

# Stanford SOCIAL INNOVATION<sup>Review</sup>

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*Viewpoint*  
**A Vast New Source for Social Purpose Finance**  
By Lester M. Salamon

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## VIEWPOINT

# A Vast New Source for Social Purpose Finance

The conversion of government-owned or -controlled assets into charitable endowments, or “philanthropication through privatization,” has succeeded around the world in creating effective foundations for social good.

BY LESTER M. SALAMON

**O**n February 21, *The New York Times* reported that Wells Fargo agreed to pay a \$3 billion fine to settle criminal and civil charges stemming from its “widespread mistreatment of customers” over a 14-year period. Although the article noted that \$500 million of the \$3 billion fine would go to the company’s investors, it failed to explain where the rest of the \$3 billion would go.

If past practice is any guide, most of such funds will go straight into the US Treasury. Some of the money may even go back to Wells Fargo to pay it for doing *post hoc* what it should have been doing *pre hoc*—i.e., protecting its customers from its own employees.

The Wells Fargo fines mystery is but one example of a much broader global phenomenon: massive flows of money from government transactions into black boxes. Trillions of dollars of assets around the world are produced from the sale, transfer, or regulation of common-use property or resources that governments own or control but that are being transferred wholly or partly into private, for-profit ownership and control. These transactions include sales of state-owned enterprises; debt swaps; royalties generated from state-regulated industries, such as lotteries or mining; transformations of cooperative or nonprofit institutions into for-profit enterprises; stolen assets; auctions of broadband spectrum; and penalties for corporate misdeeds of the sort illustrated by the Wells Fargo fine.

Such global transactions involve vast sums of money. In the four years between January 2013 and December 2016, governments around

the world generated \$998.8 billion through sales of state-owned enterprises, dwarfing the total for any previous period and demonstrating that privatization of state-owned enterprises is hardly a thing of the past.

Penalties imposed on corporations for violations of environmental, health and safety, or anti-corruption laws constitute another massive source. For example, the 1998 Tobacco Master Settlement Agreement between 46 state attorneys general and the four largest US tobacco companies netted more than \$240 billion in penalty payments. The ongoing opioid crisis litigation seems likely to yield \$75 billion to \$85 billion more. Litigation under the US Foreign Corrupt Practices Act, which applies to virtually every major corporation

in the world, generated \$2.89 billion in penalties in 2018.

How might societies best use such funds? Too often the money from such transactions is dumped into government budgets, where it is quickly lost from public view. Fortunately, a proven alternative exists for ensuring the preservation of at least a portion of the assets from such transactions for valid, long-term, common-use purposes. This option involves the transfer of all or a portion of the proceeds generated by transactions involving publicly owned, controlled, or regulated assets into permanent charitable endowments for the common good. I call this process Philanthropication thru Privatization, or PtP for short.

## FOUNDATIONS FOR GOOD

I stumbled upon the PtP alternative in the course of meeting with a number of foundations in countries around the world while raising funds for a research project examining the global nonprofit sector. Many of the foundations I encountered turned out to have emerged from the funds secured from such PtP transactions. These included the highly regarded Volkswagen Foundation in Germany, the King Baudouin Foundation in Belgium, and Italy’s many large foundations of banking origin. With support from ACRI, the association of Italian banking foundations, I was able to enlist a global team of researchers to investigate whether this phenomenon was even more widespread than I had so far discovered. Very quickly, reports from the field made clear that we had stumbled onto a phenomenon of enormous reach, and potentially momentous importance, suggesting a largely unrecognized alternative route to establishing charitable endowments that was already well developed and involved a highly diverse array of assets.



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By the time this initial round of fact-finding was complete in 2014, we had identified 565 foundations around the world that had emerged from one or another type of “PtP transaction,” and we had carried out in-depth case studies of 23 of them. We have since continued to discover new PtP foundations, with the total now standing at nearly 650.

These foundations have commonly emerged as sui generis solutions to particular local problems. For example, a dispute between the federal government of Germany and one of its states over which government owned the Nazi-era Volkswagen Company had kept West Germany from privatizing this company for a decade following the war. But when Russia launched its Sputnik satellite in 1957, sending shivers down the spines of West German leaders at the prospect of falling behind Russia in scientific progress, the country used the privatization of the Volkswagen Company to launch a major investment in German science, as well as an independent, private charitable foundation through which to pursue it. As a consequence, 40 percent of the proceeds of the Volkswagen Company sale were split between the Federal Republic of Germany and the State of Lower Saxony, and the remaining 60 percent was used to endow a Volkswagen Foundation dedicated to the promotion of German science. Starting with an endowment of 1 billion Deutsche Marks (\$238 million at the time), this foundation has now built its endowment to over \$3.9 billion—nearly the size of the US Rockefeller Foundation—while investing \$5.6 billion in German science.

Similar circumstances have produced other PtP foundations. Kazakhstan’s BOTA Foundation, for instance, was born from the embarrassing discovery of a sizable Swiss bank account held by the country’s president during his reelection campaign. In the case of Italy’s large foundations of banking origin, the country’s parliament refused to allow its prized network of 88 trustee savings banks to fall under the control of Europe’s huge banking complexes when the European Union in 1991 pressured Italy to transform these institutions into for-profit stock companies. Their solution? Place 100 percent of the resulting stock

into the charitable arms of the previous savings banks, creating 88 foundations, several of whose assets now rival those of America’s largest foundations.

PtP has repeatedly proved its value as a win-win solution offering benefits to important stakeholders involved in a wide array of complex public transactions. The Nippon Foundation in Japan, the Foundation for Community Development in Mozambique, the Renova Foundation in Brazil, the “la Caixa” Banking Foundation in Spain, the 240 health-conversion foundations in the United States, and hundreds more already make the case. Because of this track record, we don’t need to imagine how future transactions might occur.

What was lacking until the PtP research effort came along, however, was a concept to help identify the commonalities among these various institutions and transactions and to bring into focus the enormous promise they hold for the expansion of charitable endowments in many places that now lack them. It is this concept, and this potential, that the PtP Initiative, with support from the Ford, Mott, King Baudouin, Volkswagen, Cariplo, and “la Caixa” foundations, has been established to highlight and promote.

Armed with this concept, we have not only identified a substantial number of institutions already embodying it but also undertaken detailed case studies of how 25 of them have operated. In addition to examining the deals that led to the creation of these foundations, we have evaluated their governance structures, transparency provisions, and conflict of interest rules. Almost without exception, we have found that these foundations have established governance arrangements and operating procedures that rank among the best-in-class of global foundations.

## A COUNTERVAILING BALANCE

The PtP concept is more than an academic contribution. It has revealed the enormous practical potential for expanding the resources available for social, economic, and environmental problem-solving and strengthening civil society around the world, particularly in regions where charitable

endowments are limited or nonexistent, but PtP-type assets are plentiful.

PtP foundations have made major programmatic contributions to their societies. The BOTA Foundation, for example, has substantially improved the life chances of Kazakhstan youth, the Cariplo Foundation has fostered innovative low-income housing estates in Italy, and the Foundation for Community Development has contributed to significant local development initiatives in rural Mozambique.

Carefully designed, PtP institutions can assure citizens that penalty assets are used to prevent the reoccurrence of the infractions that gave rise to them; that fines for environmental damage, consumer fraud, health and safety violations, and other similar illegalities can be reliably devoted to protecting the environment, defending consumers, and advancing citizen health and safety; that the proceeds of mining can be used to support the social, economic, and environmental development of the populations impacted by it; and that the social commitments of nonprofit or cooperative organizations are still served when the institutions are converted into for-profit businesses.

Such institutions are not in any sense a substitute for the state. But with governments everywhere under stress; political forces hostile to environmental protection, health, and safety; and the rule of law increasingly threatened in many parts of the world, the need for a set of private institutions that can serve as a countervailing balance has become clearer than ever. PtP offers a proven route to creating and resourcing such institutions by tapping vast transactions that are already under way.

Accordingly, the PtP Project has launched an active dissemination and implementation effort around the world, with local exploratory committees at work or in process in Central Asia, Eastern Europe, Africa, Latin America, and the United States. Our goal is nothing less than a revolution in the charitable landscape of the world, starting with a dozen new or expanded charitable foundations over the next decade. We welcome your interest and your support for this effort. ■