Abstract

Much Corporate Social Responsibility literature suggests, implicitly or explicitly, that firms ought to engage in activities that can be characterized as philanthropy, that is, expending resources beyond what is required by law and market norms in order to promote the welfare of others. However, prominent accounts of Corporate Social Responsibility have failed to articulate a compelling moral or economic rationale for such philanthropy. In the first part of this paper, I examine debates about the nature and purpose of corporate philanthropy, concluding that, while these help clarify key questions, there are strong reasons to reject a general obligation for firms to engage in philanthropy. However, in the second part of this essay, I argue that there are two distinct rationales that can justify certain types of corporate philanthropy based on considerations of welfare economics. The first arises in cases in which firms make strategic but high-risk investments in activities that are likely to generate positive externalities even if they prove unprofitable for firms. The second arises in cases where a firm has a strong comparative advantage in its ability to address a social problem, such that alternative mechanisms of resolution would generate significantly higher social costs. I discuss important qualifications to each rationale as well as their broader implications for theories of Corporate Social Responsibility, Regulation, and Politics.
Does Corporate Social Responsibility (CSR) require firms to engage in philanthropy and, if so, of what sorts? Many of the most cited exemplars of CSR initiatives appear to involve philanthropy. For example, Toms Shoes pledges to match every pair of shoes sold with a new pair donated to a child in need, Patagonia donates 1% of sales to the preservation and restoration of the natural environment, and XEROX’s Community Involvement Program “channels funds to local teams of employees to select and work on specific community projects that they identify in their communities.” However, philanthropy occupies a peripheral and ambiguous role in accounts that have attempted to define Corporate Social Responsibility and its obligations. Indeed, the greatest theoretical weakness in Corporate Social Responsibility literature arguably lies in its vague justifications for corporate philanthropy.

In Archie Carroll’s classic formulation, CSR has four components: economic, legal, ethical, and discretionary or philanthropic (1979, 1983, 1991). Regarding the final component, he explains:

Philanthropy encompasses those corporate actions that are in response to society's expectation that businesses be good corporate citizens. This includes actively engaging in acts or programs to promote human welfare or goodwill... The distinguishing feature between philanthropic and ethical responsibilities is that the former are not expected in an ethical or moral sense. Communities desire firms to contribute their money, facilities, and employee time to humanitarian programs or purposes, but they do not regard the firms as unethical if they do not provide the desired level. Therefore, philanthropy is more discretionary or voluntary on the part of businesses even though there is always the societal expectation that businesses provide it. One notable reason for making the distinction between philanthropic and ethical responsibilities is that some firms feel they are being socially responsible if they are just good citizens in the community. This distinction brings home the vital point that CSR includes philanthropic contributions but is not limited to them. In fact, it would be argued here that philanthropy is highly desired and prized but actually less important than the other three categories of social responsibility. In a sense, philanthropy is icing on the cake.

It’s helpful to note that Carroll formulates this definition, in part, through sociological observation. As he explains in his historical survey of the concepts and practices of Corporate Social Responsibility, it is simply a fact that “Philanthropy, or corporate contributions, have assumed a central role in the development of CSR.” However, the underlying justification he offers for philanthropy is thin, resting on
“societal expectation.” The obvious problem is that, in addition to being difficult to define and measure, such expectations might not, in fact, be ethical, or even practical.

The philosophical problem that looms in trying to present philanthropy as a responsibility is an old one, concerning the relationship between the just and the good. Theories of justice that aim to delineate obligations are not well suited to justify or motivate good actions that go beyond the basic requirements of justice. Moral philosophers have debated how to define and understand so-called “supererogatory” actions - good acts that go beyond the call of duty. While insightful, these debates have not brought much theoretical innovation or clarity to the CSR literature.

It is easy to agree with Carroll that many forms of philanthropy are desirable. However, given the ambiguities regarding philanthropic obligations, from a theoretical perspective it is prudent for Carroll to relegate philanthropy to the peripheral position of “icing on the cake” and emphasize the primacy of economic, legal, and ethical considerations. These can be more readily grounded in logics that generate clear obligations if research suggests that certain empirical conditions are satisfied. This move does, however, increase the gulf between the theory and practice of CSR, for, as I suggested at the outset and Carroll suggests in his historical review, philanthropic activities are routinely cited as the exemplars of CSR - but CSR theories place these activities at the margin.

Ironically, the scholar who has most closely identified CSR with philanthropy is Milton Friedman. His classic essay “The Social Responsibility of Business Is to Increase Its Profits,” begins by noting the “analytical looseness and lack of rigor” in discussions of the social responsibilities of business. Friedman’s own approach is to analyze the use of corporate resources through the lens of ownership and responsibility. Owners of a firm (stockholders) are welcome to use any wealth that they derive from a business for philanthropic purposes (and non-profits can be organized to pursue charitable objectives in a collective manner through voluntary donations). However, corporate managers are agents of owners and have a duty to run a businesses for the purpose that the owners
intend, which is paradigmatically to make a profit. Spending firm resources on philanthropic activities that do not increase the profitability of the firm is, in effect, imposing a tax on shareholders (spending their money in a manner they haven’t chosen). Moreover, firms that expend resources on unprofitable philanthropy will be at a competitive disadvantage over time, likely compromising their viability.

Friedman acknowledges that some ostensibly philanthropic expenditures may help generate greater profits. However, in that case, there is nothing to object to, because this would simply be good business strategy. His iconoclastic conclusion follows from the basic premises of his analysis: "there is one and only one social responsibility of business--to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition without deception or fraud."

Crucially, Friedman does believe firms have an ethical obligation to confirm to the “basic rules of the society, both those embodied in law and those embodied in ethical custom.” Precisely what these rules are, or should be, is open to debate; and scholars have developed persuasive critiques of the particular understanding of laws and ethical customs that Friedman endorsed. However, note that at the general level of principle, Friedman’s commitment to profitability, law, and ethical custom corresponds almost perfectly to the foundational three components of Carroll’s CSR pyramid (the economic, legal, and ethical). It would seem that the only thing separating Milton Friedman from the most prominent account of Corporate Social Responsibility is the issue of philanthropy - the component that Carroll has suggested is the least important to his account and yet which dominates most discussions of CSR in practice.

The analytical clarity of Friedman’s essay is helpful for formulating a more precise definition of corporate philanthropy, namely: expending resources in a manner that is unlikely to be profitable and beyond what is required by law and market norms in order to promote the welfare of others. There may be some uncertainty about what profit, law, and the welfare of others require in detail, but their general meaning is clear.
“Market norms” is a trickier concept, and it’s important to distinguish it from Carroll’s account of “societal expectations,” which he invokes as a justification for philanthropy.

The key difference is captured by another word that Carroll uses in his discussions of philanthropy, namely “desire.” He explains that “Communities desire firms to contribute their money, facilities, and employee time to humanitarian programs or purposes, but they do not regard the firms as unethical if they do not provide the desired level,” and that “philanthropy is highly desired.” Moreover, he clarifies that philanthropy is “not expected in an ethical or moral sense.” Thus, it is more accurate to describe Carroll justification for philanthropy as rooted in societal “desires” rather than “expectations.” We do not literally expect every business to engage philanthropy (if so, that expectation is evidently mistaken), nor does he believe that we have a right to expect philanthropic activities (as Carroll emphasizes, we “do not regard the firms as unethical if they do not provide the desired level”). Strictly speaking, philanthropy is desirable and thus desired, but generally not expected, either as a prediction or as an ethical obligation.

By contrast, market norms do function as expectations grounded in ethical legitimacy. Perhaps the most recognizable example is tipping 15-20% at restaurants in the United States. This is a well-established, socially recognized norm that is adhered to by most patrons, despite being voluntary and not legally required. It is an integral part of the calculus that allows waiters and restaurant owners to make predictions about wages and the financial viability of their enterprise. Tipping also functions as a way to reward or penalize a waiter for the quality of service. For all of these reasons, tipping commensurate with service is properly regarded as a “market norm” and something that one ought to do. Conversely, tipping is not regarded as a form of philanthropy and one cannot claim his or her tips as charitable deductions for tax purposes. It’s just part of the cost of doing responsible business.

Although this familiar example functions at the individual level, there are analogues at the corporate level. We expect corporations to keep agreements with business partners even if not formally contracted, to abide by standards promulgated by
certain industry associations even if not sanctioned by law, to apply policies in an equitable manner even if a potentially aggrieved party does not have standing to sue, and so on. Both Friedman and Carroll agree these norms can be ethically binding, but neither views abiding by them as a species of philanthropy.

There are other explicit discussions of philanthropy within the business ethics literature, but they tend to fall within the following themes, none of which offer a satisfactory normative account: First, a large amount of research has explored the potential strategic value of philanthropy (Porter and Kramer, 2002; Saiia, Carroll, and Buchholtz, 2003). In so far as philanthropy pays, however, the case for it is fundamentally economic. A related literature has examined ways in which philanthropy can be a rational response to a firm’s regulatory environment, particularly with regard to tax incentives and the avoidance of legal liability (Halme and Laurila, 2011). Again, the ultimate rationale for philanthropy is instrumental to the firm’s private ends. Philanthropy has also been criticized because of the objectives for which it is instrumentally deployed. Jennings (2006) suggests that corporations engage in philanthropy to offset, or distract attention from, their bad behavior in other domains. Benabou and Tirole (2009) consider whether corporate philanthropy is merely a way for managers or directors to funnel money to causes they personally support at the expense of shareholders. Peter Thiel has even suggested that high levels of corporate giving indicate that a firm lacks ideas for productively investing capital and has become stagnant, preferring to mobilize donations to buy goodwill for the purpose of creating rents (Zero to One).

A large literature in moral philosophy has argued for philanthropic obligations derived from utilitarian considerations (e.g Singer). However, this literature is primarily concerned with obligations that an individual has to help others and seldom considers the implications for corporate giving. Shaw and Post’s “A Moral Basis for Corporate Philanthropy” (1993) is perhaps the most ambitious attempts to ground corporate philanthropy as a moral obligation. Based on loosely argued rule-utilitarianism, they conclude that “corporations do have a moral duty to advance the public welfare” because
“when there is an irreconcilable opposition between self-interest and utility... the good of the whole prevails.” At this level of generality, their conclusion is not very persuasive.

Part of their argument is the claim that businesses benefit from the larger social structures of a society and thus have a responsibility to contribute to their improvement as a matter of reciprocity. Moreover, the authors quote approvingly a passage by Morrissey (1989) that expresses a common supporting argument made by those who favor more corporate philanthropy:

Government, burdened by continuing deficits, unfortunately lacks the resources to effectively address many pressing national concerns. Private individual efforts also fall short of the needs. Large corporations, on the other hand, are the dominant institutions in our economy and in that sphere are amazingly efficient organizations. Much of the nation's wealth lies in their treasuries. For both pragmatic and theoretical reasons, the law should require that they broaden their mission to promote the common welfare as well as their own profitability.

While one may be sympathetic to the general principle that with great power and great resources comes great responsibility, this does not address Friedman’s challenge regarding the proper locus of this responsibility - individual or corporate. Individuals who derive great wealth from corporate profits may have a philanthropic responsibility, but urging this responsibility to be discharged by corporations suggests that individuals will not in fact be willing or able to live up to this responsibility (and that state based taxation is not a viable alternative). The idea that corporations can be more efficient than individuals, nonprofits, or the state is perhaps a relevant insight, but the implications have not been explored in a rigorous manner.

Another way of interpreting Morrissey’s argument is as an analogue to the famous response that the bank robber, Willie Sutton, offered to FBI officers tasked with interrogating him. When asked why he robbed banks, Sutton replied, “Because that’s where the money is.” Similarly, it’s obvious why anyone who would like to see more resources devoted to philanthropy would turn to large corporations. That’s where the money is. True as this may be, it does not address the deeper question of moral obligation.
A final difficulty with the moral basis for corporate philanthropy affirmed by Shaw and Post is that it offers no specific criterion or guidance for determining when or how corporations should engage in philanthropy. The authors do insist that companies should place the highest priority on remedying any harms that a company has caused, although it’s not clear why this should be considered philanthropy (rather than restitution). However, the ultimate conclusion that the authors arrive at is vague and provides little practical direction: “having consulted the available corporate resources, i.e., the firm's time, talent, and financial capacity for doing good, and having balanced those resources against the magnitude of the social need, there may well be an obligation to go to the rescue.” There may be, but how would one know? This conclusion is typical much business ethics literature that seeks to affirm the goodness of corporate philanthropy but does not articulate a rationale for deciding when exactly it is warranted.

In summary, then, there is broad consensus that socially responsible firms ought to be economically viable (a sign that they are creating value), to follow the law, and to abide by market norms. Philanthropy, however, is the elephant in the room. It plays a large role in what many consider CSR in the real world, but the lack of a compelling, articulate rationale for philanthropy appears to be the Achilles heel of CSR theories.

This problem has not escaped the attention of recent scholars. As Wayne Norman explains in a seminal article proposing a “more unified normative theory of business obligation,” existing CSR frameworks are widely attacked for “their vagueness and their disappointing inability to distinguish clearly between genuine beyond-compliance moral obligations, on the one hand, and charitable acts that are laudable but not morally obligatory on the other.” From his review of the last two decades of business ethics literature, Norman concludes:

...the common shortcoming for stakeholder theories and theories of CSR and corporate citizenship is the lack of a clear, compelling normative methodology that would allow corporations, managers, or outside observers, to justify which beyond-compliance obligations must be met, and how business actors are to trade-off in a reasonable way the claims of competing stakeholders. Most crucially, what we still lack is compelling principle-based guidance for when exactly firms
in competitive markets must constrain themselves from pursuing profitable opportunities (that is, genuinely profitable, all things considered) that are legal but possibly unethical or irresponsible.

Norman aims to develop a normative methodology that can avoid these shortcomings. Moreover, he argues that a satisfactory account should be able to justify both legal requirements and “beyond-compliance ethical obligations” within a unified framework. The account that Norman proposes - “business ethics as self regulation” - draws on and amends Joseph Heath’s “market failures approach to business ethics.”

The key starting point for both scholars is to consider the benefits of markets from the general perspective of social welfare. Heath draws on literature concerning market failures to identify specific conditions under which competition for profit generates bad outcomes from a social welfare perspective. For example, firms may be incentivized to pollute, generating negative externalities for others and failing to internalize the true cost of production, in the absence of well designed property rights or regulations. The same cost-benefit logic that justifies (efficient) laws against pollution also provides an ethical warrant for firms to self-regulate to voluntarily reduce their pollution. While reducing pollution will reduce the profitability of a firm, profiting from pollution is perversion of the market system that generates inefficiencies and harms. Thus, from an ethical perspective, a firm has no right to profit from (pernicious) pollution. The real challenge, though, is to determine which regulatory frameworks can best overcome the collective action problem generated by incentives to pollute: a ban on pollution accompanied by high fines, the assignment of property rights and ability to litigate tort claims, a cap a trade market for pollution rights, an industry pact to refrain from pollution and ostracize violators, etc.?

This is the sense in which Norman conceives of business ethics as self-regulation. It involves a search for creative regulatory frameworks, which may require varying degrees of voluntary self-restraint, to help solve the same problems that we are justified in solving through law when cost-benefit analysis identifies an efficient way to do so. However, Norman expands Heath’s approach in two ways. First, Norman argues that it is
not always unethical to profit from market failures, since failures of some sort characterize most real world markets. A detailed argument must be made for the cost and benefits at stake on any given issue from a welfarist perspective, but literature on market failures provides a model for doing exactly that. Second, Norman acknowledges that there may be objectionable business practices worth regulating whose wrongness does not concern market failure. Norman summarizes his position as follows:

We might say that the core of Heath’s market-failures approach is that firms have obligations to observe certain beyond-compliance norms, and that these obligations are based on the same criteria we have for justifying legal “compliance” norms. And since those legal norms can legitimately be based on considerations that go beyond market failure, we should expect that the beyond-compliance norms can be as well. Taking the deliberately adversarial nature of the market seriously, we find it prima facie unethical for firms to try to gain competitive advantage by ignoring legitimate norms, whether they are grounded in market failure, government failure, considerations of justice, public decency, or what have you.

Note that Norman recognizes that there is room for disagreement about what constitutes “legitimate norms,” although the criteria will be broadly welfarist. However, when the case for a norm is well established, the regulatory question offers a clear research agenda that can raise specific empirical questions and generate specific guidance for action. Norman views this as a considerable benefit that stands in contrast to the vague platitudes of much business ethics literature:

Careful analyses of the core concepts of “responsibility” or “citizenship” do not help us clarify exactly how far a given firm or manager should exceed legal standards of conduct, or in which cases they must be willing to sacrifice long term profits for the sake of beyond-compliance obligations. If anything, these core concepts confuse and obscure these issues. “Responsibility” is a notoriously vague and ambiguous deontic concept compared, say, to the concept of an obligation or a right; and what we quickly learn is that managers and firms have all sorts of competing and conflicting responsibilities with respect to different constituents or stakeholders.

By contrast, Norman argues that his approach provides clarity with regard to these vexed issues:
The virtue is that it can distinguish between drawing careful distinctions between, for example, (i) activities or omissions that are unfortunate but not ethically forbidden, (ii) activities or omissions that are either obligatory or forbidden, and (iii) activities that are permissible and beneficial, but not obligatory.

Put another way:

Business ethics as self-regulation helps us to distinguish between what exactly we think firms are ethically obliged to do, above and beyond complying with laws, on the one hand; from what it might be nice for them to do, even if they are not obliged to do so, on the other.

By this point it should be apparent that Norman thinks corporate philanthropy falls in the “nice to do” but not obligatory category. Notably, none of the examples he considers throughout his article concern philanthropy. Rather, one might view philanthropy as a fundamental target of Norman’s proposal. His point is that, while philanthropy may be nice to do, it lies beyond obligation and should not be conflated with a serious business ethics research agenda.

Norman’s framework, which I consider the most promising theoretical advance in business ethics in recent years, seems to leave corporate philanthropy by the wayside. Again, we are confronted with the incongruity between the large role that philanthropy plays in CSR programs in the real world and Norman’s insistence that it does not touch the core of ethical obligation justified by the business ethics as self-regulation approach. Norman may simply be right, and the prominence of corporate philanthropy a misguided distraction for the field, but I want to argue that Norman has not fully appreciated the implications of his welfarist approach, which can provide strong justifications for corporate philanthropy.

Here I can finally introduce the main arguments of this paper. Norman’s framework is highly compelling. However, it is a mistake for him to place questions of philanthropy beyond business ethics in the “nice to do” category. Rather, the considerations of welfare economics on which Norman’s account is grounded can provide strong justifications for corporate philanthropy and do so in the detailed manner that Norman calls for. Given that he presents his account, in part, as a plea for new
research agenda and that he sees himself “preparing the way for a larger project.” I intend my arguments below as a friendly amendment to Norman’s proposal.

The theoretical apparatus of welfare economics, which provides the starting point for Norman and Health, does in fact provide compelling justifications for corporate philanthropy that yield specific guidelines for action. In what follows, I argue that there are two distinct rationales that can justify certain types of corporate philanthropy based on considerations of efficiency, social cost, and market structure derived from welfare economics. The first arises in cases in which firms make strategic but high-risk investments in activities that are likely to generate positive externalities even if they prove unprofitable for firms. The second arises in cases where a firm has a strong comparative advantage in its ability to address a social problem, such that alternative mechanisms of resolution would generate significantly higher social costs. Moreover, the arguments for corporate philanthropy are so well supported by welfare economics that I suggest to reject them requires rejecting the larger welfarist grounding of Norman’s project.

I. Strategic but Risky Investments with Positive Externalities

Perhaps the greatest accomplishment of the CSR movement is that it has encouraged business leaders to think creatively and hard about ways to do well by doing good. That is to say that the CSR movement has encouraged entrepreneurs to search for ways of generating value by addressing social problems. As Drucker put it, “the proper ‘social responsibility’ of business is to tame the dragon, that is to turn a social problem into economic opportunity and economic benefit, into productive capacity, into human competence, into well-paid jobs, and into wealth” (Drucker, 1984, p. 62). This vision gave rise to a vast literature investigating whether CSR pays; although as critics have pointed out, to the degree that it does, the “socially responsible” angle appears moot. However, the point of Drucker’s exhortation is that profit opportunities in social entrepreneurship may not be obvious or without risk. Only once discovered and proven does a clear business case emerge that leads other firms to adopt a practice.
This explains the “time and context” dynamic of CSR that has been noted by Rivoli and Waddock (2011). Initially, only one or a handful of firms may be willing to take considerable risk investing in a business practice with positive externalities in the hope that it will generate value for the firm. If indeed this proves successful in increasing consumer demand, improving employee morale, shifting industry norms, and so on, then other businesses may find it in their interest to follow suit. An important question, however, is what justifies the decision of a first mover.

Considered from the perspective of welfare economics, certain investments with positive externalities may yield a net gain for a society, even if their expected value is negative for a firm. Such investments are thus desirable from a welfarist perspective (they may provide tangible public goods as externalities, or help with the entrepreneurial process of discovery). However, given the uncertainty surrounding “the business case,” early stage investment looks more like philanthropy than strategy - but philanthropy that can be justified by overall welfare considerations.

From a welfarist perspective, a firm should invest if the expected value and positive externalities are a net positive, all things considered. However, from a profit maximizing firm’s perspective, the firm should only invest if the expected value is positive. (Note that if the expected value is negative and large enough to offset the value of positive externalities, even the welfarist would reject an investment).

Given this analysis, a specific rationale for corporate philanthropy emerges: the larger the ratio of positive externalities to expected loss, the more justification there is for a corporation to make a philanthropic investment.

For example, imagine that a company like Netflix, whose product is greatly enhanced by a high speed internet connection, is considering whether to subsidize the installation of high speed internet cables in rural towns at a cost of $100 million. For simplicity’s sake, suppose that reliable market research suggests that there is a 50%
chance that this will greatly increase subscribers, yielding the company an additional 
$120 million of net revenue. But there is also a 50% chance that subscriber growth will 
be more modest, yielding the company only an additional $60 million of net revenue. The 
expected value of this investment for the company is $90 million (.5x120 + .5x60=90), 
which is $10 million less than the required investment of $100 million. A profit-
maximizing firm would thus judge that it is not in their interest to make this investment 
since it leads to an expected loss of $10 million. However, the investment would also 
generate a positive externality of $100 million of additional Internet infrastructure. Let us 
stipulate that 10 million people will experience spillover benefits from this infrastructure 
valued at at least $10 per person, but transaction costs make it infeasible to capture this 
value. Overall, the society would be much better off with the investment (some $90 
million better). From a social welfare perspective, the company should make the 
investment (assuming there are not alternative ways to invest the money expected to 
produce even greater benefits).

We arrive at a situation in which a corporate expenditure would generate large 
social welfare benefits at a comparatively small net expected cost and with a decent 
chance of being profitable for the firm. Because of the riskiness of the investment, there 
is not a solid business case for making it (preferences for risk could complicate the 
underlying analysis but not change the overall conclusion). However, there is a 
philanthropic rationale for making the investment, which derives from the perspective of 
overall social welfare.

Moreover, we can identify and quantify the relevant factors. First, we need a 
measure of the overall cost, which is the difference between the return expected from the 
firm’s cost of capital (~11% for Netflix x $100million= $11 million) and the expected 
loss on the investment (-$10 million); so, in this case the cost would be $21 million. 
Second we need a measure of the benefits (positive externalities), in this case estimated at 
$100 million. Thus, the overall ratio of benefits to costs in this case is 100/21 or about 
4.76. We can call this the “philanthropy multiplier.” The higher it is for a particular 
expenditure, the more compelling the social welfare justification. We can debate at what
level a serious ethical obligation begins to emerge, but the underlying calculus is clear. Note that the philanthropy multiplier goes up as a company’s cost of capital goes down, the expected value of an investment goes up, and the positive externalities go up.

II. Comparative Advantage that Lowers the Social Cost of Addressing Problems

A second kind of welfarist justification for corporate philanthropy derives from the comparatively low cost at which certain firms can address social problems. Benabou and Tirole’s (2009) have developed the idea of “delegated philanthropy” to describe a situation in which stakeholders desire that a corporation sacrifice some profits in order to engage in philanthropy on their behalf. This raises the question as to whether this is a rational approach for stakeholder to prefer. Benabou and Tirole argue that it may be, given that firms possess a unique advantage in terms of information and transaction costs:

…one needs to explain why people would want corporations to do good on their behalf, rather than doing it on their own or through charitable organizations, churches, etc. Information and transaction costs are clearly important here. In theory, consumers could send money to directly supplement the income of workers in the coffee plantations supplying Starbucks. But they would have to be informed about the occurrence of individual trades and contracts, and their financial transfers would involve enormous transaction costs. Somehow, philanthropy must thus be delegated. It could perhaps be entrusted to some charitable organization, but transaction costs are still likely to be much lower if delegation goes through the corporation, which already is involved in a financial relationship with the workers.

The key insight is that firms will have a comparative advantage in the provision of aid given the knowledge and efficiencies that accompany their business practices. Benabou and Tirole suggest that firms engage in philanthropy in response to specific stakeholder demands, although it is unclear how these are expressed and how they then mobilize firms to action. However, from the perspective of social welfare, this mechanism doesn’t matter. Rather, an analysis of the overall costs and benefits provides strong justification for corporate philanthropy on the basis of comparative advantage,
defined as the “ability of any given economic actor to produce goods and services at a lower opportunity cost than other economic actors.”

For example, consider a large bakery that closes at 5pm. The bakery has to offer a wide assortment of freshly baked goods up until closing time in order to continue to attract customers. However, at 5:01 pm its excess inventory for the day becomes worthless (e.g. bread becomes stale and other products start to spoil, making them unsuitable for sale the next day). Suppose that on any given day, the bakery closes with $500 of baked goods still on the shelf and that for reasons of regulation (health codes) and transaction costs, it’s most cost effective for the bakery to simply throw these away. However, a local food kitchen has asked the bakery to donate these excess baked good at the end of each day so that they can be served to poor families later in the evening.

The problem is that doing so will generate small, additional costs for the bakery that the food kitchen cannot cover. For example, employees will have to stay later to package and transport the food at, say, an overall cost of $50. We arrive at a situation in which, if the bakery were willing to expend $50, this would generate a $500 benefit for others. Moreover, if an independent philanthropist or non-profit wanted to feed the hungry and did not know about the bakery’s unique situation, it would cost $500 to purchase a similar amount of food at market prices. Thus, letting the food go to waste arguably destroys $450 of value. Of course, if independent philanthropists did know about the bakery’s situation and the costs of donation, an advantageous deal could be struck. However, transaction costs and the localized nature of knowledge will often preclude this.

From a social welfare perspective, the bakery should donate the food at its own expense if there is no market mechanism to compensate the bakery. Again, we can identify and quantify the relevant factors. Supposing a cost of capital of 10%, the bakery’s overall cost is $55 and the overall benefit is $500. Thus, the overall ratio of benefits to costs is 500/55 or a “philanthropy multiplier” of 9.09. Again, we can debate at
what level a serious ethical obligation begins to emerge, but the underlying calculus is clear, as is the social welfare justification.

Conclusion

Despite the widespread practice of corporate philanthropy, accounts of Corporate Social Responsibility have not provided a detailed and compelling rationale for philanthropy. Wayne Norman’s proposal for “business ethics as self-regulation” is among the most promising recent theoretical advances in the CSR literature. However, this approach also says little about philanthropy, relegating it to the domain of permissible, but voluntary activities that are “nice to do.” Upon scrutiny, however, the social welfare criteria that ground Norman’s approach can be shown to also justify certain forms of corporate philanthropy. If persuasive, my arguments can help resolve a lacuna that has plagued the CSR literature since its founding. If not persuasive, my arguments provide reason to reject Norman’s “more unified normative theory of business obligation” and the social welfare justifications that ground it.