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**“North-American philanthropy, the other side of the coin”**

Research Paper by  
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**Abstract**

North American philanthropic ventures collect donations for the needy or suffering. Few studies have analysed philanthropic ventures and altruistic promoters. In the philanthropic industry, donors mandate intermediaries (agents) to transfer donations to beneficiaries. One of the underlying assumptions of agency theory is that agents attempt to maximize their personal welfare and compensation; this behaviour may not always be in the best interests of beneficiaries. What is the malevolent business model of a philanthropic organization? Is there a monitoring process? What is the social return on investment? The complex patterns of inter-stakeholder relationships, both good and bad, are scrutinized. The research, funded by the Autorité des marchés financiers (Canadian authority on fraud and money laundering), threads it way into the ‘complexity code’ of philanthropy via archival data and forensic science data. The paper also deciphers the altruism of agents via a new behavioural matrix. To conclude, a complexity-aware monitoring process is submitted. Thus, the research sheds new light on the complexity of philanthropic ventures and proposes directions for future research.

**Keywords:** charities, altruism, governance, agency theory, business model, monitoring, traceability of funds, fraud

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## **Introduction**

Over a million North American charity ventures collect donations in the name of cancer patients, dying children, homeless veterans, food banks, earthquake victims and the like. Charities are a major economic and social force that contributes to society through the active engagement of citizens. So far, few studies have analysed malevolent charities and taxshelter promoters. Darwinian biologist Dr Michael T. Ghiselin, currently Senior Research Fellow at the California Academy of Sciences and co-Editor of the *Journal of Bioeconomics*, had cutting remarks for charity and altruism: ‘No hint of genuine charity ameliorates our vision of society, once sentimentalism has been laid aside. What passes for cooperation turns out to be a mixture of opportunism and exploitation - Scratch an altruist, and watch a hypocrite bleed’ (Ghiselin 1974: 247). Professor Michael Porter, from Harvard Business School, also reacted strongly in *The Economist’s* ‘Special Report: Wealth and Philanthropy’ (Anon 2006): ‘Foundation scandals tend to be about pay and perks, but the real scandal is how much money is pissed away on activities that have no impact. Billions are wasted on ineffective philanthropy.’ The latest *Washington Post’s* top story (June 4 2015) sheds light on the other side of the coin: “The Red Cross had \$500 million in Haitian relief money, but it built just 6 houses”. One of the most pressing philanthropic research issues in North America is the need to understand the complex structures, processes and practices inside charities, with a special focus on the behaviour of agents who manage over a trillion dollars a year.

## **Purpose statement**

The paper’s first challenge is to encapsulate key elements of the institutional complexity of philanthropy despite the opacity of the industry. A new model will describe the means by which philanthropic ventures create, deliver and capture value for some stakeholders – in economic, social, cultural or some other form. Philanthropic business models range from grant-dependent non-profits to commercially viable for-profits. Competitive rivalry within the ‘charity’ industry brings innovative, aggressive and amoral stratagems to a trillion dollar arena. A second focal point, the analysis of the complexity of agents, will help to demystify profiles of social promoters and explain how greedy agents fall off the pedestal of altruism. In the industry, donors mandate intermediaries (agents) to transfer their donations to the needy or suffering. An underlying assumption of the agency theory is that agents attempt to maximize their personal welfare

and compensation; this behaviour may not always be in the best interests of the needy or suffering.

Concepts drawn from complexity theory offer new ways to monitor philanthropic governance retrospectively. A new version of the Stacey Complexity Diagram plots issues according to the level of agreement among stakeholders about the solution to social problem versus the amount of certainty that a given intervention will have the desired result. If there is a high level of agreement and a lot of certainty about an issue, the problems are simple, i.e., a right answer exists. When you move away from certainty and agreement, the issues become political, complicated and even chaotic. Solving the problems of the needy and suffering is usually in the zone of complexity or chaos.

The emergence of complex relationships between agents and three key stakeholders (donors, beneficiaries and regulators) is studied via a complexity-aware monitoring process. Donors provide funds to philanthropic organizations or agents; in return, the agents should be accountable to the donors. The form and degree of accountability may vary, depending on the mission of the organization. In principle, philanthropic ventures must provide services to the needy or suffering. There are many unanswered questions regarding the monitoring process; one objective is to observe whether the management (the agent) acts in the best interests of the donors and beneficiaries. One of the biggest challenges of the future is to measure the social return on investment of an agent's interventions (SROI). A critical question: should regulators be accountable for the traceability of funds and the social return on investment?

### **Terms and definitions**

Charity - For The Merriam-Webster Dictionary, charity is generosity and helpfulness especially toward the needy or suffering. A charity is also a non-profit organization that focuses on philanthropic goals combined with social value (charitable, educational, religious, or other activities serving the public interest). The terms and legal aspects of a charity vary according to country and, in some instances, the region of the country; for example, French Canada uses the term *bienfaisance* instead of charity.

Philanthropy – Etymologically, philanthropy (philos: loving and anthropos: humanity) means 'love of humanity' in the sense of caring, nourishing, developing and enhancing 'what it is to be human' on the part of both benefactors and beneficiaries. For the Merriam-Webster Dictionary, philanthropy is a desire to help mankind as indicated by acts of charity.

Altruism - The term altruism is described by The Merriam-Webster Dictionary as unselfish regard for or devotion to the welfare of others. In contrast, the Stanford Encyclopedia of Philosophy defines egoists as persons having but one ultimate aim: their own welfare. Donors and agents can have an impurely altruistic behaviour; alternatively they might give in to the temptation to act selfishly, and have a impurely selfish behaviour. (Andreoni 1989)

Philanthropy governance - The term 'governance' refers as the systems by which charitable organizations are directed, controlled and accountable (Cornforth 2003). The term 'accountability of an agent' involves a transfer of information in the sense that the agent is answerable to someone else. (Hyndman and McDonnel 2009)

Traceability of donations – This refers to the ability to track a specific piece of financial information by means of recorded data or an audit trail. Traceability in the 'industry' is also the ability to verify the history, location and utilization of all donations by means of recorded documents. Traceability is very difficult operation in the philanthropic sector (Stern, 2013)

### **Research methodology**

As academic knowledge on philanthropy continues to be relatively limited, we agree with Mintzberg (1979: 80), who states that: 'It seems far more important to research important topics with soft methodologies than marginal topics with elegant methodologies... most of the real insight has come from studies that used soft methodologies.' The qualitative approach was selected because of the constraints of the enigmatic and secretive culture of philanthropic organizations. Our research methodology is partly inspired by William of Baskerville's investigation methods (Umberto Eco's medieval franciscan friar):

- a) investigate the promoter, his altruism, the cause and the disciples;
- b) analyse the interaction embedded within the social network;
- c) deconstruct the sociocultural context.

From a methodological point of view, it is feasible to use a combination of exploratory and descriptive research to satisfy the research objectives. Such a multifaceted approach can, in many cases, transform a routine piece of research into an outstanding one. Exploratory research is most useful in the preliminary stages of a research project, when there is a lack of organizational transparency, and especially when subsidiaries are invisible in the Bailiwicks of Jersey and Guernsey. This type of

research gives a high degree of flexibility and a minimal amount of formal structure, the aim being to map out the boundaries of the environment of charitable organizations in North America, particularly in Canada.

Philanthropic ventures in the United States and Canada have similar structures, processes and practices (Salamon, Lester M. et al. 2013). Although the Université du Québec research team briefly reviewed the phenomena in the United States, most of the fieldwork was done in Canada, as the research team had privileged access to archives from the federal government in Ottawa and the Canada Revenue Agency. The research was based on qualitative observations through expanded retrieval. The basic data came from a 2013 report by the House of Commons Standing Committee on Finance entitled 'Tax Incentives for Charitable Giving in Canada'. The most valuable data came from the Standing Committee's Minutes of Proceedings rather than the report itself. More than 20 submissions to the Committee were also analysed.

Stimulating data from Johns Hopkins University reports on non-profits (Hall, Michael H. et al. 2006; Salamon, Lester M. et al. 2013) and information from the Canada Revenue Agency enriched our findings; other data came from the OECD's Report on Abuse of Charities for Money-Laundering and Tax Evasion (OECD 2009). The research team also relied on secondary research data, such as the review of available documents from Statistics Canada, as well as off-the-record discussions with donors, charity employees and civil servants. Targeted emails explored the transparency of some charitable organizations. Rich data was gained through in-depth analysis of six case studies of chaotic North American charities:

- Haiti's earthquake \$9 billion donations - Where is the money? (Ramachandran 2013)
- The \$3.2 billion in false tax receipts claimed by 100,000 by Canadian donors (Donovan 2007)
- Traceability of donations and manipulation of the breast cancer cause (Lacey 2012)
- Charity status of Al-Qaeda mosque questioned by FBI (de Pierrebouurg 2013)
- The \$100 million charity swindle: The U.S. Navy Veterans Association (Stern 2013)
- Ethics and the American Red Cross (McCarthy 2009)
- American Red Cross and Katrina hurricane (Stern 2013)

### **The agency theory**

The principal-agent relationship is defined by Jensen and Meckling (1976) as 'a contract under which one or more persons (the principal(s)) engage another person (the agent) to perform

some service on their behalf which involves delegating some decision making authority to the agent'. In a company, the board of directors represents the principals and the chief executive officer is the agent. In the philanthropy sector, the donors mandate an intermediary (the agent) to transfer their donations to the needy or suffering.

From an agency theory perspective, the role of the principal or governing board is to monitor the agent or the chief executive officer in order to direct financial resources toward the beneficiaries or users rather than diverting them toward management's interest and comfort. The underlying assumption of agency theory is that agents attempt to maximize their personal welfare and compensation, but must do so within the framework of increasing revenue. These actions may not always be in the best interests of the donors and the needy or suffering.

One aspect of the study is concerned with the complex relationship between the principal and the agent (Hyndman and McDonnell 2009). Donors mandate a philanthropic organization to forward donations to beneficiaries and users, with a regulator monitoring the process. A dilemma arises when the two parties have different interests and asymmetric information, such that donors cannot directly ensure that the agent is always acting in their best interests, particularly when activities that are useful to the beneficiaries are costly for the agent, or where elements of the agent's activities are costly or complex for the donors to observe (Hyndman and McDonnell 2009).

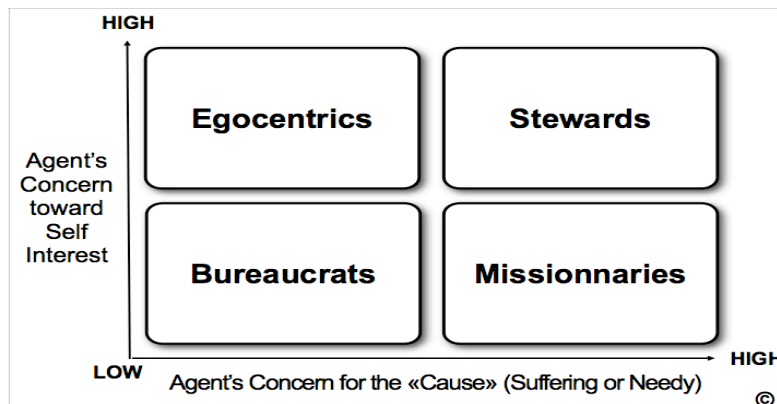
### **The agent: a complex individual**

The behavioural matrix shown in Figure 1 enables us to visualize four different styles of conduct. For pedagogical purpose, the research team narrowed the description of agent behaviour to two dimensions: consideration of the needy or suffering and concern for self-interest. The grid helps to explain how agents may fall off the pedestal of altruism. The model is represented as a matrix, with concern for self-interest as the vertical axis and concern for the cause (the needy or suffering) as the horizontal axis, each axis ranging from Low to High. The resulting four quadrants gave the following typology:

Bureaucrats or Clerks – Agents of this type have little concern for either clients or their own careers. They preserve their jobs and protect themselves by avoiding getting into trouble. They follow the rules and procedures. The main concern of this type of manager is to avoid being held responsible for any mistakes, which results in fewer innovative decisions and settling for the status quo.

Missionaries – They have high regard for the cause (often a religious or cult niche) and a low level of concern for salary and compensation. Salaries tend to be below average. These agents are on a mission, paying much attention to the needs of the suffering or the faith of disciples and the comfort of volunteers; some preachers can be considered as impure altruist. The resulting atmosphere is usually friendly, human and warm, but not necessarily productive. The team usually finds entrepreneurial solutions to improving the welfare of the needy.

**Figure 1: The Agent Behaviour Matrix**



Egocentrics – Having a high level of concern for their own comfort, they have no empathy for the needy; often sociopaths, they manipulate and exploit the volunteers. Having all the answers, they control the charity and do not tolerate opposition. They are Machiavellian, ‘the-ends-justify-the-means’ types, even to the point of making false tax receipts or creating umbrella subsidiaries. Opportunistic and narcissistic, they adore media exposure and the limelight. A signal to identify them: their salary must be higher than a prime minister or the President of the United States of America, they have a chauffeur, and they absolutely must travel first class. In Canada, more than 3,000 charity agents earn over CA\$160,000 a year.

Stewards – They have a high regard for beneficiaries and a high interest in the comfort of the members of the organization. Stewards are honest agents who contribute and commit themselves. Team leaders, they are pastor-figures who need followers. They are best characterized by a paternalistic style: they like to prescribe and guide. Considering themselves as patriarchs or matriarchs, they will always act in the best interests of the organization, meaning the volunteers and beneficiaries. They are always symbols of good governance.

### **Charities in the United States**

Charities and non-profit organizations have a significant presence in the economy of the United States. Non-profits represent more than 6 per cent of the gross domestic product, and the paid workforce makes up more than 7 per cent of the country's total workforce (John Hopkins University Report 2013). The main regulator is the Internal Revenue Service (IRS), which grants charities their tax-exempt status and can audit their financial filings. Once charities start raising money, monitoring is largely left to each state; it is very complex to identify the regulators in different states. In California, it is the Attorney General; in Florida, the Department of Agriculture and Consumer Affairs; and in Texas, two departments enforce three different statutes that apply to different types of charities. Rules vary from state to state and are very hard to follow. The IRS approves more than 99.5 per cent of all applications for charitable status, creating more than 50,000 new charities each year. Once a non-profit is started, the IRS and state regulators exert negligible oversight; even charities exposed as scams can be nearly impossible to shut down (Clyne 2013).

According to the National Center for Charitable Statistics, there are 1,406,820 tax-exempt organizations in the United States, including 945,415 public charities. In 2011, public charities reported over US\$1.59 trillion in total revenues and US\$1.49 trillion in total expenses. Twenty-two per cent of the revenue came from contributions, gifts and government grants, 72 per cent from program service revenues, which include government fees and contracts, and 6 per cent from other sources, including dues, rental income, special event income and gains or losses from goods sold. Public charities reported US\$2.87 trillion in total assets in 2011. The latest Charity Navigator Study shows that over fifteen charity managers (agents) across the United States of America command annual salaries of over a million dollars; the president of United Way earns US\$1.5 million a year. An important salary benchmark in North America is the salary of the the Governor of the State of New York ( Chief executive of the U.S. state of New York; the governor is the head of the executive branch of New York's state government and the commander-in-chief of the state's military and naval forces. ). Governor Cuomo earns US\$179,000 a year.

The Tampa Bay Times and CNN allege that lack of regulation and insignificant penalties allow malevolent charities to flourish. The Center for Investigative Reporting spent a year identifying the 50 'worst charities' in the United States. Over the past decade, the 'worst charities' generated more than US\$1.3 billion in donations, about 75 per cent of which went to pay the charity agents and solicitors who raise the money



(Taggart and Hundley 2013). *Business Week* (2014) discovered that TGS, a charity with 200 subsidiaries is hiding US\$13 billion. Technology also allows scam artists to be magicians. The FBI has estimated that after Hurricane Katrina, 2,400 fake charity websites were set up to relieve the needy or suffering (Stern 2013).

According to the New York Times, it is very complex to identify which charities are trustworthy: 'There are approximately 60,000 charities in this country with the word 'veterans' in their names. Only a few specialists can claim the expertise to say which are the best, let alone which are trustworthy.' (Stern 2013). The Université du Québec research team on charities identified over 50,000 charitable organizations in the United States and Canada with the word 'Cancer' or 'AIDS' in their names : a real labyrinth, where the main beneficiaries are often the charity's for-profit fundraisers.

### **Charities in Canada**

A Johns Hopkins University research group conducted a major study on the non-profit sector in 37 countries (Hall, Michael H. et al. 2005). Canada's charity sector represents an amalgam between the European welfare partnership model and the Anglo-Saxon model, where there is stronger volunteer and private philanthropic support. The latest Johns Hopkins University report (Salamon, Lester M. et al. 2013) confirms that Canada has one of the largest, most vibrant non-profit and voluntary sectors in the world. The sector represented CA\$223 billion in revenue and a total of CA\$215 billion in expenditures in 2012, making it larger than the automotive or manufacturing industries. A revelation: the top 1 per cent of charitable organizations command 60 per cent of all revenues.

Donors play an important role, but the most important revenue source is government grants. There are an estimated 185,000 non-profits and charities in Canada, half of which are run entirely by volunteers. The Canada Revenue Agency confirmed that 86,000 charities were registered as of January 2013, with 90 per cent of them classified as charitable organizations (40 per cent of charity missions are cult related). Smaller provinces have a higher number of organizations relative to their populations. The Report of the Standing Committee on Finance (2013) highlighted that in December 2011, registered charities reported having 1,307,565 permanent full-time positions (8 per cent of the total labour force) and 1,882,522 part-time positions.

- Some of Canada's largest and best-known charities are paying their top officials generous annual salaries. Government filings show that 3,000 individuals earned more than

CA\$160,000. An important salary benchmarking tool in Quebec is the premier's salary, which is CA\$175,000 (university professor with a Ph.D. earns CA\$90,000). The Palme d'Or goes to the former chief executive officer of ORNGE (a nonprofit air ambulance charity) receiving with a total of CA\$9.5 million salary over a six year period. Small charities, comparably efficient to large charities, have more realistic salaries. The Human Council for the Non-Profit Sector provides interesting data on the salaries of small charities: overall, almost two-thirds of employees of small charities make less than CA\$40,000 per year. The province of Quebec has the lowest average compensation cost per full-time employee, with CA\$33,207, and the Northwest Territories has the highest, with CA\$48,610. With competitive rivalry within the charity industry and barriers to entry, small local charities must have innovative and aggressive stratagems to access the CA\$200 billion arena.

Fiscal aspect – The competitive advantage for a charity doing business in Canada is the fact that the country has the most generous tax incentive system in the world. The most important benefit is the ability to issue official donation receipts. A Canadian specialist on charity law and philanthropy explains the system as follows: 'The ability to issue a tax receipt is almost like having a license to print money. If a donor makes a donation of CA\$1,000,000 and a charity issues a receipt for CA\$1,000,000, the value of that tiny little piece of paper that takes minutes to produce is CA\$460,000.' (Blumberg 2011) The Canadian Revenue Agency informed the House of Commons Standing Committee on Finance that, on average, only 1 per cent of all registered charities are audited each year, and that for the 2010-2011 fiscal year, with only 751 charity audits conducted, 635 charities had their status revoke for failure to file an annual return.

Schemes and scams - Along with lawyers and stock brokers, charities' agents invented a complex 'legal' stratagem via a creative 'Triple-dipping tax shelter', using flow-through share donations where taxpayers and governments take 100 per cent of the risks, creating a 'win-win-win-win' situation for donors, charities, brokers and lawyers (Mackenzie Tax & Estate Planning 2006). Some other promoters have created illegal tax shelters that provide a tax receipt for an amount larger than the cash investment of the donor-investor. As of March 31st, 2014, there had been approximately 200,000 Canadian donors involved in a traffic of tax shelters. The CRA has denied more than \$CA6.3 billion in donation claims and reassessed over 190,000 taxpayers who participated in the traffic of donation receipts. The CRA also gave CA\$162 million in third-party penalties against

the promoters and tax professionals involved. The following examples are typical Canadian donation schemes where taxpayers receive an official donation tax receipt that is higher than the actual cash disbursed, thus 'profiting' from the donation.

- A donor gives CA\$3,000 cash to a charity and then "receives" property (art, photography, medicines, software, etc.) with a false market value of CA\$7,000 from a trust. The property from the trust is then donated to the charity. The donor receives a CA\$10,000 donation receipt, which is then claimed on their income tax return. The donor never takes possession of the property.
- A donor borrows CA\$8,000 (from a firm involved in the scheme) to donate to a charity and donates CA\$2,000 out of his pocket to the charity and receives a CA\$10,000 donation receipt. There is usually no expectation that the "loan" be repaid.
- A donor buys property for CA\$3,000 and donates it at an inflated "fair market value" of CA\$10,000. The donor receives a CA\$10,000 donation receipt but never takes possession of the property.
- A 'Pump and Dump' scheme : A group of investors take control of a 'penny stock' at \$0.10 a share. With the help of stock brokers, the 'penny stock' is 'pushed' at a value \$2 a share. The investors give the shares to a charity at a value of \$2 in exchange of donation receipts. The deal done, the 'penny stock' comes back to \$0.10 a share.

Transparency – Some charities, with the help of lawyers, are very creative in setting up complex structures. The Minutes of Proceedings of the House of Commons Standing Committee on Finance revealed the case of ORNGE, a health charity of Toronto, that spent CA\$11 million on legal fees to set up complex structures of fifteen underground business units (for-profits and non-profits) that largely deal with barriers to the audit trail and traceability of donations. Another suspicious behaviour: some charity agents are serial entrepreneurs and control over ten charities at the same time (Standing Committee on Finance 2013). For donors and regulators, there is a traceability issue in following donation money through the delivery chain to beneficiaries. It is also very difficult to access charities' financial statements. There is a major incongruity in the monitoring system: the confidentiality provisions of the Canadian Income Tax Act prohibit the Canada Revenue Agency from informing the police or the public of a criminal act or fraud. Donors do not have a clue as to the honesty of the charity soliciting money, and will never know the names of the charities and the Canadian agents involved in the CA\$6 billion fraud.

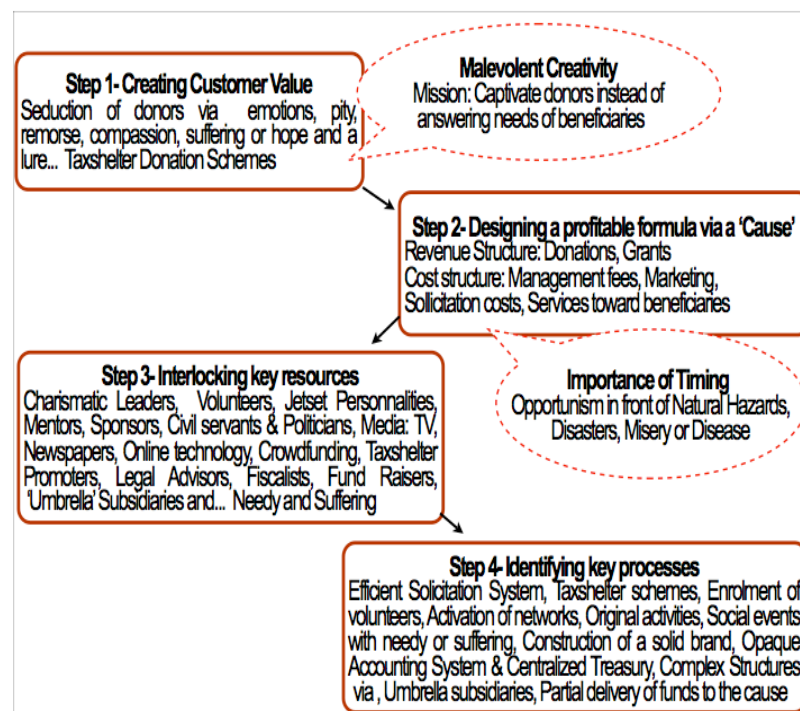
Confidence in charities – The 2014 Bank of Montreal's BMO Philanthropy Report released that there is a widening trust gap between donors and charities. In the BMO survey, 43 per

cent of donors said they fear a charity would not use the money wisely. Furthermore, the BMO Report says that donors want to know how charities spend their money and see the social impact of their activities.

### Cracking the code of a malevolent charity business model

The business model shown in Figure 2 consists of four interlocking elements that create and deliver value for some stakeholders. The business model is ‘amoral’, showing no concern for whether behaviour is morally right or wrong.

Figure 2 The Malevolent Charity Business Model



Customer value proposition – The first step of charitable organization is to create a customer value proposition. In the charity sector, there is a paradox: the strategic clients are not those the charity is set up to help (the needy or suffering). The real clients are the donors. A malevolent charity is one that has found a way to create value for the donors, the promoters and the management team. Once a charity has understood that donors are ‘impure altruists’ imbued with a complex mix of intrinsic emotions and social emotions such as shame, guilt, embarrassment, pride, recognition, pity and ‘warm glow’, the charitable organization is able to prepare, with taxshelter promoters, a customer value proposition with a lure: generous tax incentives.

Profitable formula – The second step, the profitable formula, is the blueprint that defines how a charity creates value for itself while providing value to the donors. It consists of the following formula: revenues come from donors and grants or subsidies from local, regional or national governments. The cost structure is predominantly driven by opportunistic timing (natural hazards or disasters) and marketing costs, especially solicitation and lobbying costs, taxshelter promoter commissions). Depending on logistics, entrepreneurial charities can achieve strong margins.

Key resources – The third step is to identify key resources, which are assets such as the people, technology, facilities, channels and brands required to deliver the value proposition to the targeted donors. The aim is to interlock the key resources: charismatic leaders, notables, major business sponsors, sport and show-business personalities, politicians and civil servants, the media and a solid team of fundraisers (needy persons are utilized to promote the cause), clever lawyers and accountants.

Key processes – Finally, malevolent charities design complex operational and managerial processes that allow them to deliver value in such a way as to successfully repeat their activities and increase revenues year after year – including recurrent social activities. Entrepreneurial charities can be very creative when it comes time to seduce donors, especially via online giving and viral marketing (such as the ‘Ice Bucket Challenge’ or ‘Fighting prostate cancer with a mustache’). Some multinational charities have also a complex legal structure and an opaque accounting system, making it impossible to measure the efficiency of their philanthropic activities.

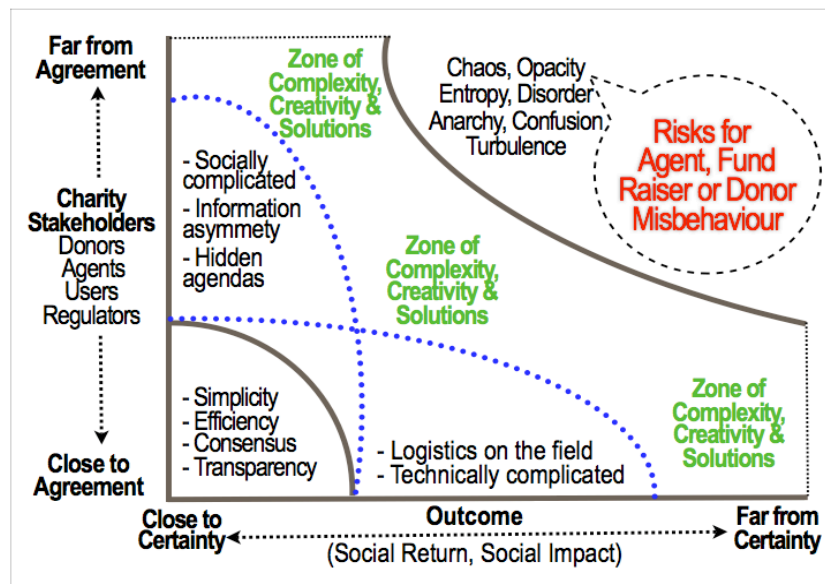
### **Understanding the complexity of charities**

Concepts drawn from complexity theories offer new ways to monitor the behaviour of charities. The Stacey Diagram (1996) plots issues according to the level of agreement among stakeholders about the solution to a problem versus the amount of certainty that a given intervention will have the desired result. If there is a lot of agreement and a lot of certainty about an issue, the problems are simple, i.e., a right answer exists. Moving away from certainty and agreement, the issues become political, complicated or even chaotic. Solving the problems of the needy or suffering is usually in the zone of complexity or chaos.

Since 2000, professor Ralph Stacey has taken a different course, moving away from organizations as systems toward patterns of interpersonal relationships, both good and bad (complex processes of interactions, power relations, ideologies,

choices and intentions). What happens is the emergence of the uncertainty and unpredictability of human life. An advisor to the Université du Québec research team on the utility of the complexity matrix, Professor Stacey had the following comments in 2013: ‘I suppose the diagram could be useful depending on just how it would be used. I have more sympathy for instruments like the diagram being used retrospectively to analyse what happened than I am to their use for deciding what to do in the future.’

**Figure 3 Understanding Charities via Stacey’s Diagram**



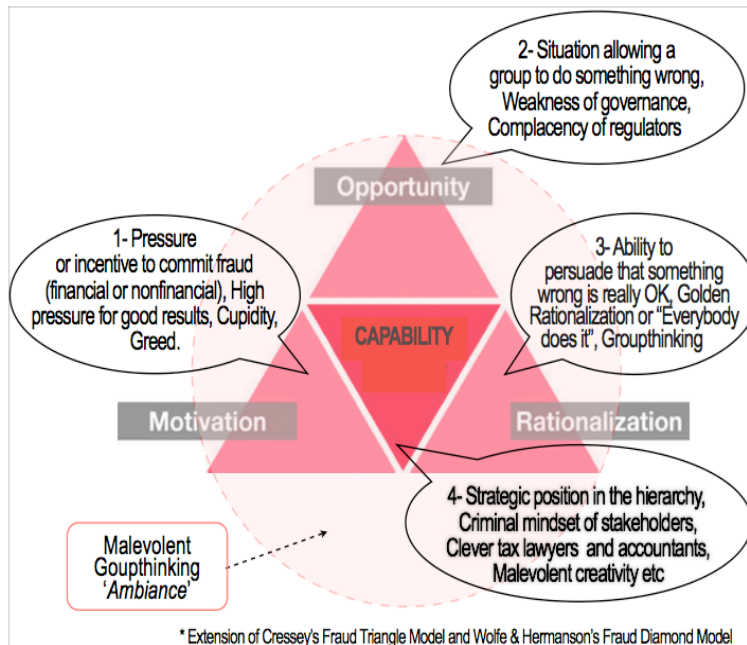
The horizontal axis of the extension of the Stacey Diagram indicates movement from situations close to certainty to situations far from certainty, while the vertical axis indicates movement from situations in which people are close to agreement with each other to situations in which they are far from agreement with each other, as indicated in Figure 3. In conditions close to certainty and agreement, it is possible and useful to use the standard monitoring tools. In intermediate situations ‘close to certainty but where there is a high degree of disagreement’ or in conditions ‘close to agreement but some way away from certainty’, innovative monitoring techniques are required (Britt 2013). In conditions ‘very far from certainty and agreement’ (chaos, anarchy and misbehaviour), standard monitoring tools and techniques cannot be used. Complex aspects of a situation cannot be known ahead of time. In general, social impacts of charity interventions tend to contain a mix of complicated and complex aspects. These cause-effect

relationships emerge only retrospectively.

### Charity Fraud, a Team Work

Concepts drawn from the Fraud Triangle Theory (Cressey 1953) and the Diamond Fraud Theory offer new ways to understand the malevolent behaviour of charities. Usually, the scheme is a team work of 'creative malevolent' professionals.

**Figure 4 : Charity Fraud, a Team Work**



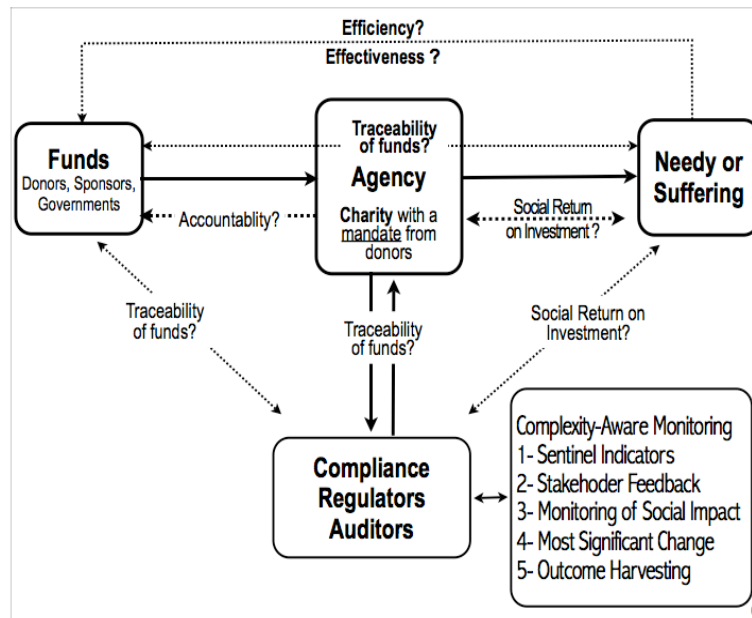
Using the four-element the fraud diamond developed by Wolfe and Hermanson (2004), it is easier to understand the 'schemes & scams'. The malevolent team's thought process might proceed as follows (Figure 4):

- 1- Incentive or motivation to commit fraud : high pressure for results, greed, cupidity, personal problems;
- 2- Opportunity structure or weakness in the system that the team exploit : weak governance, complacency of regulators, weak internal control, generous tax shelters;
- 3- Rationalization : wrong for others but OK for us, everybody does it, groupthinking;
- 4- Capability of the team: positions at top-management levels, necessary traits and abilities to be the right group to pull it off, strategic position of stakeholders, clever tax lawyers and fiscalists, malevolent creativity of the team.

### Interrogating the monitoring process

The emergence of complex relationships between agents (the charity) and four key stakeholders (taxshelter promoters, donors, beneficiaries and regulators) is described in Figure 5.

**Figure 5: Toward a Malevolent-Aware Monitoring Process**



Donors provide funds to the charities, or agents. In return, the agents should be accountable to regulators, the beneficiaries and the donors. The form and degree of accountability may vary, depending on the mission of the organization. In principle, charities must provide services to the needy or suffering. Although they are under no obligation to do so, charities may make themselves accountable to users by, for instance, having user representatives on their boards. Alternatively, charities may solicit user feedback on the level and quality of service provision. As beneficiaries receive services and have the right to be involved in decisions that affect their daily lives, their involvement might provide management with valuable knowledge on service provision effectiveness. Many board and management members express resistance towards having beneficiaries or their representatives on their boards or at general meetings; expertise representativeness issues are offered as an explanation for this resistance. Charities are also forced to comply with government legislation that often involves reports to a special regulator, with the regulator's power varying from one jurisdiction to the next. In return, charities benefit from tax



exemptions. Usually, charities must produce annual reports and other information, as well as being subject to further investigation if the regulator deems it necessary. (Note that Canadian regulators only audit 1 per cent of charities each year). There are many unanswered questions regarding the monitoring process; one objective is to observe whether the charity's management (the agent) acts in the best interests of the beneficiaries and the donors. One of the biggest challenges of the future is to measure the social return on investment (SROI) of an agent's interventions. A typical complex impurely altruistic dilemma: a Toronto food bank for sick kids where directors of a board, often co-opted by the agent, must respond to the agent's annual salary of CA\$350,000. Is he worth that amount, or would the donation money be better spent on food for the needy or suffering?

USAID (Britt 2013) recommends five approaches for complexity-aware monitoring:

- Sentinal indicators - indicators are placed at critical points in a system map to monitor the relationship between the project and the context;
- Stakeholder feedback - monitoring approaches are developed to receive data from the field (citizen reports, community scorecards, user surveys);
- Process monitoring of social impacts - identifies processes relevant for the achievement of results or impacts;
- Most significant change - consist of the collection and analysis of stories from beneficiaries and users describing the most important project outcomes;
- Outcome harvesting - monitors projects backward via forensic investigation to establish a cause-effect explanation of how and why the project did or did not contribute to social improvement.

## **Conclusion**

The research team's first challenge was to encapsulate the ingredients of a theoretical malevolent business model despite the opacity of the charity sector. The model provides a better understanding of the complex structures, processes and practices of delinquent charitable organizations. The research paper cast a new light on the interactions among donors, agents, regulators and beneficiaries. A managerial matrix describing the altruistic charity promoter versus the narcissistic charity promoter was also developed to better understand the behaviour and motivations of social promoters.

The researcher has a plethora of new research avenues: How do charities create value and what is the social impact of donations? Who are the principals in a non-profit charitable organization? Why are the regulators so indulgent with delinquent charities? Should the state assign forensic accountants a more important role? How can we monitor digital giving and crowdfunding methods?

The main focus of the article has been the description of a malevolent charity business model. One question worth considering at this stage is whether this model can be generalized in other countries. One way to test this would be to analyse malevolent charity operations in emergent countries. Another important follow-up research question relates to the governance of funds: in-depth organizational case studies based on interviews of boards of directors could be an effective alternative method for assessing field interventions and measuring the social impact of donations. A candid question: Should beneficiaries or users be involved in the measurement of the efficiency and effectiveness of a charity's performance?

In the Tragedy of Hamlet, Marcellus says to Horatio: 'Something is rotten in the state of Denmark.' Is something rotten in charity governance? In the coming decades, poor charity governance could severely undermine confidence in the sector, reducing both charitable giving and charitable activity. Appropriate guidance and efficient monitoring could be strategic tools for the management of North America's US\$100 trillion in intergenerational wealth to be transferred by 2050.

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