GRIT WITH GRACE

# Givin' on a Prayer: The Myths that Starve Philanthropy

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with research assistance from Dustin Lowman

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> *He was starving in some deep mystery,*
> *Like a man who is sure what is true.*
>
> - Leonard Cohen, "Master Song"

Philanthropy is one of my favorite things. I have dedicated many hours to it for myself — and for my clients — over the past 25 years. But, as Andrew Carnegie said, "It is more difficult to give money away intelligently than to earn it in the first place." Philanthropy — it's a messy business. And, in philanthropy even more than in investing, far too often we (including yours truly) are still ruled by our caveman brains.


To borrow a phrase from the brilliant Dan Ariely, humans are "predictably irrational." Certain that our emotions and our instincts are unimpeachably true, we don't interrogate them. Far too often, our cognitive biases rule our decisions. It's the same cognitive block that causes people to call their wealth advisors to sell stocks when the market dips. Pulled into a lizard-brain fight or flight mode, people fail to stop, take a deep breath, and ask, "**Why**?"

"Given that, in the long term, the most tried and true way to make money has been by investing in the stock market, **why** sell during a downturn? Why not buy, as stocks have gone on sale?" You've never seen me run out of Saks, frantic that my favorite shoes are now on sale, have you?

In philanthropy, it would go something more like: "Given that I spend a lot of time and money making sure my investments are sound and solid, **why** do I donate without first doing much due diligence research?" As Ken Stern wisely says in his myth busting book, *With Charity for All*:

> "For most charities, the story from the front lines is the most important measure of success, one that typically confirms the importance of the work and reassures stakeholders. Empirical

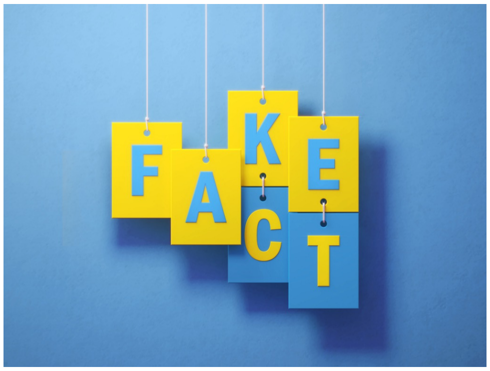
and research studies are to be avoided as expensive, distracting, and potentially dangerous. In some ways, the charitable world exhibits an almost medieval aversion to scientific scrutiny and accountability."

Or, "**Why**, when I see the (501c3) label, do I take that to mean the organization is 'good,' when there might be evidence to the contrary?" Surely, as well all know, examples of **(501c3) frauds** abound.

Better yet, and my favorite pet peeve of all is, "**Why** would I rather my money get spent on research expenses than on state-of-the-art infrastructure (otherwise known as overhead), which is actually the lifeblood of any organization?"

I believe that if donors asked these questions of themselves, charitable giving would be far more effective.

Solving intractable social issues takes constant, sustained effort; it takes a network of donors who believe in the cause and who are willing to commit to a long process of trial-and-error (depending on the problem); it takes extremely talented, gifted leaders, who are capable of uniting goodhearted people around a common cause; and it takes rigorous systems of evaluation to help determine whether all the work is paying off. And, perhaps above all, it takes rational, clear-headed thinking.




But instead of all that, far too often, deeply flawed evaluative systems and thinking has plagued the world of charitable organizations. This approach causes donors to value certain types of organizations over others, making them less committed to trial-and-error than to the immediate gratification of feeling like they're donating "to the cause."

In this article, I detail a few of the cognitive fallacies surrounding philanthropy, and provide alternate perceptive frameworks for improving the way we think about charities. I implore you to stop believing in certain "myths" and to open your mind to new ways of thinking about philanthropy. If we can evolve how we think about our philanthropic giving, we can significantly clean up the messy and muddy world of philanthropy, and contribute to a more civically responsible society.

## Public Enemy #1: Overhead

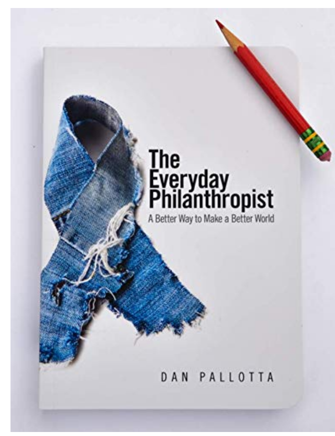
Spending that falls under the wide umbrella of "overhead" has long been viewed as abhorrent by organizations that evaluate charities, and consequently, by the donors who might otherwise give them money. Vilifying overhead spending causes charitable organizations to spend less on it than they should, making them more appealing to donors, but paradoxically, far less effective at curing their chosen social ill. In a landmark 2009 report published by the Stanford Social Innovation Review (SSIR), this insidious process was termed the "starvation cycle," in which charities are rewarded by donors for purging themselves of overhead expenses which are, very ironically, fundamental for them to fulfill their stated purposes.

Among that study's findings were that, because of how much donors despised overhead spending, charities were relying on "nonfunctioning computers, staff members who lacked the training needed for their positions, and, in one instance, furniture so old and beaten down that the movers refused to move it…nonfunctioning computers cannot track program outcomes," the researchers stated, and "poorly trained staff cannot deliver quality services to beneficiaries."

That was 2009. Surely that study would have shaken things up, right? Shined a light on our irrationality, and brought in a new wave of thoughtful charitable giving?

Not exactly. In 2013, Guidestar, Charity Navigator, and BBB Wise Giving Alliance finally acknowledged this issue, and penned an open letter — eventually known as the Overhead Myth Letter — in which they pleadingly reiterated the SSIR's findings of four years earlier. "The people and communities served by charities don't need low overhead," they wrote, "they need high performance." What they didn't mention in the open letter was that they'd been perpetuating the overhead myth for years.

Here is evidenced a key fallacy: Overhead is a false God and a meaningless metric. As Albert Einstein so wisely said, "Not everything that can be counted counts, and not everything that counts can be counted." Evaluate a charity not by its overhead, but by its impact. If the point of a charity is to raise literacy among underserved portions of the population, why evaluate them on how readily they hire under-trained, inexpensive staff?




Remarkably, the topic still has yet to be resolved. *The Everyday Philanthropist*, a 2020 mini-treatise by Dan Pallotta on effective charitable giving, details the *same* phenomenon. Pallotta indicates another source of the problem: What few charity watchdogs there are cannot possibly conduct in-depth evaluations of every charitable organization's impact. So, "many of the watchdogs rely on inexpensive, easy-to-acquire financial information," like, of course, overhead expenses.

Executives often take the brunt of the overhead myth. When donors worship at the altar of reduced overhead, executive salaries are among the first in the firing line. Viewed through an emotional lens, it makes sense — the point of a charity is to solve social problems, not to make executives wealthy.

But viewed through another, considerably more rational lens, if charities are unable to offer their executives competitive pay, those same executives are going to get other, more compelling offers. The people who tend to pursue those executive jobs tend not to be extraordinarily wealthy — and, even if they were, why shouldn't they be? I neither know nor care about football, but my research assistant tells me that people cheerfully pay Roger Goodell $40 million per year to make sure we can watch football. I know and do care a lot about hedge funds. A successful hedge fund manager can make billions a year. Yet we bristle at the idea of someone making $500,000 per year for helping address world hunger and save people's lives. These executives are often faced with a painful choice between sticking to their values-based guns and working for the charity anyway, or taking what amounts to a much better deal. As my good friend Bruce DeBoskey puts it, “The mutually exclusive choice currently faced by many qualified candidates [is]: Do well or do good.” True, but **why**?

Why does the overhead myth persist? When I’m at my most cynical, I theorize that people haven’t wised up yet because they’re less interested in solving problems than getting that immediate-gratification burst of altruistic pride that comes with giving money away. In other rather blunt words, they’d rather feel good about themselves than really help solve a social problem.

But when I’m thinking more idealistically, I believe that if people had access to more thorough, more revealing data about charitable organizations’ *impact*, they’d be more likely to donate more thoughtfully. It’s not that they don’t care about outcomes and effectiveness, it's that they don’t yet see the evaluative methods by which they can accurately judge whether charitable organizations are solving the problems about which they care. In the immediate term, more services which can compellingly propose alternate metrics may be what we need the most. They could follow in the footsteps of the brilliant and dedicated people at Givewell.org, whose purpose is to evaluate effectiveness, and whose mission is to use deep research to search for the charities that save or improve lives the *most per dollar*.

## Restricted — Nay, Suffocated — Giving

Restricted giving — the practice of earmarking a donation for a single specific purpose — became increasingly popular throughout the previous decade. This was especially common for educational institutions, as alumni donors devoted their money to scholarships, new facilities, professor salaries, and other specific programs.

But restricted giving can be an inflexible and foolish way to give to charities. I have often told my clients that if they don’t trust an organization’s management enough to let them allocate their funding, perhaps they should find an organization with management they do trust. In circumstances where a charity needs to modernize their tech, or needs to raise the salaries of long-standing, results-providing employees, restricted money is of no use. “Restrictions are terrible for the growth of [charitable] organizations,” wrote Felix Oldenburg in a Forbes article entitled “Let’s Put an End to Restricted Giving.” He continued, “Typically, these restrictions direct spending towards field activities rather than toward core investments in people, systems, and infrastructure that could drive growth.”

Restricted gifts are much easier to secure than unrestricted ones. They play off of our emotions and desire for control. Think of the heart-tugging advertisements for animal rescue charities or child cancer care charities. True, who wouldn't want to see all of those animals in safe, happy homes? Who wouldn't want to see those children cured of that awful disease? How gratifying to say, “Here is my money but only if you save the kind of dog breed I love the most, or the African children in one particular village, or country.” But, again — **why**?

Not all restricted giving is harmful. Indeed, some circumstances warrant it, and if it's between a restricted donation and no donation at all, few charities balk at accepting the restricted donation (although in certain cases they should, and they do). But in the worst situations, restricted giving can amount to unimpactful developments, unspendable money, or worse, can cause an organization to take its eye off of its main cause.

## Philanthropic Exceptionalism

An underlying problem with philanthropy which extends to all that I've discussed so far is that people think about it differently than they think about the rest of their money. In what behavioral psychologists label "mental accounting," or the tendency of people to make financial decisions based on irrelevant but powerful mental categories, donors often put philanthropy in its own category. This is a mental bucket in which emotions form the bases of decisions and where good intentions take the place of good research. People view philanthropic giving as exceptional — not subject to the same rigors as investing a mutual fund, a startup, a house, etc. Lottery winners are often plagued by the same bias. Sadly, countless lottery winners go bankrupt for this reason.

Besides the **scams and fraud** that occur in the charity world, we should remember that the ability to inspire passion does not necessarily mean the charity has the power to deliver results. An emotional response should not be a deciding factor, but rather a jumping-off point to investigating the target charity's work, and determining whether they do good work.

Thinking of philanthropy in these needlessly exceptional terms is part of why charitable donations have been shown to rise as much as 42% around the holiday season. People are *feeling* generous around the holidays. Understandably wanting to spread some cheer, they use it as a time to donate. But I say, why not indulge that gratitude all year round? Rather than concentrating donations on a single wintry month, why not give regularly, and provide charities with critical reliable bases of support?

## The Quest for Enlightenment

Philanthropic giving is riddled with cognitive errors that make it much less effective than it could be. As discussed above, chief among these is the overhead myth, which is a millstone around the neck of the entire industry, and has far-reaching consequences. It causes competent executives to earn less than they should. It causes donors to restrict a disproportionate volume of donations, which reduces charities' flexibility, hampers their growth, and diminishes their ability to support the cause that their donors care about most.

I've dedicated decades to helping my clients protect and grow their financial capital, only to then give it away. Often, this is where happiness and money intersect! For me, it's one of the great joys of my career. But, I'm telling you that raw emotional situations are also ripe for waste, or even worse, fraud, and that you should be *doubly* investigative, not *half* as investigative when it comes to charitable giving.

When contemplating future philanthropic endeavors, I ask that you challenge certain assumptions, take the time to ask "**Why**?", conduct research, investigate whether your target charities are doing what they claim to be doing, and give in a way that's consistent with their missions and your values.

*If you found this of interest, please check out* With Charity for All, Uncharitable, *and other books in my* *Give Smart* *reading list.*

*Want to talk more about this topic? Don't hesitate to reach out!*

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## ABOUT THE AUTHOR

Randy Kaufman, formerly a corporate tax attorney and investment banker, is now a wealth advisor who prides herself on focusing on what matters most: clients' peace of mind, family dynamics, and getting *enough*, not *more*. Randy is a passionate student of impact investing, strategic philanthropy, and behavioral psychology (while not a psychologist, she occasionally plays one in the boardroom). She is dedicated to helping the underprivileged, and is a proud member of global venture fund Acumen's advisory board. A thinker, learner, and pursuer of overarching truths, she is always eager to discuss big ideas about money, and its off-and-on associate, happiness.