



Profit versus Nonprofit

“Philadelphia Scandal Underscores Pitiful State of Public Housing Oversight,” read Jonathan Berr’s Aug. 28 report in the Daily Finance. It was a story about Carl Greene, the embattled director of the Philadelphia Housing Authority (PHA). He was put on paid leave while the board investigates charges that he settled four sexual harassment claims against him without notifying the PHA, doled out work to politically connected law firms and pressured employees to donate to his favorite nonprofit. Greene is also being investigated by the U.S. Attorney General Office for the Eastern District of Pennsylvania and HUD’s Office of Inspector General. They have yet to bring criminal charges against him.



People always act surprised by revelations of political corruption but the Philadelphia Housing Authority corruption is highly probably in nonprofit entities such as government. Because of ignorance and demagoguery, being profit-motivated has become suspicious and possibly a dirty word. Nonprofit is seen as more righteous. Very often, people pompously stand before us and declare, “We’re a nonprofit organization.” They expect us to believe that since they’re not in it for money, they are somehow above self-interest and have the public interest as their motivation. There’s little much further from the truth.

People are always self-interested. It’s just when they manage a nonprofit organization such as the Philadelphia Housing Authority, government entities in general, universities and charitable organizations, they face a different set of constraints on their behavior. The fundamental difference between nonprofit organizations and their profit-making counterparts is that nonprofits tend to take a greater portion of their compensation from easier working conditions, more time off, favors and under-the-table payments. Profit-making organizations take a greater portion of their compensation in cash, except those that are highly regulated.

In the profit-making world, there is much greater monitoring of the behavior of people who act for the organization. Profit-making organizations have a financial bottom line they must meet, or sooner or later, heads will roll. Not so with nonprofits, who have no bottom line to meet. On top of that, incompetence for nonprofits means bigger budgets, higher pay and less oversight. That description aptly fits one the nation’s largest nonprofit organizations — the public education establishment.

Profit is vital to human well-being. Profit is the payment to entrepreneurs just as wages are payments to labor, interest to capital and rent to land. In order to earn profits in free markets, entrepreneurs must identify and satisfy human wants and do so in a way that economizes on society’s scarce resources.

Here’s a little test. Which entities produce greater customer satisfaction: for-profit enterprises such as supermarkets, computer makers and clothing stores, or nonprofit entities such as public schools, post



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offices and motor vehicle departments? I'm guessing you'll answer the former. Their survival depends on pleasing customers. Nonprofits, such as public schools, post offices and motor vehicle departments, survival depends mostly on pleasing politicians.

When a firm fails to please its customers and thereby fails to earn a profit, it goes bankrupt, making those resources available to another who might do better. That's unless government steps in to bail it out. Bailouts permit a business to continue doing a poor job of pleasing customers and husbanding resources. Government-owned nonprofit entities are immune to the ruthless market discipline of being forced to please customers. The same can be said of businesses that receive government handouts.

It's this ruthlessness of market discipline that forces firms to please customers, economize on resources and thereby earn profits or go out of business and goes a long way toward explaining hostility toward free market capitalism. And much of the hostility toward free market capitalism is held by businessmen. Adam Smith recognized this in his "Wealth of Nations" when he said, "People of the same trade seldom meet together, even for merriment and diversion, but the conversation ends in a conspiracy against the public, or in some contrivance to raise prices." Their co-conspirator is always government.

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