
The Nonprofit Industrial Complex

Is there such a thing as too much civil society?

BY GERARD ALEXANDER

As if the United States doesn't stand out enough these days, yet another trend is making us more and more distinct in the world: the massive growth of our nonprofit sector. Some people hope, and others fear, that this might change the very nature of American society. Western countries have already been transformed by industrialization, the rise of the service sector, and the growth of big government. The result has been wealthy economies, middle-class societies, and vast bureaucracies. Our country might now be transformed again by the spread of what Richard Cornuelle dubbed the "independent sector." The growth of nonprofits—from the Getty Museum to Seattle's Children's Hospital, Emory University, and your aunt's country club—has created the world's largest sector that is neither business fish nor government fowl. It has the private sector's diversity and independence but the government's lack of a profit motive. It is a different way of doing business. It may be a different way of making a country. But is it a whole-some one?

The sheer scale and rapid growth of America's nonprofit sector make it difficult to ignore. In most of history, private not-for-profit organizations weren't a topic of much attention because they weren't especially important compared with the markets from which people drew their sustenance and the governments that often extracted whatever they could from them. But with the growth of our national wealth, nonprofits have been expanding relentlessly. The Independent Sector, which is basically the industry group for nonprofits, reports that the combined annual expenditures of all the not-for-profit organizations required to file

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Form 990 with the U.S. Internal Revenue Service had grown to nearly \$1 trillion in 2004. (That's about half what the federal government spends each year, not counting defense.) In 1977, nonprofits employed around 6 million Americans; by 2001, that was up to 12 million. Roughly 85 percent of this work is in health care (primarily hospitals and nursing homes), social services like child care and job training, and education. If volunteer time is counted, nonprofits represent over 10 percent of all U.S. employment.

If anything, statistics like these underreport the size of America's nonprofit sector, because they often don't include large religious organizations, which have a distinct tax status. And they generally don't include state universities and colleges, which are technically government entities but now often register as nonprofits, frequently get only a minority of their funding from government, and function as nonprofits in almost every meaningful sense. Colleges add real heft to the numbers. In 1940, there were only 147,000 faculty members nationwide. By 1970, there were 474,000, and by 2003, almost 1.2 million, 54 percent of them full-time and most of them at state schools. And this doesn't include hundreds of thousands of college administrators.

All these nonprofits get the bulk of their money either through donations, from government subsidies, or by charging fees like tuition, hospital bills, and AAA memberships. They also get a healthy slice of their revenue from tens of thousands of foundations that are the financial heavyweights of America's nonprofit world. The Foundation Center estimates that the combined assets of these grant-making bodies (in current dollars) grew from \$30 billion in 1975 to \$227 billion in 1995 and about \$525 billion in 2005. The Gates Foundation is the largest, with about \$29 billion even before Warren Buffett's \$30 billion, multiyear pledge. The Ford Foundation is in second place with around \$12 billion. All U.S. foundations (including corporate foundations) gave away \$33.6 billion in 2005, more than double in real terms what they gave only a decade earlier.

And they aren't the only nonprofits with bulging portfolios. The top 765 U.S. universities and colleges (including state schools) tracked by the *Chronicle of Higher Education*

jointly held \$340 billion in their endowments as of mid-2006. At least 62 of them have endowments of \$1 billion or more, with Harvard at \$29 billion, Yale at \$18 billion, and Stanford at \$14 billion. Northwestern, Emory, and Washington University in St. Louis each have around \$5 billion. Here, too, growth has been accelerating. In 1981, Harvard was the only single-campus school to have more than \$1 billion in the bank. But in the 1980s, schools started aggressively fundraising, and in the 1990s, many schools doubled or even (like Yale and MIT) tripled their endowments. By 2002, Harvard alone had amassed more than the combined endowments of all 192 colleges that had been tracked in 1981. With massive ongoing fundraising campaigns, university endowments could easily surpass traditional foundations as the largest nonprofit asset-holders, each one with a single designated recipient. Harvard may already have more money than the Gates Foundation, and four other schools have surpassed the Ford Foundation.

America is such a rich and charitable country that the list doesn't stop there. Their annual reports show that the Howard Hughes Medical Institute, in Chevy Chase, Md., has a \$16.3 billion endowment; New York City's Metropolitan Museum has amassed \$2.2 billion; the Wildlife Conservation Society, which funds New York City's zoos, has \$463 million invested; and the Metropolitan Opera has \$300 million in the bank. These institutions have hundreds of more modestly endowed counterparts in hospitals, zoos, and arts institutions across the country. Ten leading U.S. think tanks have just under \$1.4 billion in combined endowments.

Even secondary schools are in the game. The titan is the ethnic-favoring Kamehameha School group in Hawaii, which has over \$7.6 billion to its name, deriving from an original property bequest. Of the better-known boarding schools, the leading dozen (such as Andover, Deerfield, and Choate) have more laboriously amassed endowments that approach a whopping \$4 billion combined. The next dozen have hundreds of millions more. And none of this includes the assets held more opaquely by institutions like the Church of Jesus Christ of Latter-day Saints, whose assets were estimated a full decade ago at \$25-30 billion.

All U.S. nonprofit endowments combined probably exceed \$1 trillion, sloshing around America's stock, bond, and real estate markets. And observers see more coming, if high-asset baby boomers, as expected, pour tens of billions more into personalized foundations designed to cure specific ills at home and abroad.

America's nonprofit sector is now so large, and hosts so many well-feathered nests, that academic programs are being built around the subject. A slew of university centers are devoted to the study of nonprofits and philanthropy, scores of graduate schools, including leading business schools, now offer concentrations in nonprofit management,

and in 2004 Indiana University launched a Ph.D. program in philanthropic studies.

And the United States is leading the way. Only a few small countries have a greater share of their workforces in paid employment at nonprofits. And none matches this country in terms of assets. This is partly because "European countries do not offer comparable tax benefits" for charitable donations, points out Tyler Cowen, an economist at George Mason University. Compared with charity-favoring U.S. laws, European rules often offer donors complicated, few, or even no tax deductions, and make foundations very labor-intensive to create and then difficult to run under state supervision. Higher tax-takes may also mean that Europeans amass less of the private wealth that is the basis of most philanthropy.

Whatever the reason, Europeans make donations, for example, to their alma maters at what Americans would consider very low rates. So it's not surprising that most European universities have few assets. Cambridge and Oxford are standouts for their American-style endowments of around £4 billion each. But the U.K.'s other universities lag far behind, with only a handful having as much as \$150 million in recent years. That means that Phillips Exeter boarding school has a larger endowment than more than half a dozen leading British universities combined. And many continental universities don't have endowments to speak of at all. It's no coincidence that some European nonprofits like British universities and museums come to the United States in search of donors.

We can tell a similar story about foundations. Europe has a number of sizable foundations, especially in Germany, where the 15 largest private (often corporate) foundations have combined assets of about \$23 billion—about the size of two Ford Foundations—in addition to religious charities. But foundations are anemic in rich countries like France and Italy. Throughout Europe, it is government that funds the vast bulk of education, health care, research, and culture. For that matter, Japan has the world's second-largest economy, with about 37 percent of America's gross domestic product. But at the start of this decade, the 20 largest Japanese foundations had only around 3 percent of the assets of the 20 largest American ones.

You might expect Americans to cheer the growth of their nonprofits, since they reflect American generosity and may transform society in do-good directions. Yet the growth of nonprofits has caused extensive unease. Radicals on the left have long feared that foundations, for example, prop up capitalism by mitigating its worst effects. And even many conservatives, otherwise famous for championing voluntarism and the mediating institutions of civil

society, are worried that the nonprofit sector may be turning out to be more vicious than virtuous. This concern is encapsulated in the law formulated by John O'Sullivan when he was editor of *National Review*: "All organizations that are not actually right-wing will over time become left-wing." In this view, nonprofits gravitate through the years to agendas not only that their original donors never intended but that are unrepresentative of American society. And then they are immune to reform.

Nowhere is this clearer than with foundations whose endowments let them operate in perpetuity. After the original donor departs the scene, foundations can be taken over by professional staffs who literally have a blank check with which to pursue their own agendas. These staffers don't have to answer to dues-payers or even donors, and they help select their boards of directors and then their own replacements. As scholar Kenneth Prewitt puts it, an endowed foundation is "perhaps unique in its distance from any accountability mechanism: no shareholders, no customers, no voters, no dues-paying members, no clients who can withhold contributions or support."

Conservatives' favorite example is the Ford Foundation, which came to pursue agendas that Henry Ford would have found repugnant and which several of his descendants criticized to no avail. The Manhattan Institute's Heather Mac Donald has chronicled how the Ford staff, priding themselves on subverting America's inadequacies, funded projects that urged "marginalized" Americans to seek solutions to their problems through government assistance and identity politics rather than through self-reliance and in their local communities. These efforts may well have encouraged new forms of economic, political, and cultural segregation that ultimately hurt those they were meant to help.

Agendas like these have placed Ford outside the mainstream, which is why it's so difficult to imagine a Ford Foundation president serving today at the highest reaches even of a Democratic administration, in the way that Ford's McGeorge Bundy or the Carnegie Corporation's John Gardner did in the 1960s. But there are no mechanisms to prevent senior staffers at foundations like Ford from using "their position at the intersection of the elite worlds of government, politics, academia and the press to remake America in their own progressive image," or at least to try to.

Much the same can be said about universities. Almost all faculties dramatically underrepresent conservative and especially social-conservative beliefs. The most obvious result is a liberal-leaning climate on the campuses that educate the next generation of America's professionals. Another result is that a solidly middle- and even upper-middle-class professoriate has become a notable donor base for progressive political causes. The Center for Responsive Politics

reports that employees of universities and other educational institutions gave over \$36 million to all presidential campaigns in 2004, almost 80 percent of it to Democrats. That year, Harvard and the University of California system were the top two institutions in terms of employee per capita contributions to John Kerry. Faculties serve as an institutional base for what passes as radicalism these days. Cranks on the right have to wait until they get home from work to chase Vincent Foster's real killers. But the Scholars for 9/11 Truth can make conspiracy-theorizing and activism part of their job descriptions.

As with foundations, the unrepresentativeness of campuses may be permanent, because tenured professors select their own replacements and universities rival foundations in their insulation from outside pressures. Not only do elite universities have large endowments, but they aren't even especially responsive to donors, because what college fundraisers do best is commodify nostalgia for what campus-life was like 40 years earlier, rather than "selling" their school's current practices. Given the size and complexity of modern universities, even careful donors would find it difficult to detect the Ward Churchills they've never heard of. The result is that universities end up using donated money for things that both earlier and many ongoing donors would be disgusted with.

Similar criticisms are directed at nonprofits that are ostensibly more susceptible to pressure. Many nonprofits are technically membership organizations, but their professional staffs are often as insulated from members' opinions as corporate CEOs are from average stockholders. And many social services nonprofits get most of their funding from government, which makes them even more prone to politicization. Instead of acting as a bulwark of civil society, these nonprofits often press for ever more government spending.

Of course, there are grounds for skepticism about the most outsized charges leveled against "nonprofits gone wild." After all, the multiculturalism, balkanizing ethnic and gender studies programs, and other developments often attributed to the long arm of the Ford Foundation are if anything even stronger in Europe, where such foundations are weak or absent. Moreover, there is every reason to assume that one of the main criticisms of governments—that a lack of incentives makes them inefficient and often ineffective—applies just as much to nonprofits.

Still, it is hard to deny that the New Left's long march through our national institutions landed it in firm control of the one sector that's exempt from the discipline of both the marketplace and the polling booth, and it is using this power to try to turn us into Sweden by stealth. And if anything, the situation stands to get worse. Remember those graduate school programs in philanthropic studies? It is universities, of all unbiased places, that are in charge of

training the people who will staff the growing nonprofit sector down the road.

Concerns like these have inspired calls for political oversight of nonprofits. Some continue to come from the left. When Warren Buffett added his billions to the Gates Foundation, Elizabeth Boris of the Urban Institute wondered “whether or not the equivalent of \$60 billion in assets invested in decision-making by three people is good for society. Any three people.” Rick Cohen, then of the liberal National Committee for Responsive Philanthropy, insisted that “when the money is in the Gates Foundation . . . it is money that we have entrusted that foundation to use in the public interest.”

But the most intense skepticism toward America’s emerging nonprofit industrial complex is coming from conservatives and libertarians, who normally champion civil society. Some are trying to use publicity to pressure for reform. Daniel Klein and other scholars have researched the partisan orientations of university professors and disseminated the predictable results. The American Enterprise Institute and the Federalist Society launched an “NGO Watch” website in response to the “fast and often unchecked growth” of the nonprofit sector. The Capital Research Center tracks and publicizes political bias in foundations and other nonprofits. Some have tried to organize donors and trustees to pressure universities into becoming more politically representative. The Robertson Foundation is even suing Princeton to retrieve millions of dollars from an endowment that they say is misused.

But perhaps inevitably, some are pressing for political intervention. David Horowitz aims to deliver more political balance through an “academic bill of rights,” which he threatens to impose on state universities through the legislative process if necessary. Some have considered legally forcing all foundations to “sunset”—i.e., eventually give away all their assets—rather than exist in perpetuity, to avoid their eventual capture by unrepresentative professional staffers. Last June, Republican state representative Bill Huizenga cosponsored a bill in the Michigan state house that would oblige foundation boards to follow the intent of original donors. To be sure, Horowitz is targeting only public universities, since that’s where legislatures have leverage. But these are all attempts to use political means to rein in highly unrepresentative but powerful nonprofits that seem beyond the reach of any other means of control.

Concerned conservatives could even decide that what some liberals think is good for the foundation goose might be good for the university gander. After all, Harvard’s \$29 billion endowment is in effect a massive foundation that is basically controlled by the self-selecting members of the

not-at-all-transparent Harvard Corporation, whose names even most Harvard alums don’t know and who are much less known to the public than Bill and Melinda Gates and Warren Buffett. (They are: professors Derek Bok, Patricia King, and Nannerl Keohane; businessmen James Houghton, James Rothenberg, and Robert Rubin; and the Urban Institute’s own president, Robert Reischauer.) Maybe the political process should have a say in college endowments?

But calls for political intervention should sound serious alarms. The only sector we make fully accountable to the political process is government itself. It is the unique risks posed by government’s coercive monopoly that justify subjecting it to the very costly and inefficient discipline of elected politicians and, behind them, a sovereign electorate “whose vocabulary is limited to two words, ‘Yes’ and ‘No,’” as political scientist E.E. Schattschneider once put it.

By contrast, the for-profit economy is unthreatening even without political “accountability,” because its power is diffused among scores of millions of people who are under the relentless pressure of mutual competition. Forced to attract their customers anew every week, quarter, or year, businesses have to be responsive and constantly innovate. This creates a climate of dynamism in which no one entity or agenda can gain a hegemonic position from which to threaten everyone else.

The same things—pluralism, competition, change, and dynamism—are what make political intervention unnecessary in America’s nonprofit sector. New nonprofits arise, old ones disappear, and many that survive do so by adapting to changing circumstances, including to the changing tastes of a shifting cast of donors. And the nonprofit sector remains startlingly permeable and diverse. Numerous progressive institutions are accompanied by many centrist and conservative ones, both secular and religious. Not surprisingly, the most promising efforts aimed at making universities more politically balanced are emerging from elsewhere within the nonprofit sector.

But most of the change in the nonprofit sector comes from the waves of creative construction surging outward from America’s dynamic economy. More than anything, this will keep shaking things up even for the nonprofits that seem the most insulated from change. For one thing, money made in the marketplace is constantly creating new nonprofits. The Foundation Center reports that of the foundations that either had assets of at least \$1 million or gave away at least \$100,000 in 2004, a fifth were launched in the 1980s and fully half created since 1990. This includes some behemoths. The Gates Foundation was created only in 2000, and its annual giving—even before Buffett’s massive contribution—is already beginning to rival Sweden’s annual foreign aid. Yet the United States “is such a charitable country that even with Buffett’s billions, the Gates Foundation will still

account for only 1 percent of American charitable giving,” points out Adam Meyerson, president of the Philanthropy Roundtable. This leads Meyerson to venture the prediction that “20 years from now, Gates will not be America’s largest foundation.” The point is that not even the best-endowed foundations have guaranteed influence or status. We can’t foresee the content of the coming American philanthropic wave, any more than we’ve been able to predict the direction of America’s innovative economy.

Just as important, for-profit firms have discovered ways to do business in areas in which nonprofits once grew fat and lazy. Consider health care and education, traditionally the two largest sectors of nonprofit activity. Nonprofit hospitals decisively surpassed their for-profit competitors by the middle of the 20th century. But these nonprofits became increasingly dependent on private markets for capital, and a number converted to for-profit status in the 1980s and mid-1990s. For-profit hospitals have been gradually clawing their way back, initially at the expense of direct government provisioning. From 1975 to 2003, the for-profit sector has grown from 7.8 percent of beds in community hospitals to 14 percent, as the local, state, and especially federal government shares shrank and the nonprofit share merely held steady. Nonprofit hospitals are looking over their shoulders, and prosper only by reforming and innovating.

For-profit growth is even more dramatic in health insurance. In years past, mainline insurers like Blue Cross/Blue Shield and the early health maintenance organizations (HMOs) were nonprofits. But for-profits became powerful HMO players in the 1980s. And mutual and nonprofit insurers began a wave of conversions to for-profit status, despite frequently having to pay the price of placing sizable assets into “health legacy foundations.” In 1994, Blue Cross/Blue Shield allowed for-profits to become member plans for the first time. By 2002, Blue plans had converted to for-profit status in over a dozen states, including California and New York, many of which then merged into WellPoint, Inc.

Trends in education are nearly as dramatic. Those of us who grew up with television ads for the New England Tractor Trailer Training School tend to think of for-profit education as a very modest affair. Not any more. Three-quarters of a million students and tens of thousands of full- and part-time faculty can now be found enrolled and employed in the (mostly U.S.-based) programs of America’s seven largest for-profit higher education companies: ITT Educational Services, Laureate Education, Career Education, DeVry, Strayer, Corinthian Colleges, and the market-leading Apollo Group, which owns the University of Phoenix. These companies are directly competing with community colleges and now better schools by offering price-competitive degrees and aggressive job placement in business management, education, health care, technology, and human resources. The point is not that

Strayer will soon go head to head with Princeton. It’s that colleges being challenged by the for-profits can’t afford to be complacent and are having to implement reforms that will likely ripple upward. The for-profits might even offer some political diversity to the education sector. The Center for Responsive Politics reports that while employees of many traditional universities regularly give 90-95 percent of their contributions to Democratic candidates, in the 2006 elections, the employees and corporate PACs of the Apollo Group gave a majority of their contributions to Republicans, while at Corinthian Colleges, the breakdown was only 60 percent to 40 percent in favor of Democrats.

Structural changes like these in health and education may help explain why nonprofit employment seems to be leveling off. At least as measured by jobs in membership associations and organizations, employment in nonprofits through the 1990s grew faster than job growth in either government or the for-profit sector. But it then plateaued and has grown more slowly, possibly substantially so, than total employment between 2003 and now.

America’s economy is so dynamic that it can humble even huge endowments. In only a decade of public trading, the Apollo Group has achieved a market capitalization of \$7.54 billion, more than a quarter the value of Harvard’s endowment. The combined market capitalization of the seven for-profit higher-education companies listed earlier currently stands at \$22 billion, more than Princeton and MIT’s endowments put together. And this doesn’t include billions more in value in a privately held firm like Education Management Corporation. In other words, America’s most venerable nonprofits are being given a serious run for their endowment money by a for-profit sector that virtually no one saw coming just 15 years ago.

The combination of economic growth and proliferating new nonprofit groups means that the weight even of the very largest nonprofits is very limited and can easily decline over time. For example, the Ford Foundation’s annual giving hasn’t risen but instead *fallen* as a share of America’s gross domestic product, to about one-third of what it was in 1960, and around two-fifths of what it was in 1968, when Ford was at the height of its supposed culture-subverting power.

Of course, the story is very different in developing countries. There, scores of politicized nongovernmental organizations funded by Ford and other Western foundations can distort the local political, activist, and media scene in ways that weak local economies and civil societies cannot easily resist. But in America, the creativity and resilience of civil society in general and the profit-making economy in particular ensure that the nonprofit industrial complex adds to, and doesn’t endanger, our national life. One more reason maintaining economic dynamism should be one of our highest priorities. ♦