the reality of managerial capitalism—much as the *nomenklatura* of the Communist Party had every interest in keeping the fantasy of "People's Democracy" alive.

From the motivational viewpoint, the bizarre model structure does not work *unless* those who are legally outsiders on the other end of the employment contract—getting only the economic reward of salary or wage—are to a significant degree committed to and identified with the company. Although this is almost entirely ignored by conventional, exit-oriented economics, Herbert Simon has emphasized the point: "Organizations would be far less effective systems than they actually are if such [economic] rewards were the only means, or even the principal means, of motivation available. In fact, observation of behavior in organizations reveals other powerful motivations that induce employees to accept organizational goals and authority as bases for their actions. . . . [The] most important of these mechanisms [is]: organizational identification" (1991, 34). Hence the members of the de facto company do in fact tend to identify with the company even though they are legally outside the company!

The large American firm is thus a rather odd and incoherent organization. Those who are legally inside the firm (shareholders) use the logic of exit as if they were outside, and those who are legally outside the firm (employees) often use the logic of commitment as if they were inside.

This mismatch between the model and reality leaves the analyst in a quandary. Should one analyze the rather mythical company model that lives in the law books and in the economics textbooks? That is the “American model” broadcast to the world by ivory tower academics who might think that American companies actually work that way. But since actual organizations need a healthy dose of commitment-oriented behavior to work well, the archetypical exit-oriented “American model” is a textbook model only. Actual large, widely held American companies use a version of the logic of commitment, but the top managers who assume and exercise the legal rights of the insiders (owners) often try to treat all the *other* employees as outsiders on an exit-based model (in the labor relations system, for example). Those other employees have the collective self-interest to address local social problems, but the top managers invoke the exit-based employee model for the de facto members of the firm in order to deny their voice. Hence the actual large, widely held American company ends up being something of a contested battleground between the two logics.

The Modern Japanese-Style Company

In their introduction to a book of essays by Japanese authors about the Japanese-style firm, Ronald Dore and Hugh Whittaker echo Herbert Simon at least as regards the Japanese case: “Most of the authors would agree that if you want to understand what goes on in Japanese boardrooms, you can throw most of the writings that go under the rubric ‘agency theory’ out of the window” (1994, 3).

In the postwar era the large Japanese firms have perhaps gone the farthest in developing the organizational logic of commitment and contrasting it with the logic of exit. For instance, to one trained to think in terms of the logic of exit, any immobilities, rigidities, or barriers to exit would just seem inefficient and irrational, but Japanese economists have developed the notion of useful barriers to exit, as in the practice of a captain being expected to go down with his ship:

> The way in which underpayment of wages in the early years of service and the acquisition of firm-specific skills create barriers to exit is obvious. These exit barriers perform several important functions for the firm as an organizational entity. The first is the incentive function whereby the interests of the firm and the interests of the individual are linked. Unable easily to exit, people can only protect their interests by working to ensure that the firm prospers. . . . The interlinking of interests means that when crisis looms, efforts are redoubled. The option of leaving the sinking ship is not freely available, either to the crew or the captain (Kagono and Kobayashi 1994, 94).

Barriers to exit can enhance identification and thus effort-efficiency or "X-efficiency" (Leibenstein 1984).

In a similar vein, John Maynard Keynes was much concerned with the adverse effects of the stock exchange on real investment and enterprise. He argued that significant investment in productive enterprise should be largely immobile and the management of an enterprise should have a long-term commitment and engage in the application of "intelligence to defeat the forces of time and ignorance of the future" (1936, 157). In short, investment should be based on the logic of commitment. But when investment is securitized as a marketable asset on the stock exchange, then it "is as though a farmer, having tapped his barometer after breakfast, could decide to remove his capital from the farming business between 10 and 11 in the morning and reconsider whether he should return to it later in the week" (151). The stock exchange panders to the "fetish of liquidity" and thus the logic of exit continually undermines the bonds of long-term commitment that are so important to problem-solving and productive enterprise.

The current economic crisis offers ample new examples of how securitization breeds irresponsibility by substituting the logic of exit for the logic of commitment. For instance, the traditional commitment-based banking relationship between a local bank and a homeowner was transformed by the securitized mortgage obligations into an irresponsible relationship where bankers could make subprime mortgages and then slough off the consequences onto distant financial institutions which lacked the local knowledge to value the financial assets.

The argument being made here is that this securitization-breeds-irresponsibility phenomenon (by substituting the logic of exit for the logic of commitment where the latter may be more appropriate) has occurred on a massive scale in the widely held American-style corporation. With "ownership" securitized and scattered to the four winds, the most powerful non-governmental organizations may slough off social responsibility to the communities where they operate. Or, put the other way around, the people in those communities are blocked from using their principal associational involvement to address local problems. This organizational failure in the form of institutionalized social irresponsibility then increases the need for increased government involvement or a third sector response to address the problems.

Conclusion

Beyond the family, most people have thick day-to-day participation in only one organization: their workplace. They may have some participation on weekends and evenings in other groups such as churches and various social clubs and hobby groups, but that marginal participation is rarely coupled with effective social action. The more natural site for collective action to address community problems would be where people are involved in effective collective action all day long: their work organization. Yet we have seen that the peculiar organization of the American-style company leaves the de facto members of the firm without any franchise to address their common problems in the community or environment. In contrast, there would be no such limitation on embedded companies such as locally owned businesses or family farms making their contribution to local problems directly through their businesses.

As was noted long ago (for example, Scitovsky 1951), there is no reason for the entrepreneur or family firm to take profits as the sole maximizing goal (although costs, of course, have to be covered for long-term sustainability). But with scattered, absentee owners, profit seems to be the only thing that they can agree on in general. Hence profit maximization has been canonized as "the goal" of the firm when in fact it is only an artifact of a particular and in some respects incoherent organizational form. A Japanese-style firm such as Toyota has a much more complex set of goals (where corporate social responsibility is not just a public relations stunt) and yet can still out-compete its American counterparts. For the connection with the local community, one might compare any of the large car-producing Japanese cities to Detroit. The empirical hypothesis is that the relative size of the nonprofit sector in a country is roughly proportional to the prevalence of the American-style model of a company as a piece of property widely held by absentee investors with (thus) the sole goal of profit maximization.

By this argument, the size of the philanthropic or nonprofit sector in America is a result, over the decades, of the organizational blockage in the absentee-owned corporation that prevents people from attending directly to local matters through the organizations where they already have collective efficacy. With those natural channels of social action blocked, special or ad hoc nonprofit corporations need to be created to try to address the social problems that government leaves unresolved. Then attention is focused on how to vitalize or revitalize the nonprofit sector so that its organizations are as effective as the productive organizations of the modern economy.

Our analysis suggests that the root of the matter is that the primary organizations for effective collective action are limited by their ownership structure to narrow, profit-maximizing goals, and this in turn requires the strengthening of the third, "nonprofit" sector which attempts, often ineffectively, to address the social problems unresolved by government.

REFERENCES

Aoki, Masahiko. 1988. *Information, Incentives, and Bargaining in the Japanese Economy*. New York: Cambridge University Press.

Berle, Adolf and Gardiner Means. 1932. *The Modern Corporation and Private Property*. New York: MacMillan Company.

Dore, Ronald and Hugh Whittaker. 1994. "Introduction." K. Imai and R. Komiya, eds. *Business Enterprise in Japan: Views of Leading Japanese Economists.* Cambridge: MIT Press.

Ellerman, David. 2005. "The Two Institutional Logics: Exit-Oriented Versus Commitment-Oriented Institutional Designs." *International Economic Journal,* 19 (2 June): 147-68.

Godbout, Jacques T. 1998. *The World of the Gift*. Montreal: McGill-Queen's University Press.

Goyder, George. 1961. *The Responsible Company*. Oxford: Basil Blackwell.

Hayek, Friedrich A. 1973. *Law, Legislation, and Liberty.* Vol.1, *Rules and Order*. Chicago: University of Chicago Press.

———. 1989. *The Fatal Conceit: The Errors of Socialism*. Chicago: University of Chicago Press.

Hirschman, Albert O. 1970. *Exit, Voice, and Loyalty: Responses to Decline in Firms, Organizations, and States*. Cambridge: Harvard University Press.

Jacobs, Jane. 1992. *Systems of Survival: A Dialogue on the Moral Foundations of Commerce and Politics*. New York: Vintage Books.

Kagono, Tadao and Takao Kobayashi. 1994. "The Provision of Resources and Barriers to Exit." K. Imai and R. Komiya, eds. *Business Enterprise in Japan*. Cambridge: MIT Press.

Keynes, John Maynard. 1936. *The General Theory of Employment, Interest, and Money*. New York: Harcourt, Brace & World.

Leibenstein, Harvey. 1984. "The Japanese Management System: An X-Efficiency

Game Theory Analysis." M. Aoki, ed. *The Economic Analysis of the Japanese Firm*. Amsterdam: Elsevier.

McGregor, Douglas. 1960. *The Human Side of Enterprise*. New York: McGraw-Hill.

Percy, Eustace. 1944. *The Unknown State: 16th Riddell Memorial Lectures*. London: Oxford University Press.

Ross, Stephen A. 1973. "The Economic Theory of Agency: The Principal's Problem." *American Economic Review*, 63: 134-9.

Scitovsky, Tibor. 1951. *Welfare and Competition*. Chicago: Irwin.

Simon, Herbert. 1991. "Organizations and Markets." *Journal of Economic Perspectives,* 5 (2, Spring): 25-44.

Stiglitz, Joseph E. 1974. "Incentives and Risk-Sharing in Sharecropping." *Review of Economic Studies,* 41: 219-255.

Williamson, Oliver E. 1985. *The Economic Institutions of Capitalism*. New York: The Free Press.

COMMENT

EXPLAINING THE SCALE OF THE PHILANTHROPIC SECTOR

David L. Prychitko

David Ellerman offers a nice paper on organization theory, one that combines Hirschman's two logics (exit and commitment) with Simon's work on organizations. He suggests that the size of the philanthropic sector in the United States is positively related to the size of the absentee-owned, profit-maximizing corporation. This is a novel hypothesis.

I agree with the bulk of his lengthy discussion of Hirschman and Simon (and the contrast between the theory of American firms versus J-firms), and this accounts for almost the entire paper. Those of us acquainted with the literature will find little that is new here. This makes it something of a challenge for me to find something to criticize.

I do have a few disagreements, however, and I hope that my brief discussion of them does not distract from the key issue at hand: an explanation of the size of America's civil or voluntary sector.

For example, I disagree with Ellerman's lumping of neoclassical and Austrian economics, which he characterizes as focusing almost exclusively on market organizations using the logic of exit. He suggests, in fact, that Austrian economics has little or no theory about organizations, particularly for-profit corporations. The theory of market exchange crowds out a theory of corporate organization, what Ellerman describes as "the other half" of a modern market system. He chides Hayek in particular for apparently juxtaposing the market system, as a spontaneously generated order, with that of government planning. "There is no recognition of [corporations] as the principal actors in a modern industrial economy and little recognition that much of the spontaneous order theory about the market does not apply to organizations (taxis)." (Ellerman 2009, 84) On this, Ellerman might be comforted to hear that younger Austrians

Prychitko, David L. 2009. Explaining the Scale of the Philanthropic Sector. *Conversations on Philanthropy VI*: 97-100.
ISSN 1552-9592

have been working on the theory of the firm and on market-based management.

On a related note, it might be worthwhile to consider corporations—or for-profit firms in general—as institutions that combine workers, managers, and owners in an "ends-oriented" sense. People with unique knowledge and skills are combined with financial and physical capital to produce not only a product or service but also ultimately to produce profits for the owners. That is their economic "end" or goal. We can also consider nonprofit and not-for-profit associations as ends-oriented as well. The markets within which firms coordinate their plans (Simon's red-colored social structures) are largely "means-oriented," which is to say, profit-seeking organizations approach one another as means to the fulfillment of their own ends. Similarly, nonprofit firms obtain physical plant and equipment not with the intention of being "charitable" to the suppliers but instead with the goal of accomplishing their own missions.

The modern economy, and the "civil" or "philanthropic" sector too, is indeed unthinkable without "ends-oriented" organizations—institutions—that fulfill their plans through "means-oriented" exchanges. I wouldn't refer to them as the other half of a market economy. I fully agree with Ellerman that they are the primary actors that seek mutually beneficial coordination among themselves using market processes. In this sense planning is universal; it is not restricted to the interventionist plans of contemporary government bureaus. It's a question of who is planning and for what ends. The resulting pattern of coordination within markets is not planned as a whole—it is not an end sought by its participants—but emerges as a spontaneous order.

I have a minor point of disagreement with Ellerman's brief claim that consumers don't follow the logic of commitment. I think we witness today a panoply of goods that consumers (not simply the workers) strongly identify themselves with, for better or worse. Nike, Apple, Windows, particular brands of clothing and shops, autos, and so on inspire a sense of attachment: "I'm a Ford Man." "Not me, I'm a Dodge Man." "I only drink Sam Adams." This has also grown to the more abstract level of "Buy American." There seems to be little of that kind of identification with large philanthropic organizations, but it does seem to be growing among local consumer co-ops and other associations.

One last, minor point. I find it more difficult to accept that the family is perhaps the clearest example of a commitment-oriented institution. Ellerman offers the relationship of the parent to the child, but today divorce is widespread and marriages are entered into with a strong exit-oriented strategy. One might say, using Habermas's language, that the market has "colonized the lifeworld" of potential marriage partners. One need not follow Habermas here, but perhaps the modern economy's exit-strategy and means-oriented behaviors are now reaching into areas that were once strongly tied to commitments. On a related issue, if philanthropic enterprise is modeled after for-profit, "competitive" business organizations (if only theoretically, as in the work of Weisbrod), I think all bets are off regarding the possibility of a vibrant and growing civil sector.

Ellerman, to his great credit, makes no recommendations whatsoever that the philanthropic organization should be viewed through the narrow lens of neoclassical economics and business-model imagery. I would guess that he, like me, would hesitate to use the term "philanthropic enterprise," because it connotes and may even encourage the image of enterprise as commonly understood.

But it is also unclear to me what an alternative theory of philanthropic organizations would look like. How might the Hirschman-Simon approach cast light on civil-sector associations in general? This is not the aim of Ellerman's paper, so I raise the question not as a criticism but instead as a suggestion for further research.

Ellerman's discussion of the literature of organizations seeks to show that the American-style corporation is wedded to the logic of exit, and he suggests (at least implicitly) that this institutional form is unlikely to be transformed into one organized by the logic of commitment. He points to the Japanese-style firm as being partly rooted in the logic of commitment (if imperfectly). He suggests that the J-style firm tends to satisfy the local, specific needs and community-oriented spirit of its workforce, lowering the incentive for people there to adopt philanthropic associations, because they find it within their own corporate enterprise.

His is largely a theoretical paper, and I find no fault in that. At the end he raises a testable and potentially fruitful idea: "The empirical hypothesis is that the relative size of the nonprofit sector in a country is roughly proportional to the prevalence of the American-style model of a company as a piece of property widely held by absentee investors with (thus) the goal of profit maximization" (Ellerman 2009, 94) The American economy is more likely to have a robust set of voluntary associations than the Japanese economy because American corporations aren't designed to satisfy the non-work needs of citizens, who, in turn, pursue the economist's logic of exit. Agreements based upon commitment are more likely to emerge in the civil sector, which is not guided, for the most part, by the exit strategy.

From the perspective of mathematical statistics, Ellerman suggests a positive partial derivative. (That's merely a fancy way of saying there are other variables at work that might explain the relatively large scale of our philanthropic sector.) There are probably other "parts" to the explanation. I would imagine that arguments can be made to suggest that the scope of the state (and its unintended consequences), the level of wealth, long-term economic growth, taxation, and other such factors also affect the incentives and motivation to pursue philanthropic activities. In short, this is a *ceteris paribus* experiment, one that good social science is apt to make.

Testing it could be a challenge. We would need to home in on the specifics. For example, how might we measure the prevalence of the American-style company? Corporate profits as a percent of GDP? That approach would measure prevalence by means of accounting profit. But profits in the aggregate change from year to year, along with real GDP, and even if we could identify a long-run trend, is it a meaningful measure? Should prevalence be measured instead by the level of the workforce employed in corporate firms? (This is an interesting issue if proprietorships employ a larger percentage of the workforce. Could we predict a kind of reversal process if the number of people employed by proprietorships increases because of significant job losses in the corporate sector, whose long-term consequences include a growing commitment to the philanthropic sector, all other things constant?) How, too, might we measure the relative size of the philanthropic sector? This immediately raises the difficult issue of defining the philanthropic sector, a problem with which we are all too familiar. Does it include foundations along with all sorts of voluntary associations from the Little Brothers of the Poor to the local branch of Narcotics Anonymous? Would we look at the number of people who are employed and volunteer in these organizations? Would we add foundation incomes and the estimated values of volunteers' labor time? Would we seek to develop some kind of shadow-estimate of the dollar market values of the services these organizations provide?

Ellerman's fine paper encourages us to reconsider the organizational logics and strategies of for-profit firms and their implications for civil society associations. It should also further encourage us to develop clearer concepts with which to study and measure the nonprofit sector.

REFERENCES

Ellerman, David. 2009. "Rethinking Philanthropy and Business." *Conversations on Philanthropy VI*: 79-96. ©2009 DonorsTrust.

COMMENT

OUT OF PHILANTHROPY AND INTO SOCIAL ENTERPRISE? PROBABLY NOT

Roger A. Lohmann

In his essay on "Rethinking Philanthropy and Business," David Ellerman makes it clear that he has little interest in the existing phenomenon that Bremner (1988), Payton (1988), Ealy (2009), McCully (2008) and others characterize as philanthropy. Ellerman's presentation of philanthropy in this piece is idiosyncratic, endorsing in turn both a residual, "government failure" approach and a market failure approach to which he adds his own "philanthropic failure" approach which, he says, could be corrected by corporate reform. The result is a view of philanthropy and nonprofit activity, which he says is much the same thing, as epiphenomena whose existences are conditional on the failures and inadequacies of corporate business in enabling individuals to address collective concerns through their work life. In this way, Ellerman seeks to move philanthropy entirely off the map of human affairs. In its place, he offers a fairly concise definition of what others today call social enterprise. His distinct contribution here may well be his effort to give voice to a firmly anti-philanthropic view within the literature of philanthropy itself. For those whose primary interest (and engagement with this journal) is mediated not through a primary interest in "business (in some sense)" but through an interest in understanding philanthropy, it appears that the Ellerman "rethinking" presaged in the title is largely a matter of simple and complete dismissal. That business may—or in some reconfigured form, would—offer a socially responsible venue for collective action is one of a number of unexplored presuppositions in the paper.

Given his declared interest in replacing talk of philanthropy with a focus on social enterprise, the paper holds little mystery about where he will eventually

Lohmann, Roger A. 2009. Out of Philanthropy and Into Social Enterprise? Probably Not. *Conversations on Philanthropy VI*: 101-110. ISSN 1552-9592

come out: philanthropy holds no promise of becoming a spontaneous order and needs to be reconfigured as socially responsible business (about which no view on spontaneous order is offered). There is, it would seem, no hope of spontaneity from the more conventional nonprofit sector of "outside-the-family organizational involvement to address local problems" (Ellerman 2009, 79), which is the conception of "philanthropy" Ellerman consistently employs throughout the paper. In contrast to the approaches of Bremner, Payton, Ealy, McCully, and others, philanthropy for Ellerman is synonymous with existing local nonprofit sectors and a faulty human project that ought to be discarded.

The Hirschman Typology?

Several presuppositions that appear to interest Ellerman most, or at least are a major theme of the paper, are discussed within a framework of exit and commitment he claims to be derived from the work of Albert Hirschman (1981). Ellerman's reason for introducing the Hirschman typology appears to be located in his subsequent elaboration of an extensive search-tree formalism. However, I fail to find any connection to philanthropy or, for that matter, to his central argument, although there are some potential points of entry to his social enterprise perspective.

Let me note here that Ellerman and I disagree fundamentally over our respective readings of Hirschman, and that this disagreement is systematically related to our respective views on philanthropy. As the title of Hirschman's 1981 book indicates, his formulation was a three-term model, locating exit, voice, and loyalty as strategic options (as the subtitle notes) *in response to decline in institutions* including firms, organizations, and states. In embracing this model, Ellerman appears to assume that philanthropy is currently either in a state of decline or has always been in the sorry state he sees it in at present. After a brief mention of Hirschman, he substitutes his own two-part formulation for the original, one that conflates Hirschman's trio into a pair of options, which Ellerman terms exit and commitment. Ellerman's commitment is a concept that places greater emphasis on what Hirschman calls loyalty than on what the latter terms voice. It also excises the Hirschman typology from its original context of strategic responses to institutional decline. Ellerman offers no explanation for why anyone faced with the state of institutional decline in philanthropy that he alleges should have only the options of fleeing or remaining committed to a deteriorating institution. His own formulation, as noted above, steps outside those narrow choices and gives voice to a thoroughgoing reform strategy.

The overall effect of his narrowing of Hirschman's options enables Ellerman to channel any resulting discussion of philanthropy into instances in which philanthropic impulses can only serve to depart completely (as he himself does) or embrace without challenge the existing philanthropic order. In other words, by this theoretical narrowing of Hirschman he deprives philanthropists of what many in the field would see as a primary avenue of arresting institutional decline: giving voice to their discontents.

This constitutes a rather subtle elimination, at a conceptual level, of almost any possibility of an emerging spontaneous order in philanthropy, by removing the theoretical grounds for such emergence. In effect, Ellerman's discussion and his branching diagram offer philanthropists two options: they can go along with things as they are, or they can leave. He even explicitly refers to this choice as a refinement of the "love it or leave it" option. What the original Hirschman argument said, however, was more along the lines of "love it, leave it, or speak up about it."

It might be interesting for a deeper understanding of the potential for spontaneous order in actual philanthropy (as opposed to Ellerman's straw man) to develop the branching diagram within Hirschman's original tripartite distinction, allowing room not only for exit and loyalty but also for voice (in such diverse forms as assembly, representation, speech, petition, and protest). For it is in voice where much of the action and in particular the possibilities of both spontaneous order and of independent philanthropy are to be found. By excluding voice, Ellerman in effect cuts philanthropy off at the taproot. For voice, far more than exit or loyalty, is a key dynamic of philanthropy, even in Ellerman's narrow sense of "outside-the-family organizational involvement to address local problems."

The omission of philanthropic voice is, however, consistent with the other parts of Ellerman's argument, such as his statist assumption that philanthropy is a derivation of government failure. This arises first in his question, "How might people address their community's social and environmental problems *to the extent that government is ineffective?* (2009, 79)" Ellerman himself clarifies this issue for any who might doubt that this question embodies a government-failure thesis. He makes quite clear in the final paragraph of the paper that it is his intent to see philanthropy and nonprofit organization as not arising independently but at least in part from the failures of government.

One might well wonder why he takes this tack. In combination, these rhetorical devices enable Ellerman to present nonprofit philanthropy as a weak and febrile phenomenon largely without redeeming social value and incapable of improvement within the narrow dynamics of exit and commitment, devoid of voice, and thus any possibility of spontaneous order. Small wonder that Ellerman seeks to dismiss such an emaciated model of philanthropy and replace it with what he sees as a more robust, dynamic model of socially responsible business enterprise. A pesky question we must ask is whether such an anemic portrait of philanthropy has any grounding in reality, or if it serves only as a straw man to be upended in favor of the more robust, virile, socially responsible business Ellerman obviously prefers. For many of us, another question is whether philanthropy and social enterprise should be seen as mutually exclusive alternatives?

This brings us around to the rationale of his argument: the great mystery here is why Ellerman bothers to even mention philanthropy. Clearly, his first interest here is corporate reform in the business sector to foster greater responsibility and social engagement of business. This is a reasonable and enlightened objective that can easily be pursued with little or no attention to philanthropy. Why, then, does he bother? (For one possible answer, see my comments on his late introduction of the market-failure thesis, later in this essay.)

Similar derivations of government-failure theory have often been employed to rationalize philanthropy as a by-product of public sector inadequacy or failure. This is a presupposition that simply gets things backwards, at least in the American case. As Richard Cornuelle (1993) first suggested, a genuinely *independent* (and primary) sector for philanthropy requires no derivation from failures of either government or market. I have argued that it makes greater sense to see an independent sector as the staging area for organizing republics and democratic government than the other way around. Abraham Lincoln's evocative formulation of republican democracy as "government of the people, by the people, for the people" suggests in part that legitimate political states are formed in public or civic space outside of both governments and markets and take their legitimacy from the philanthropic acts of the citizens who form them.

Countless examples support this view, including such major social acts of philanthropy as the American Revolution and, earlier, the Mayflower Compact (McCully 2008). In such cases, a group of citizens voluntarily associating elects (both in the sense of choice and of representation) to form a governance structure or a market without raising our suspicions. By contrast, if an existing market or government elects to form a philanthropic project of any sort, suspicions in some quarter will almost certainly be aroused. It is a principal challenge of Ellerman's logic to address those suspicions in the case of corporate business.

Ellerman's conflation of loyalty and voice into the single dynamic of commitment also has the unfortunate effect of effectively ruling out of bounds some of the most distinct and effective potential loci of spontaneous order or change in philanthropy. The case of the Puritans on the Mayflower may be slightly ambiguous: formulating that compact situated voice within a dual strategy of exit from merry old English persecution and the need to elicit loyalty to ensure survival in the wilderness of North America. However, the case of the American Revolution as philanthropy is, following McCully, much more clear on this point. By focusing on the voices of the revolutionary patriots, we can easily see that this particular revolution was a gift to the world and to history of a distinct vision of a workable democratic republic. The Declaration of Independence, the Articles of Confederation, the Federalist papers, and the Constitution and Amendments (notably the First), as well as other, lesser-known documents such as the letters of the committees of correspondence, all might be recognized in philanthropic terms and termed gifts of liberty to the human community.

By contrast, interpreting the American Revolution as philanthropy within the Ellerman model dulls much of its luster. It reduces the matter to a choice between exit (from the British Empire or back to the empire for the Tories who exited to Canada) and commitment (to the new republic). In this dual choice, the larger significance of these historic events for the rest of the world is lost entirely, precisely because the voice of the revolution is lost. And how these events would have been better served philanthropically by socially responsible, profit-oriented business activity is a mystery. Yet, operating within Ellerman's logic, these are the only options.

In more contemporary, pedestrian, and mundane terms, philanthropic mission and vision statements, advocacy activities including protest demonstrations, assorted manifestos, strategic plans, and numerous other examples taken from contemporary third sector practices all illustrate similarly provocative and enduring roles of voice in philanthropy, even in the narrow sense in which Ellerman defines it.

Exit and Brand Loyalty

The absence of voice in Ellerman's paradigm also means that his treatment of the relationship between market and exit is also rather one-dimensional and ultimately unconvincing. It may, indeed, be the case that denizens of markets exercise exit options when the price is not right for them. However, the suggestions that exit or commitment (perhaps in the form of brand loyalty) are the only options and, more importantly, that only in markets can exit be exercised, are equally false and misleading claims. Strikingly similar exit options are available to all participants in voluntary activities of all types, and philanthropy in particular. Members of an organization may exit at any time; that's why it is called voluntary association. Likewise, donors may simply withhold their donations, and volunteers may withdraw their volunteer labor. The problem often is that a simple choice between mute commitment and exit isn't really the range of choice members, donors, or volunteers may be looking for. At times they just want someone to notice, speak out, or listen.

Moreover, the choice between exit and commitment as Ellerman presents it here serves also to minimize or discount the spontaneous order of philanthropy in an area close to his main interest: the kind of philanthropic entrepreneurial activities that might best be termed product definition and market formation. As I have noted elsewhere, the creativity of spontaneous orders is not limited entirely to business (Lohmann and Lohmann 2002, Lohmann 2009). One of the things philanthropic enterprises sometimes do, at times exceedingly well, is spontaneously define through their philanthropy new products and services which are subsequently shown to be commercially viable and around which new markets may form. Long before there was an insurance industry or any life insurance products in the world, nineteenth-century mutual aid and self-help organizations in the United States and Europe pioneered this field and demonstrated the enormous commercial markets latent in their "burial funds." The fact that they may not have done it as profitably as the later insurance industry is less germane than the fact of the spontaneous generation of a new market order through their philanthropy. Much the same can be said more recently for child and adult day care, home health and homemaker and chore services for the elderly, home-delivered meals, and most forms of education.

It is certainly not my intent to suggest that philanthropy is the ultimate source of all (or even much) market innovation. That would be an absurd suggestion. However, it is equally erroneous to ignore or discount any philanthropic role in product development and market formation. And both voice and spontaneous order in philanthropy are often closely associated with such innovation.

Simon Says: There Are Lumps in that Buttermilk

The part of Ellerman's paper that is most important for his project is his introduction of Herbert Simon's analysis of markets and organizations. Whether other Austrian economists concur with him regarding Simon's thesis on the relative balance of markets and organizations will remain relatively unimportant to the study of philanthropy. However, the recognition of the importance of organizations is an important one that bodes well for any understanding of philanthropy precisely because so much of the current philanthropic enterprise institutionally resides in organizations and there are so few genuine, recognized philanthropic markets.

It is in this discussion that Ellerman outlines his strongest defense for the social enterprise perspective which appears to be close to the heart of his interest. He writes, "one does not need to look to the philanthropic sector to find alternatives to the narrow self-interest usually taken as the model of market exchange." [2009, 84] The use here of the phrase "philanthropic sector" is one of numerous indications throughout that Ellerman equates the nonprofit sector and philanthropy, as noted. And one can agree with him that narrow self-interest need not equate with market exchange. There is room here for Adam Smith's moral philosophy alongside his economics, and for some Tocquevillian "self-interest properly understood."

Ultimately, space must be made in Ellerman's project for discussion of possible exceptions and lacunae in the rule of thumb that corporations legally serve the interests of their shareholders only when they are profit-maximizing. The statements above in which Ellerman outlines a focus on local, community-level concerns offer support for a more engaged social enterprise perspective quite independent of any concern with philanthropy. Whether in new product development; disaster recovery contexts in New Orleans or Biloxi; in the consequences of deindustrialization that remain concerns throughout the Rust Belt and beyond; or in other instances, socially responsible business is not so much in conflict with independent philanthropy as with its own legal strictures and limits. To suggest that this must be seen in a kind of either-or choice of philanthropy or social enterprise is misleading.

To forget about philanthropy completely and address his vision of social enterprise directly would be the most logical next step for Ellerman along the path he sets out here. Unless some partial resolution of the question of establishing shareholder responsibility is addressed, Ellerman's vision of reestablishing business responsibility seems futile, much less capable of harnessing "the far-flung shareholders from the social and environmental impact of their 'corporate governance'" for "outside-the-family organizational involvement to address local problems." And without such reforms in corporate governance, supplanting philanthropy through reforms in corporate social enterprise—which seems to be Ellerman's ultimate objective—would remain pretty much an empty gesture.

But it is equally clear that reforming business corporations has little to do with the primary concerns of most "philanthropologists" (to use Amos Warner's 1896 neologism for those who study philanthropy). For Ellerman, however, such changes appear to be the very essence of overcoming the institutional decline he sees in philanthropy, as noted in the final section of his paper, because he seems to believe—in contrast with civil society theorists and most sociologists and political theorists—that the corporate workplace is the primary non-family feature of modern social life.

"Beyond the family," he says, "most people have thick day-to-day participation in only one organization: their workplace." And thus, he continues, "The more natural site for collective action to address community problems would be where people are involved in effective collective action all day long: their work organization" (2009, 94). In Ellerman's hands, this does not appear to invoke any familiar workplace philanthropy such as workplace giving campaigns.

Furthermore, Ellerman appears to discount completely those workaday philanthropoids who have some minimal engagement in work-related activity and whose real interests and engagements are wrapped up in church, membership associations, social networking, and forms of social action. He simply equates civil society with commercial society, almost as though Adam Smith had written only *The Wealth of Nations* and Adam Ferguson had written only of civil society. Yet his argument against philanthropy is upended when one recognizes that for the idle (not employed) wealthy, retired, unemployed, adolescent dependents, and numerous others, "thick day-to-day participation" in the workplace does not accurately describe their circumstances. Even at those moments in history such as the present where Ellerman's "most people" statement may be at least partially true, one might respond that there is nothing inherent in the nature of philanthropy that makes it an issue subject to majoritarian rule. And even if it applies only to a minority, one cannot blithely discount the reality of philanthropic involvement lacking any discernible links to the workplace.

All of the diverse considerations and preconceptions of Ellerman's perspective come together in the final section of the paper, where he offers his own unique and ahistorical explanation of the existence of contemporary philanthropy-as-nonprofit-sector as a response to the failure of the corporate structure of absentee-owned business to solve the problem of collective action in the workplace:

"Our analysis suggests that the root of the matter is that *the primary organizations for effective collective action* are limited by their ownership structure to narrow, profit-maximizing goals, and this in turn requires the strengthening of the third, "nonprofit" sector which attempts, often ineffectively, to address the social problems unresolved by government" (2009, 95). [emphasis added]

That last sentence of his essay effectively summarizes Ellerman's commitment to the combined market-failure and government-failure justifications for the nonprofit sector and to the philanthropy = nonprofit sector presuppositions on which his call for corporate reform is premised. For him these compound failures do not yield contending explanations for how philanthropy is derived, but point instead to corporate reforms that would simultaneously eliminate any necessity for both independent philanthropy and government action.

The proof here is in the pudding: Until there is evidence of the corporate reforms he proposes actually eliminating absentee ownership and increasing corporate responsibility combined with further evidence of increased workplace-related engagement with major social problems, it will be interesting to contemplate the possibilities of Ellerman's call for local social enterprise, but impossible to take seriously his dismissal of philanthropy and the nonprofit sector.

REFERENCES

Bremner, Robert Hamlett. 1988. *American Philanthropy*. 2nd ed. The Chicago History of American Civilization. Chicago: University of Chicago Press.

Cornuelle, Richard C. 1993. *Reclaiming the American Dream : The Role of Private Individuals and Voluntary Associations.* New Brunswick, NJ: Transaction Publishers.

Ealy, Lenore. 2009. Personal Communication. June 26, 2009. See also, http://web.archive.org/web/20080123190358rn_1/www.thephilanthropicenterprise.org/main/index.php/

Ellerman, David. 2009. "Rethinking Philanthropy and Business." *Conversations on Philanthropy VI:* 79-96. ©2009 DonorsTrust.

Hirschman, Albert O. 1981. *Exit, Voice, and Loyalty: Responses to Decline in Firms, Organizations, and States.* Cambridge, MA: Harvard University Press.

Lohmann, Roger A. 1992. *The Commons: New Perspectives on Nonprofit Organization, Voluntary Action, and Philanthropy.* San Francisco: Jossey-Bass.

———. 2009. Spontaneous Order and the Somewhat-Less-Hidden Hand. *Studies in Spontaneous Order,* 2 (1).

Lohmann, Roger A. and Nancy Lohmann. 2002. *Social Administration*. New York: Columbia University Press.

McCully, George. 2008. *Philanthropy Reconsidered: Private Initiatives, Public Good, Quality of Life.* Bloomington, IN: Author House.

Payton, Robert L. 1988. *Philanthropy: Voluntary Action for the Public Good*. New York: American Council on Education.