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CHANGING LANDSCAPES FOR CHARITIES IN CANADA: WHERE SHOULD WE GO?

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SUMMARY

Charitable giving in Canada has never been higher. Between 1992 and 2008, contributions to charitable organizations more than doubled, from \$4 billion to more than \$9 billion. Donations to charitable foundations grew at an even more remarkable rate: more than 250 per cent, over the same period.

But those striking numbers mask more puzzling, some might say more worrying, trends. While donations overall have grown, not all charity types have shared equally in the gains. Religious charities and health-related charities have seen the lowest amount of growth. Meanwhile, the country's larger charities and foundations have seen substantial increases in donations, but donation rates to smaller charities have been relatively flat. As for the donors, it's almost entirely high-income Canadians who seem to be giving significantly more, while the rate of giving among middle-income and lower income Canadians has hardly grown at all. In fact, the share of people claiming tax credits for donations in each income group is actually in decline, meaning fewer of us seem to be giving to registered charities, while the richest Canadians are primarily responsible for the rise in donations.

The reasons for these unusual trends are unclear – though there is some evidence that the more ethnically diverse our country has become, the less inclined we are to donate. And whether we should even be concerned about these uneven patterns – the wealthiest Canadians giving bigger cheques to the country's biggest charities and foundations – is also an open question.

But the uncertainty about what these trends mean, why they're happening, and whether they're even a problem, is not something we should take lightly. Changes may be coming soon to Canadian charity policy: Last year, a House of Commons committee began a sweeping study of charitable giving in Canada, and it is already evaluating dozens of suggestions for policy adjustments. But, while we can discern some patterns and trends in giving, the reality is that we actually still know very little about why Canadians give, and how we, as a society, want to change the way we give, if at all. And until we make the effort to learn considerably more, any policy changes aimed at altering the landscape for Canadian charities are at risk of being politically driven, rather than evidence-based, and they could very well end up creating more problems than they solve.

[†] The author wishes to acknowledge the helpful comments of the anonymous referees.

INTRODUCTION

Over the last few years, concerns have been raised about the state of charitable giving in Canada. These concerns range from: claims of declines in giving by subgroups of the population (e.g. younger adults) or across the board; the tax treatment of donations; and the oversight of charity operations. On December 15, 2011, The House of Commons standing committee on finance announced that it was undertaking a study of charitable giving in Canada in 2012. The committee has received over 55 submissions and held several days of meetings that covered presentations from many perspectives. The committee stated that the focus of the study would be:

“ ... in respect of both individuals and corporations, current and proposed tax measures to encourage charitable giving. The examination will include the charitable tax credit amount and the possible extension of the capital gains exemption to donations of private company shares and real estate. The study will also focus on the feasibility and cost of changes to existing tax measures as well as the implementation of new tax incentives.”

The submissions to the committee covered many ideas and suggestions. Some of the more popular points included:

- Creating a single tax credit, at least at the federal level. Current policy provides a federal credit of 15 per cent for the first \$200 donated and 29 per cent for any amounts above \$200.¹
- Creating a “stretch” tax credit, which would increase the tax credit for giving if an individual gives more than she has previously given, but with a cap that would limit the extra credit so that it could be applied only to a maximum of \$10,000 in additional donations.
- Eliminating the capital gains tax on donations of private (as opposed to publicly traded) company securities, placing it on equal footing as donations of publicly traded company securities.
- Eliminating the capital gains tax on real estate donations.
- Differentiating the level of tax credits available for donations based on the type of goods and/or services provided by the recipient charity and/or providing a greater tax credit for an initial dollar-level of donation, and a lower tax credit for every dollar beyond that threshold.
- Creating special tax incentives for donations of items such as food and basic necessities.
- Asking for more clarity in the information made public by registered charities and similar organizations (for example, the tax returns of non-profit organizations). Similarly: Promoting greater transparency and reducing regulatory abuse by charities to help promote public trust in charities.
- Promoting a regulatory environment that would allow charities greater flexibility in raising revenue to support their goods and services.
- Concerns regarding perceived declines in the donor pool and a shift in support to larger charities and foundations, hurting smaller and medium-sized charities.

¹ Note: Additional credits are available at the provincial level, providing donors with a higher tax credit overall. Federally, there is a cap on charitable donation tax credits equal to a maximum of 75 per cent of income.

A brief review of the submissions reveals that, while many of the submissions focused on encouraging individual giving through the enhancement of tax credits, most lacked an evidence-based analysis of charitable giving in Canada to support their positions. Moreover, there was little discussion about how a change in the tax treatment of private giving might impact direct government support of charity operations. This is a serious shortcoming. Policy prescriptions should be based on evidence-based research. Failure to do so increases the risk that policy decisions will become politicized and will be based on unsubstantiated beliefs.

What do we really know about charitable giving in Canada? What do we know about Canadian foundations and charity operations? It is easy to toss numbers around and make them sound meaningful. It appears that most advocates take it as given that giving in Canada has fallen. Is this true? Has giving changed in meaningful ways that could help us understand better how to direct our energies when it comes to charitable giving and charity operations? These are very big questions that will take more than one report to answer.

The focus of this report is to promote more critical analysis to help us understand the dynamics of giving and charity operations. This report explores the direction of changes in giving to charity and how these changes have impacted the charity landscape. Once we have a better understanding of the giving landscape in Canada, only then can we better evaluate whether and how to change it. Individuals give both money (including marketable goods) and time. This report focuses on the giving of money. Equally valuable, however would be a better understanding of the giving of time.

WHY USE THE TAX SYSTEM TO ENCOURAGE GIVING?

In general, when we think about tax incentives to promote giving, we use a model where individuals make economic decisions based on their preferences for charitable and other goods, given their income and wealth constraints. We can model these preferences in many ways. One commonly accepted model is where an individual cares about the overall provision of the charitable good and her donation towards that provision, something commonly referred to as the “warm glow” effect. If a donor’s motives are purely altruistic — and not to feel a “warm glow” at all — then an increase in donations to her chosen cause by other donors, or greater government support for that cause, would result in a decline in her donation at a dollar-for-dollar rate (since she would believe the need served by her dollar would now be served, instead, by someone else’s). If a donor is both altruistic and motivated for “warm glow” reasons, then an increase in donations to her chosen cause by other donors, or greater government support for that cause, would most likely result in a decline in her donation, but at a rate less than dollar for dollar (since the donor perceives a value in her donation beyond its utility).

For this reason, governments may support charitable giving through the awarding of grants and contracts to charities. Alternatively, the government can choose to forgo tax revenue, giving the donating individual a tax credit and/or deduction. The tax credit effectively lowers the price of giving. And so, by lowering the price of giving, individuals may give more. Bakija and Heim²

² Jon Bakija and Bradley Heim, “How Does Charitable Giving Respond to Incentives and Income? Dynamic Panel Estimates Accounting for Predictable Changes in Taxation,” NBER Working Paper #14237 (2008).

summarize the research that studies how changing the price of giving affects giving. This effect is commonly referred to as the tax price elasticity of giving — meaning the level of responsiveness shown by individuals after a one per cent change in the price of giving (after the tax credit). More recent estimates suggest this elasticity is close to negative one (-1) meaning that a one per cent decrease in the price of giving should result in a one per cent increase in giving.

However, inducing a change in the price of giving may or may not be a societal benefit. Many of the changes in tax policies over the last 20 years have disproportionately benefitted wealthier taxpayers. If the types of charitable goods to which these taxpayers donate differs from the types of goods that are supported by the government, is this good or bad? Thus, in the next sections, let us examine patterns of giving and how they have changed over the last couple of decades.

PATTERNS IN REPORTED GIVING

Measuring charitable giving is challenging. There is no one source that captures fully how, and to what causes, Canadians give. On the data front, there are three main sources. The first source is to look at giving as reported on individual tax returns. Given that there are tax credits available for charitable giving, we might expect giving to be reported on tax returns. Tax credits, however, are only offered for gifts for which a tax receipt is issued. Giving money to a person on a street corner is not a donation for which a tax receipt is issued. Adding a donation to a grocery bill also does not count as tax-receipted giving. Buying a ticket to a fundraising event is typically not treated as a tax-receipted donation. Moreover, tax credits are non-refundable. Thus, if an individual has no tax liability, there is little incentive for reporting donations. Information from individual tax returns, thus, can only provide a partial picture. Given that tax-receipted giving represents a large portion of giving, however, data from tax returns can help us to discern patterns in giving and changes in those patterns over time.

A second source of information on giving is the periodic surveys conducted by Statistics Canada on individual giving and volunteering. These surveys are useful in that they ask individuals to report on different sorts of giving, including things such as giving to the person on the street corner, as well as the giving of time. A challenge with these surveys, as with any survey, is that they rely on the individual's recollection. Also, they are only conducted periodically, and while great efforts are made to capture a representative sample of Canadians, for several reasons it can be difficult to draw reliable conclusions about changes in individual giving habits over time and throughout someone's lifecycle.

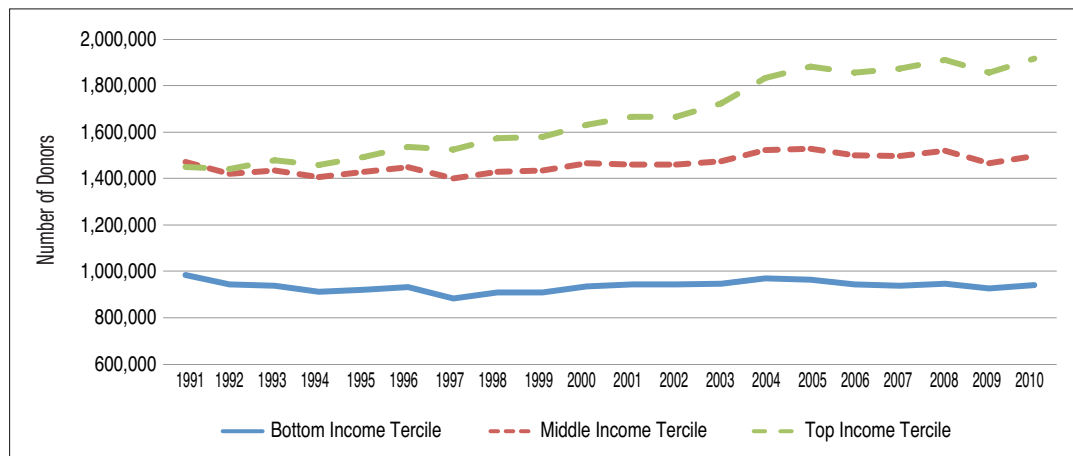
A third source of information on giving is what charities report on their information returns. All registered charities are required to file returns with the Canada Revenue Agency (CRA). As charitable status can be revoked for failure to file a return, there is an incentive to file and to provide accurate information. The information return asks the charity to report funding from different revenue sources. This allows us to capture information about different types of giving, including those for which a tax receipt was issued, donations of non-cash items, and revenues from fundraising events. The charity information return should capture the donation that is given to a person on the street corner, provided that person is collecting money for a charity. It will not, however, capture the money given directly to a homeless person.

Let us look at all three data sources to discern trends in giving.

Individual tax return data: The number of donors has increased for some neighbourhoods and remained flat for other neighbourhoods. As the number of tax filers has increased over time, however, the share of tax filers reporting donations has fallen. Donations from higher income neighbourhoods have increased dramatically. Donations from lower income and middle-income neighbourhoods have remained flat or decreased.

Starting first with the individual tax return data, my analysis focused on urban and suburban areas in Canada. I obtained data for the period 1991 to 2010, at a local level, in areas that resemble small neighbourhoods: the area covered by the first three characters of the postal code (known as a forward sortation area, “FSA”), which typically covers 5,000 to 8,000 households. I classify each area as being in the bottom, middle, or top grouping as measured by average household income as reported in the 2006 census.³ In Figure 1, I depict the number of tax filers reporting donations by these three classifications. For the lowest income and middle-income groups, the number of filers reporting charitable donations has remained relatively steady. For the higher income group, the number of filers has increased from more than 1.4 million in 1991 to approximately 1.9 million in 2010. There was a dip in 2008/09 (the period of the most recent recession), but donations appear to be bouncing back.

FIGURE 1 NUMBER OF TAX FILERS REPORTING DONATIONS, BY NEIGHBOURHOOD GROUPING

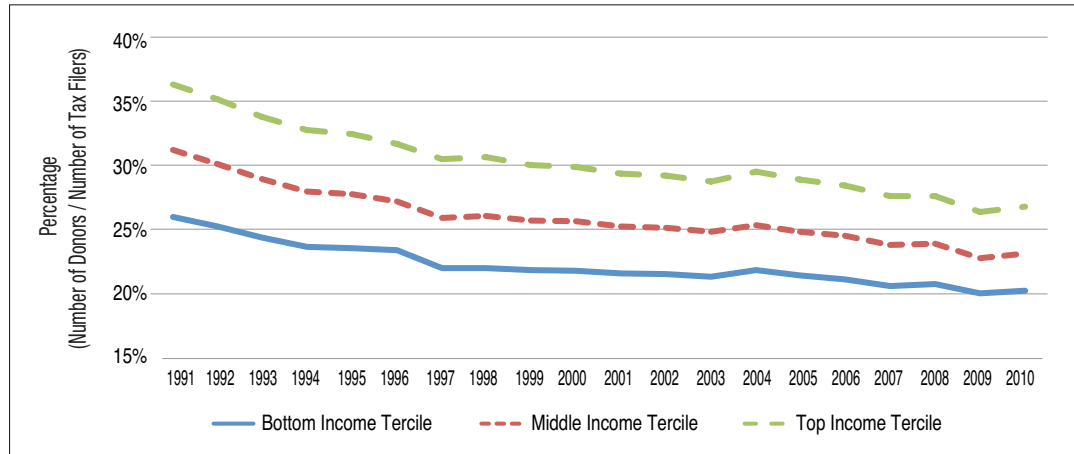


In Figure 2, I report the share of tax filers reporting charitable donations by income group. The share of filers reporting donations has declined across all groups. If the number of tax filers reporting charitable donations has increased overall, why are there claims that there has been a decline in giving by Canadians? There are two likely reasons. First, the number of tax filers has increased over the last two decades. For the neighbourhoods I studied, the number of tax filers increased from 12.4 million to 18.3 million. Thus, if we look at the share of tax filers that report charitable donations (Figure 2), we see that there has been a decline in this share because the rate of growth in tax filers is faster than the rate of growth in donors. Second, we

³ Between 1991 and 2010, neighbourhoods did change with respect to their socio-economic characteristics. I use the 2006 measure of average household income to reflect the most recent information available about each neighbourhood and to allocate each FSA to a single grouping. There are many ways the FSAs could be grouped (e.g. average income over the entire period or average income for the first part of the period). While not all variations were explored, when various different definitions were used to group neighbourhoods, the strongest growth in reported donations was still shown by higher income neighbourhoods.

have a tax system that generally provides greater tax benefits for couples who report their charitable donations on a single tax return. Over the last 20 years, there has been an increase in the use of tax software to complete personal tax returns. Most software programs identify the potential cost savings from combining and reporting donations on a single return. Thus, with these data, it is difficult to discern how much of the decline in the share of tax filers reporting donations is attributable to a wider use of tax software programs, which, ultimately, may be leading more couples to report their donations on one return.

FIGURE 2 SHARE OF TAX FILERS REPORTING TAX-RECEIPTED GIFTS, BY NEIGHBOURHOOD TYPE



In Figures 3a and 3b, I report the total donations (adjusted for inflation) reported by the three neighbourhood groupings. Total giving is relatively flat for those in the lower income and middle-income neighbourhoods. If one adjusts for overall macro-level trends over the period, donations have been falling in the lower and middle-income neighbourhood groups. In both figures, however, there has been significant growth in giving reported by tax filers residing in higher income neighbourhoods.

FIGURE 3A REPORTED TAX-RECEIPTED GIFTS, BY NEIGHBOURHOOD TYPE

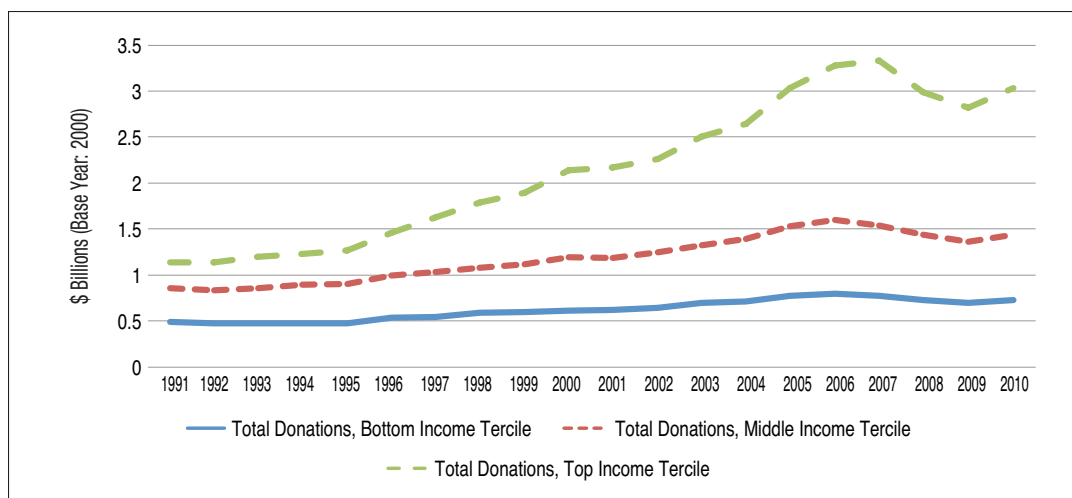
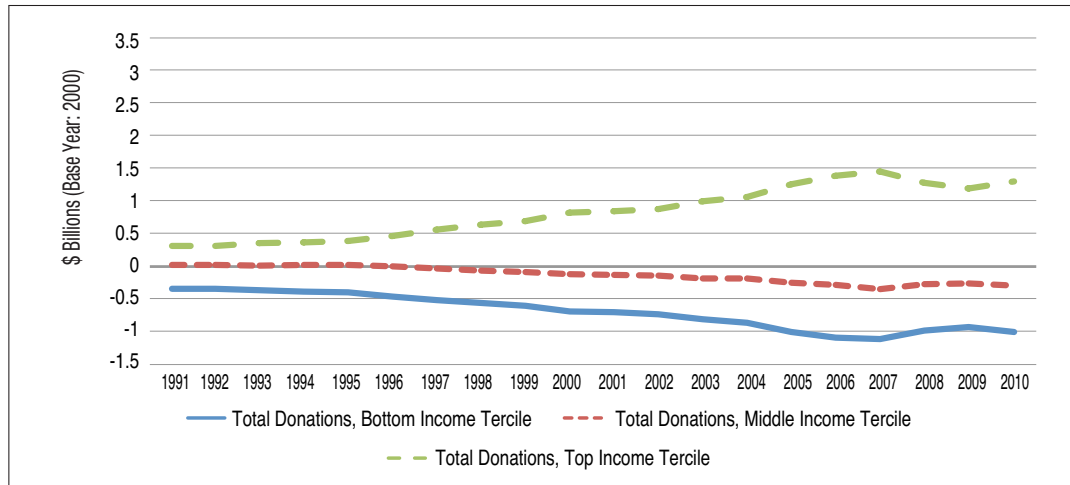


FIGURE 3B: REPORTED TAX-RECEIPTED GIFTS, BY NEIGHBOURHOOD TYPE (REMOVAL OF AGGREGATE-YEAR EFFECTS)



Judging solely from information from individual tax returns, it appears that growth in tax-receipted giving has been driven by individuals residing in wealthier neighbourhoods. This growth, however, has been tempered by slower growth in other neighbourhoods. In other words, while individuals residing in higher income neighbourhoods have been giving more, individuals residing in lower income neighbourhoods have been giving less. Understanding the dynamics of these changes would be greatly enhanced by using individual tax-return data that can be linked across years and across households.

Individual survey data on giving: Donation rates between 2004 and 2010 have remained flat

Recently, Statistics Canada announced the release of the initial results from the 2010 Canada Survey of Giving, Volunteering and Participating. Imagine Canada issued a report comparing the results from this survey with surveys conducted in 2004 and 2007. It found that the share of individuals that identify themselves as donors has remained relatively unchanged.

Approximately 84 to 85 per cent of the respondents identify themselves as donors. It also found that the level of giving, after controlling for inflation, has remained relatively flat. Why is this different from the statistics found in individual tax returns? In part, it can be attributed to differences in what we might consider “donations”: with tax return data, we are specifically considering donations for which a tax receipt has been issued and where the deduction has been claimed by the donor (or her spouse). In the Statistics Canada survey, what constitutes a donation is more broadly defined. It includes any amounts given to charities or nonprofits. At a minimum, it includes amounts that would not qualify for a tax credit.

In the tables issued by Statistics Canada, survey respondents who reported donations differ in their level of giving based on: age distribution (older people give more); income and educational background (people with higher levels of income and education give more); and geographic location.

Charity level data: The numbers of charities has increased in the last two decades. Overall giving to charities increased in the 1990s and 2000s; foundations grew substantially and big charities benefited from increases in direct government funding.

Turning next to data from charities, I have collected and cleaned data from the information returns filed by charities from the early 1990s to the present.⁴ For the purposes of this report, I rely on the cleaned data and examine all charities and foundations that have completed an information return between 1992 and 2008. I exclude returns that cover an accounting period that is shorter than 10 months or longer than 14 months since it is important to study annual changes in revenues. I also exclude returns that are in the top 0.5 per cent of the distribution for revenues from private donations and government grants in each year of study. The reason for this exclusion is that it appears there are returns filed (or transformed into an electronic version) with absurdly high levels of revenues. These high levels of revenues may give a mistaken impression about the patterns in revenues experienced by most charities.

Charities are grouped based on their last known status with CRA: charitable organizations or foundations. In principle, charitable organizations are charities whose primary mission is to deliver goods and services, while foundations have a primary mission to raise funds and then distribute these funds to charitable organizations. The further classification of a foundation as a private or public foundation depends in part on the number of contributors to the foundation and the relationship between the foundation and its contributors. The difference between public and private foundations lies primarily in legal definitions that pertain to the relationship (arm's-length or not) between donors and the directors of the foundation. A public foundation is one with an arm's-length relationship between the directors and donors, and often involves many funders — for example, a community foundation. If a foundation receives the bulk of its donations from a few donors and/or maintains a non-arm's-length relationship with its donors, it is likely to be classified as a private foundation.

The number of charitable organizations increased...so did the number of foundations. Growth in giving to foundations, however, surpassed the growth in giving to charitable organizations.

The first set of figures examined in this section pertain to the growth in the number of charities in Canada and the distribution of these charities across broadly defined categories, which are based on the most recent category code that CRA has assigned to the charity. In Figures 4a and 4b, I depict the distribution of charities, by category, in 1992 and 2008, respectively. In 1992, there were approximately 58,000 charities and by 2008 the number had grown to approximately 73,000. At both the beginning and end of the measured period, those organizations classified as religious charities (churches, synagogues, mosques, etc.) represented

⁴ To this day, returns from charities are filed manually with CRA. To create an electronic version, the returns must be scanned and/or input by hand. The data obtained from CRA, therefore, may suffer from a variety of data quality issues. The first issue pertains to the quality of the information provided by the charity. Many charities rely on volunteers to complete returns. From year to year, the person who completes the return may change. As the format of the information returns varies (there have been three significant changes in the forms since the early 1990s), the interpretation of the questions asked on the form may also vary. The second issue pertains to the quality of the transformation of the information return from a paper to an electronic version. As a result of these issues, it is important, as with any data set derived from administrative data, to explore the data and to try to resolve idiosyncrasies before using the data in analysis. I have spent the last several years developing methods that help make it feasible to use the information return as a more reliable source for research analysis.

the greatest number of charities, followed by those focused on welfare, education, and community-related work. While the share of charities falling within the religious category declined, the actual number of religious charities increased, from approximately 28,000 to 32,000. In contrast, the number of welfare-related charities increased from about 8,600 to nearly 13,000. The distribution across other categories remained fairly proportionate.

FIGURE 4A 1992 DISTRIBUTION OF CHARITABLE ORGANIZATIONS

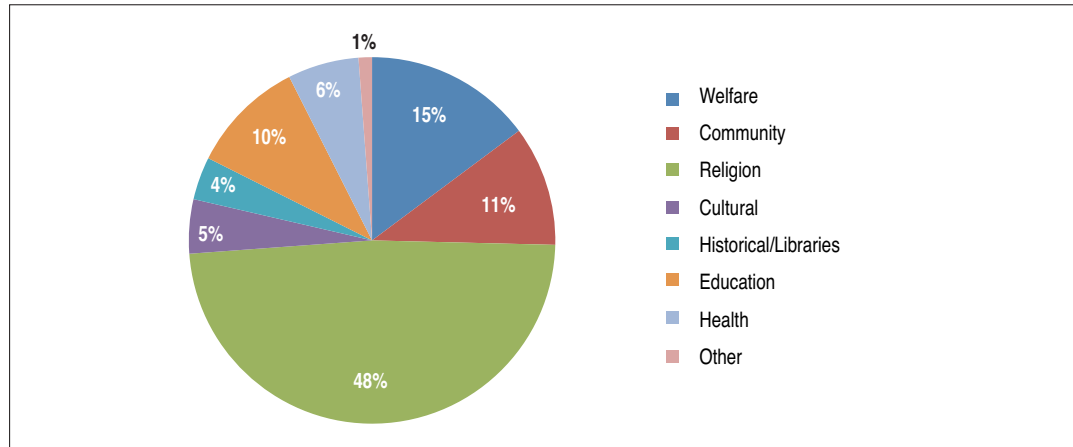
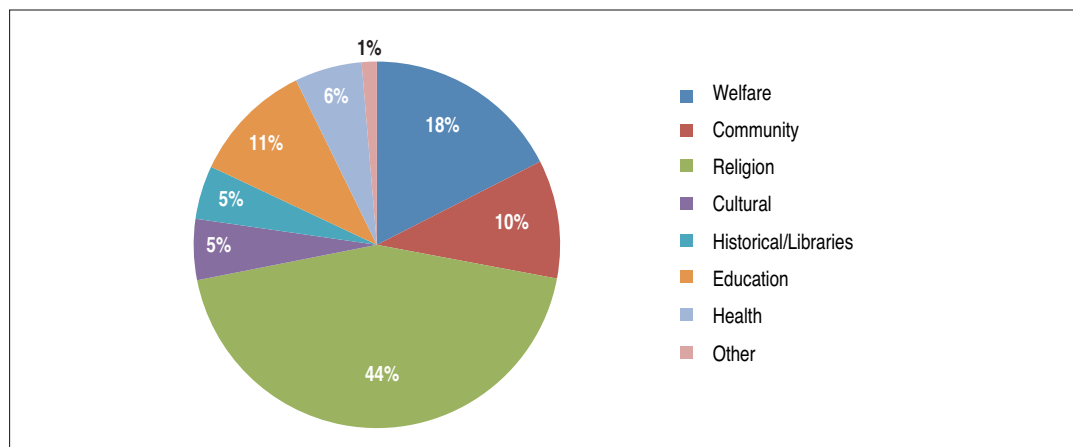


FIGURE 4B 2008 DISTRIBUTION OF CHARITABLE ORGANIZATIONS



Another way to compare the distribution of charitable organizations is to compare total tax-receipted gifts and/or total revenues (excluding capital gains) reported by the charities. Overall, tax-receipted gifts grew by about 56 per cent between 1992 and 2008. Total revenues (excluding capital gains) grew by 154 per cent. In 1992, approximately 51 per cent of reported tax-receipted gifts were donated to religious charities, while between 10 and 12 per cent of tax-receipted gifts were donated to each of the groups of charities classified as welfare, education, health and “other” (with remaining groups, such as “community,” “historic/libraries” and “cultural” each representing two per cent of donations, or less). By 2008, the share of tax-receipted gifts to religious charities declined to 48 per cent and the share of gifts to welfare- and education-related charities increased to 14 and 17 per cent, respectively.

By looking at total revenues, we can count funding not only from private sources but also direct funding from public sources. The share of total revenues collected by religious charities fell from nine per cent in 1992 to five per cent in 2008. There was little change in the share of revenues collected by welfare charities (which remained relatively flat, around nine per cent), community charities (relatively flat at just over two per cent), education charities (which stayed at approximately 36 per cent) and “other” charities (which continued to hover around three per cent). The share of total revenues that went to health-related charities increased from 37 to 43 per cent, while arts and cultural charities saw their share decline from 2.2 to 1.4 per cent.

In Figures 5a and 5b, I depict the distribution of foundations — public and private — in 1992 and 2008, respectively. Over this period, the number of foundations nearly doubled. In 1992, a high proportion of foundations were classified as welfare-related, education-related, and health-related. By 2008, there had been a shift in the distribution, with a substantial increase in the proportion of foundations classified as welfare-related.

FIGURE 5A 1992 DISTRIBUTION OF FOUNDATIONS

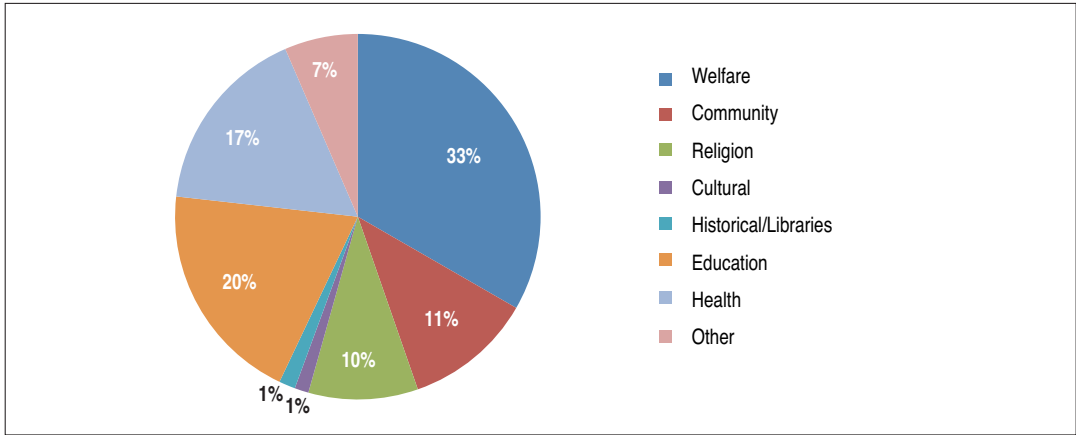
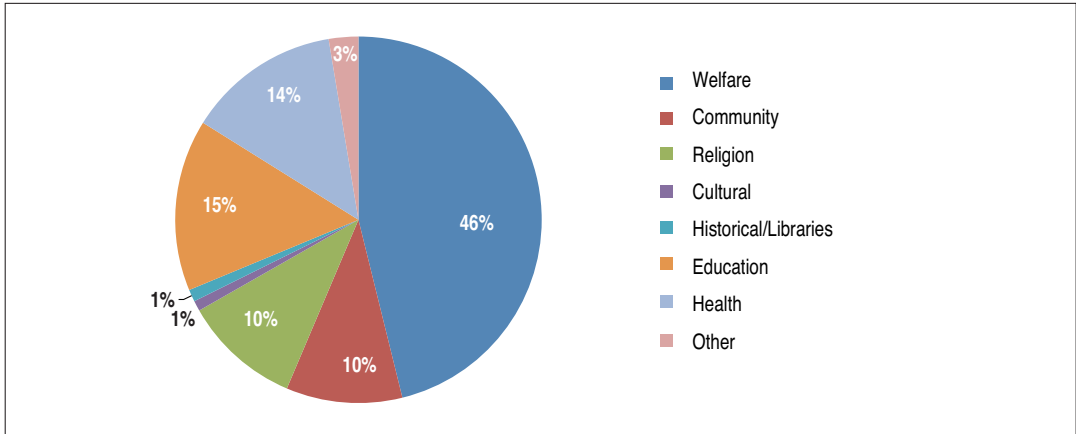
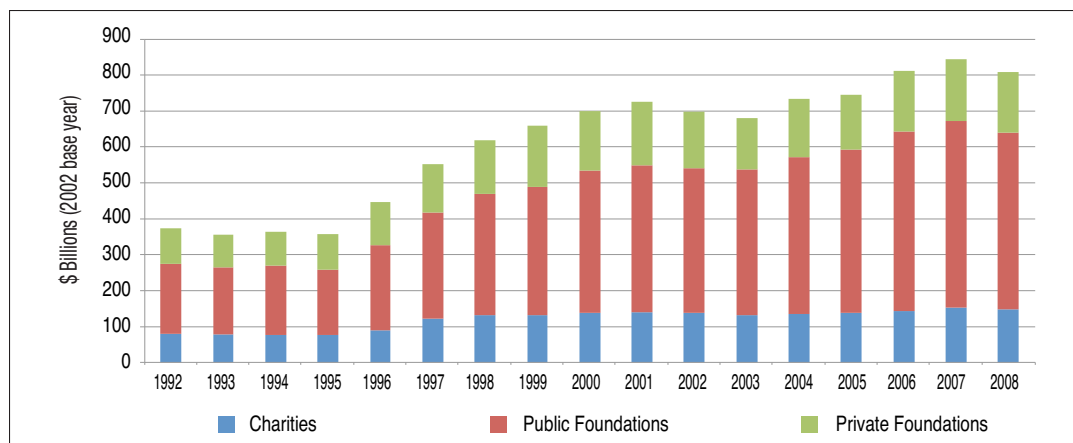


FIGURE 5B 2008 DISTRIBUTION OF FOUNDATIONS



If the number of charities is increasing, how has that affected donations to charities? I depict in Figure 6 the total donations over the same period that charities collected from: tax-receipted donations; donations from other sources (except those from other charities or foundations); and revenues from fundraising activities for the three groups of charities. Overall, there was a growth in donations from approximately \$4 billion in 1992 to more than \$9 billion in 2008 — an overall increase of more than 130 per cent over a 16-year period. Contributions to charitable organizations increased around 117 per cent, whereas contributions to foundations increased more than 250 per cent. While these donation statistics show tremendous growth over a 16-year period, it is more difficult to measure that growth in a context that relates it to some measure of the changing need or importance of the goods and services these charities provide. For one thing, over this 16-year period, Canada’s population increased by approximately five million. Moreover, the biggest donation growth was in contributions to foundations. In general, foundations disburse funds to charities, but they do so over time, meaning that not all of these contributions were actually used over the same 16-year period to support the goods and services delivered by charities.

FIGURE 6 TOTAL REPORTED DIRECT DONATIONS AND FUNDRAISING REVENUES, BY CHARITY TYPE



Medium-sized and large foundations benefited the most from private contributions. Contributions to small foundations were flat over the period.

Have all charities and foundations experienced similar growth in giving? To best answer this question, given the wide range in charity sizes, I narrowed the set of charities and foundations to those that existed prior to 1995 and continued to exist after 2005. In addition, I only looked at those charities for which we have at least 10 years of data. Thus, for the next set of figures, I exclude charities that have started up in the latter part of the sample period and those that have closed down during most of the period.

To best explore potential differences in the growth of public and private revenues across size, I grouped the charities based on the average of their total reported revenue (excluding capital gains) for the years 1992, 1993, and 1994. A small organization is one that had reported total revenues of less than \$100,000 (including 60,853 charities, 3,935 public foundations and 3,811 private foundations). A medium-sized organization is one that had average revenues between \$100,000 and \$1 million (including 26,867 charities, 1,676 public foundations and 1,643 private foundations). A big organization is one that had average revenues of more than \$1 million (including 5,863 charities, 516 public foundations and 494 private foundations).

Figures 7a and 7b depict the average of total private contributions to foundations (public foundations depicted in Figure 7a and private foundations in Figure 7b) in each of the three size groupings. What is striking about both charts is the difference in the growth rates for big foundations relative to the small and medium-sized foundations. Average revenues from private giving grew from approximately \$1 million to almost \$3 million over the period. Medium-sized foundations, saw contributions from private giving grow from an average of \$150,000 to \$450,000 — an increase of about the same rate. While the average revenues for the medium-sized foundations are about one-third less than those reported by big foundations at the end of the period, the growth rate provides some evidence that the public foundation sector is seeing a rise in the number of foundations with good revenues. In contrast, the average growth in revenues from the private foundation sector has been much flatter.

FIGURE 7A AVERAGE REPORTED DONATIONS AND REVENUES FROM FUNDRAISING FOR PUBLIC FOUNDATIONS

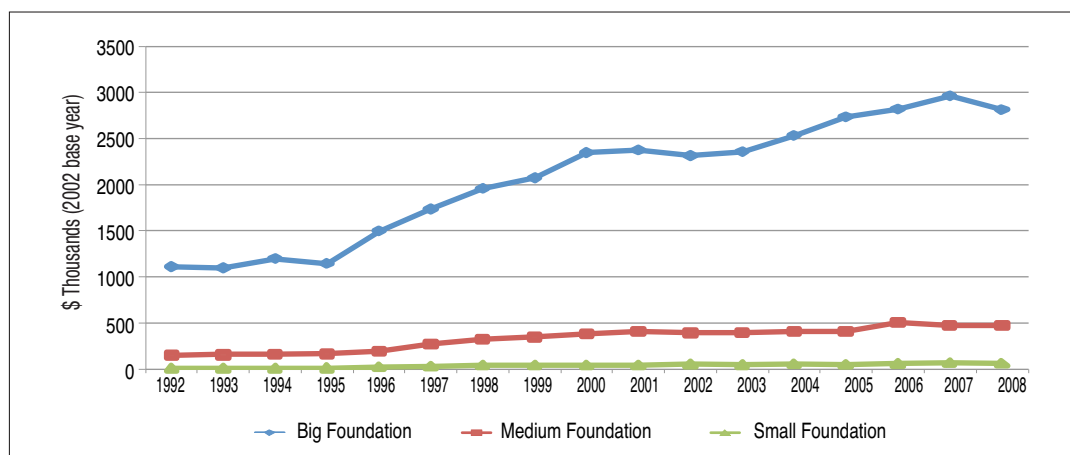
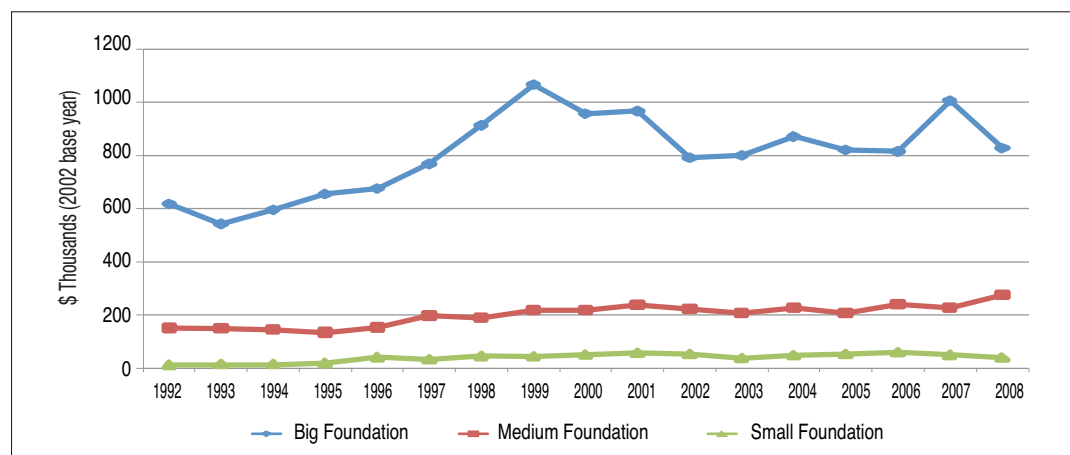


FIGURE 7B AVERAGE REPORTED DONATIONS AND REVENUES FROM FUNDRAISING FOR PRIVATE FOUNDATIONS



The next set of figures depicts changes in average private contributions to charitable organizations. The set also depicts average government funding to charitable organizations. While there has been much discussion about the merits of changing tax policy to promote greater charitable giving, a government offering a larger giveaway of tax credits will also decrease its revenue, inevitably making less public money available for direct government funding to charities.

Figure 8a depicts growth in government funding and private contributions for big charitable organizations. The average government grant far exceeds the average level of private revenues: At the beginning of the period, the average government grant was \$5.8 million and the average level of private giving was \$382,000. Because these figures depict average levels for the group of charities classified as big organizations, it masks differences across the charities in terms of their reliance on government and private funding. For the most part, both government funding and private giving increased over the period. Private giving increased most dramatically in the mid- to late-1990s and there is evidence of a slight dip at the end of the period. The growth in government grants to these charities increased more steadily. In Figure 8b, I depict the average private and public contributions to small and medium-sized charities. Both groups of charities have experienced, on average, greater growth in government grants than in private giving. The overall gap in private revenues grew between small and medium-sized charities, especially when we take into account that there are close to 61,000 small charities and 28,000 medium-sized charities that reported revenues for at least 10 years over the period.

FIGURE 8A AVERAGE FUNDING FROM PUBLIC (GOVERNMENT) AND PRIVATE (DONATIONS AND FUNDRAISING) SOURCES FOR CHARITIES WITH AVERAGE REVENUES > \$1 MILLION PER YEAR

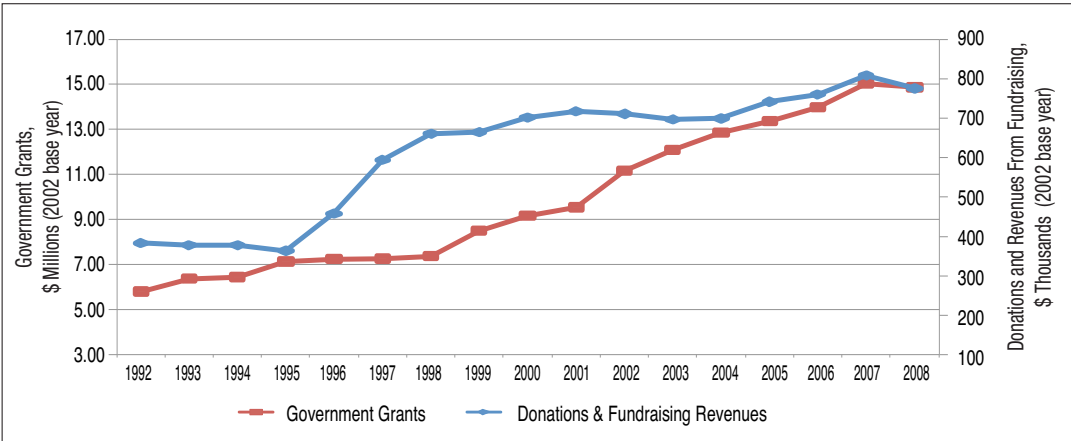
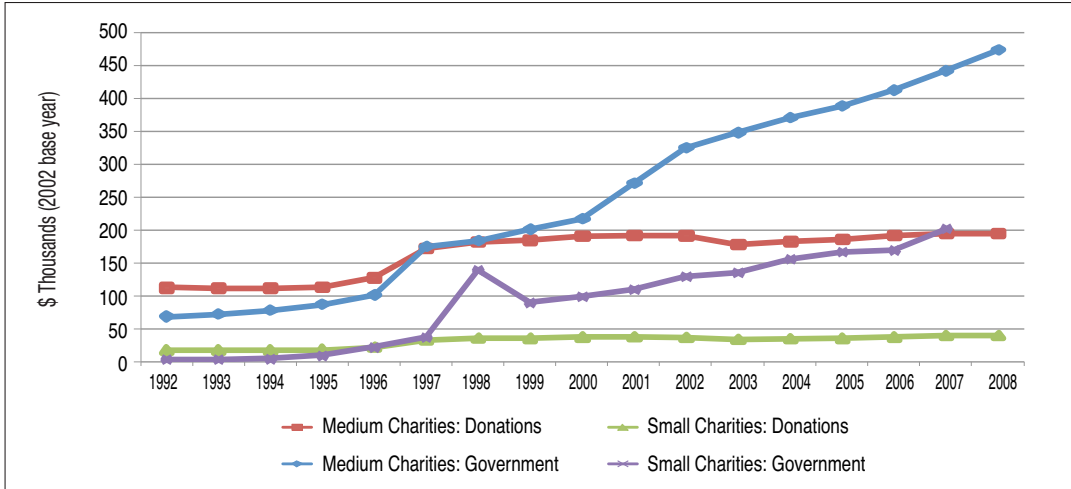
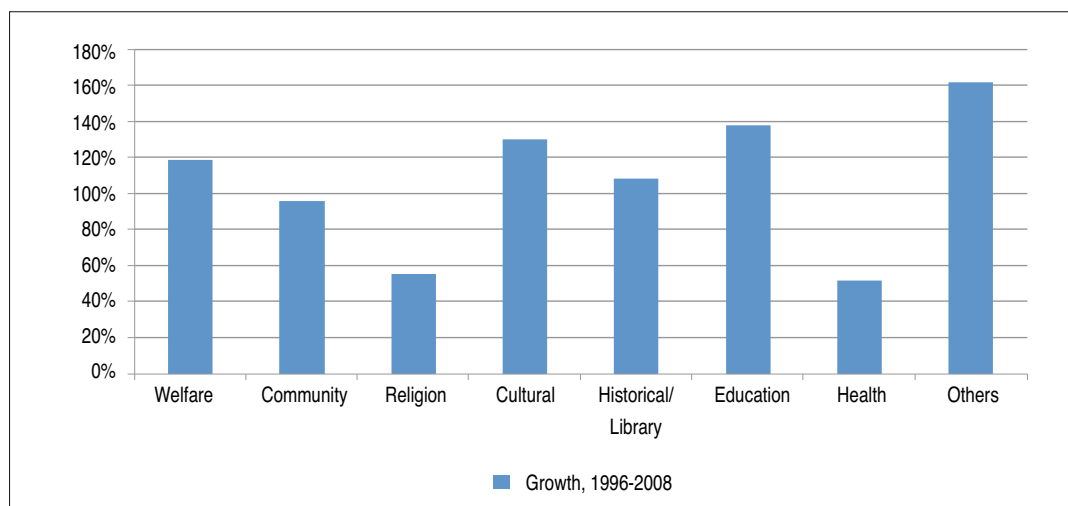


FIGURE 8B AVERAGE FUNDING FROM PUBLIC (GOVERNMENT) AND PRIVATE (DONATIONS AND FUNDRAISING) SOURCES FOR MEDIUM (\$100K - \$1MILLION) AND SMALL (<\$100K) CHARITIES



Another issue to consider when thinking about the growth in private giving to charitable organizations is whether the growth is similar across different charity types. In Figure 9, I depict the overall growth in private giving by charity type for the period 1996 to 2008. The greatest growth is seen in the charity grouping “other.” Charities in the education group also experienced high growth in private giving. Surprisingly, charities in the health group and religious group experienced the lowest level of growth. One explanation for the relatively low growth in private donations to health-related charities could be that, if part of the growth in private donations to foundations is directed towards health-related areas, then this might reflect a shift from certain donors contributing to health charities directly, and instead concentrating their giving to health foundations. Given that there is a small proportion of foundations identified in the religious group, that same possible phenomenon could not be used to explain the lower growth in giving to religious organizations.

FIGURE 9 GROWTH IN DONATIONS AND REVENUE FROM FUNDRAISING (1996 - 2008)



DISCUSSION

Based on the simple statistics depicted above, several stories begin to emerge. The first story is that growth in giving may largely be attributable to those in higher income brackets. This, in part, may be the result of changes in tax policy regarding the giving of such things as publicly traded securities and other donated items that are more likely to be held by higher income individuals. To truly understand whether this is one cause of increased giving by higher income individuals, however, would require a study involving using individual tax-return data.

A second story is that giving by individuals in lower income and middle-income neighbourhoods has, at best, remained flat, but has more likely declined. This decline, however, may be more attributable to an increase in the population than a change in individual giving behaviour. This raises the question of why overall giving has declined as our population has grown. And why do we observe a decline in giving if we study individual tax returns, but we don't observe a similar decline when we use the results from the Canadian Survey of Giving, Volunteering and Participating?

A third story is that the number of charities and foundations has grown substantially over the last two decades, but larger charitable organizations and foundations have enjoyed the greatest growth in giving and in direct government funding. Private and public support has been flatter for smaller charities and foundations.

Should these stories concern us? Possibly. I encourage further exploration of each story to understand in more depth the extent to which we are observing important changes in charitable giving and the potential impact of these changes on charity operations. This discussion below provides some direction for thinking about these stories, relying on current and past research on related topics.

What explains a decline in giving? What explains a lower growth in giving to smaller charities?

In the first story we saw that, while the number of donors has increased, the share of tax filers reporting donations has declined. In part, this decline is attributable to a growth in our population. Why would population growth decrease giving? There are several plausible explanations. One is that, as our population has increased, Canada has become a more diverse population. As the population becomes more diverse, the interest in supporting charitable goods and services becomes more diverse and so it becomes more difficult for charities to respond to these more diverse interests.

Andreoni, Payne, Smith, and Karp⁵ explore the effect that changes in neighbourhood diversity has on charitable giving, using the grouped data from individual income tax returns in Canada. In urban areas across Canada and elsewhere, neighbourhood diversity is increasingly common. Diversity in communities is something that most Canadians would view as positive. From a public economics perspective, however, public-good provision has been observed in numerous studies to decrease with increases in diversity — this includes a decrease in spending on hospitals, roads, and schools.⁶ If diversity results in fewer public goods, is the same true for charitable goods? Standard economic models suggest that the prediction of this effect is unclear. If charities benefit individuals outside of one's group, or provide services that are of concern to certain types of groups but not others, diversity may result in less giving by the members of the group that are not being serviced by the charity. On the other hand, if individuals group together based on characteristics such as ethnicity or religion, then organizations that cater to those groupings may enjoy an increase in giving. Andreoni, Payne, Smith, and Karp use a measure of diversity called a fragmentation index that combines the share of neighbourhood populations based on visible minority status or religious status. They find that, while the average adult contributes approximately \$200 per year to charity, a 10 percentage-point increase for ethnic composition on the fragmentation index implies a decrease in giving of \$27, a decline of 14 per cent. An increase in religious diversity in the neighbourhood also suggests a decline in giving, but the estimates from the analysis of religious diversity are estimated with less precision.

⁵ James Andreoni, A. Abigail Payne et al., "Diversity and Donations: The Effect of Religious and Ethnic Diversity on Charitable Giving," NBER Working Paper #176118, in submission (November 2012).

⁶ A. Alesina, R. Baqir, et al., "Redistributive Public Employment," *Journal of Urban Economics* 48(2) (2000): 219-241; A. Alesina, R. Baqir, et al., "Public Goods And Ethnic Divisions," *The Quarterly Journal of Economics* 114(4) (1999): 1243-1284; James M. Poterba, "Demographic Structure and the Political Economy of Public Education," *Journal of Public Policy Analysis and Management* 16(1) (1997): 48-66; C. Goldin and L. F. Katz, "Human Capital and Social Capital: The Rise of Secondary Schooling in America, 1910 to 1940," *Journal of Interdisciplinary History* 29(4) (1999): 683-723.

Do charities play a role in giving?

When we discuss charitable giving, we often assume that charities are passive in their collection of donations. Yet we know that most charities ask individuals to give. Some individuals are active in their giving and seek out information about charities. Other individuals, however, may be more passive, or may not know how to gather information about charities. And so, charities may need to fundraise in order to both ask individuals for contributions, and as a way to advertise or provide information about their goods and services. Fundraising, however, sometimes carries with it a negative connotation. Moreover, many charities may prefer to focus their efforts on the provision of goods and services, rather than raising revenues for their operations. Using data from the U.S. and from Canada, Andreoni and Payne⁷ find that, typically, for every dollar spent by charities on fundraising and promotional activities, an average of five dollars is raised in private donations. These estimates correspond with other research on the impact of fundraising on private giving. In standard economic theory, charities are not behaving optimally; instead, these estimates suggest that charities may view fundraising as a necessary evil.

How does direct government funding of charities impact private giving?

In the past, the theory around how government funding impacts private giving has viewed charities as passive recipients of private donations. The extent of the impact that government grants can have on private giving depends on (a) how individuals value a charitable good and (b) the level of information the individual has on private giving. Individuals may care only about the provision of the charitable good, regardless of the source of funding. Under this assumption, an increase in government funding is predicted to decrease private giving, dollar for dollar. If, however individuals receive some private benefit (commonly called a “warm-glow effect”) in knowing that part of the charitable good is coming from their donation, then traditional theory would lead us to expect that an increase in government funding would still decrease private giving, but at a lower rate than dollar for dollar. In research using data from the U.S. and the U.K., Payne⁸ and Khanna, Posnett and Todd⁹ find that, when government funding increases, private donations decline, but at a rate that is less than dollar for dollar.

Alternatively, what if a donor has a difficult time assessing the value of a charitable good? Take for instance, a gift to support research in health, or other areas. Do most individuals know how to value a research project? In this instance, it may be that the government grant serves as a signal of quality. If so, then we would observe an increase in private giving when we observe increases in government grants. Payne¹⁰ observes this effect when studying research funding to universities.

⁷ James Andreoni and A. Abigail Payne, “Crowding-Out Charitable Contributions in Canada: New Knowledge from the North” (Mimeo, McMaster University, 2012); James Andreoni and A. Abigail Payne, “Is Crowding Out Due Entirely to Fundraising? Evidence From a Panel of Charities,” *Journal of Public Economics* 95(5-6) (2011): 334-343.

⁸ A. Abigail Payne, “Does the Government Crowd-Out Private Donations? New Evidence From a Sample of Non-Profit Firms,” *Journal of Public Economics* 69(3) (1998): 323-345.

⁹ Jyoti Khanna, John Posnett and Todd Sandler, “Charity Donations in the UK: New Evidence Based on Panel Data,” *Journal of Public Economics* 56(2) (1995): 257-272.

¹⁰ A. Abigail Payne, “Measuring the Effect of Federal Research Funding on Private Donations At Research Universities: Is Federal Research Funding More Than a Substitute for Private Donations?,” *International Tax and Public Finance*, 8(5-6) (2001) 731-751.

But what if charities are not passive recipients of private donations? If charities must engage in efforts to fundraise and/or promote their charity, and view such fundraising as a necessary evil, to what extent do they decrease their fundraising efforts when they receive a government grant? Andreoni and Payne¹¹ observe this effect when studying American arts and social-welfare organizations. This decrease in fundraising results in declines in private giving. Using data from the U.S., Andreoni and Payne¹² find that the bulk of the decline in private giving that occurs when an American charity receives a government grant is attributable to a decline in fundraising.

Is this decline in giving also true for Canada? In preliminary work by Andreoni and Payne,¹³ they find a similar effect. Overall, they find that a one-dollar increase in government funding reduces private giving by 80 to 98 cents. The bulk of this decline is attributable to a decline in revenue from fundraising activities. Funding from foundations and similar organizations also declines as government funding to the charity increases.

Can government policy counteract this crowding out effect from government funds? Possibly. One obvious response would be the use of matching grants. However, if an organization cannot raise the matching funds privately, then the government funding may be given to another organization that may or may not make the most effective use of the funding. Another option would be to find ways to encourage a grant-receiving charity to continue to fundraise and seek private giving. But this too has its challenges. While some fundraising is beneficial, as it helps to raise awareness about the charity and the goods and services it provides, it also can be wasteful and it detracts time and funding for the direct provision of the goods and services provided by the charity.

Is the significant growth in giving to foundations a good thing?

Based on data from 2008, of the 25 wealthiest charitable foundations in the world, none are Canadian. Foundations from the United States claim 18 of the spots. The United Kingdom comes in second with three foundations. The top three foundations in the world are the Bill & Melinda Gates Foundation (endowment of US\$37.1 billion; founded in 1994), the Stichting INGKA Foundation in the Netherlands (endowment of US\$36 billion; founded in 1982), and the Wellcome Trust in the United Kingdom (endowment of US\$22.9 billion; founded in 1936).

By comparison, based on amounts reported on the information return to CRA in 2011, it appears there are only a couple of Canadian foundations with more than \$1 billion in assets: The MasterCard Foundation (\$2.3 billion) and the Lucie and André Chagnon Foundation (\$1.3 billion). Of the nearly 5,000 Canadian foundations that have operated over the last 20 years, fewer than 15 per cent (750 foundations) have average annual levels of assets of more than \$1 million. Of course, there are some notable charitable organizations (not foundations) with relatively high levels of assets. Most notably, several universities have substantial assets. For

¹¹ James Andreoni and A. Abigail Payne, "Is Crowding Out Due Entirely to Fundraising?," (2011); James Andreoni and A. Abigail Payne, "Do Government Grants to Private Charities Crowd Out Giving or Fundraising?," *The American Economic Review*, 93 (2003) 792–812.

¹² James Andreoni and A. Abigail Payne, "Is Crowding Out Due Entirely to Fundraising?" (2011).

¹³ James Andreoni and A. Abigail Payne, "Crowding-Out Charitable Contributions in Canada: New Knowledge from the North" (2012).

example: University of Toronto (\$4.6 billion); University of British Columbia (\$4.4 billion); McGill University (\$3.3 billion); University of Calgary (\$2.9 billion); McMaster University (\$1.9 billion); Queen's University (\$1.7 billion); and University of Waterloo (\$1.4 billion). But these assets are generally used by the recipient charitable organization, while foundations have the ability to spread their wealth across a number of charitable organizations.

For the most part, the growth in the wealth amassed by foundations over the last two decades should be welcomed. Whether the growth makes Canada more comparable to other developed countries, once we take into account population differences and other factors, is an open question. Most likely, Canada remains on the lower end of the spectrum. Why might supporting foundations be beneficial for charitable organizations? If foundations are adjuvant in distributing their funding, they can help stabilize charity funding during times of economic turmoil. Potentially, foundations can be more strategic and nimble with their funding than governments can, given that they are not encumbered by the added layer of politics. Moreover, the sole purpose of foundations is to support the charitable sector. Governments face pressures from many sources.

In preliminary research, Kryvoruchko¹⁴ presents a model suggesting that foundation grants to charitable organizations may help provide a positive signal to individual donors about the quality of the charitable organizations. In her model, she assumes that finding information about charities, and the quality of the goods and services provided by these charities, may be difficult for the typical donor. Foundations, however, may engage in efforts to better understand the activities of the charities they fund. Using data on grants to charitable organizations from Canadian foundations, Kryvoruchko's initial findings suggest that, indeed, a charity that receives a grant from a foundation will also enjoy an increase in individual donations to the charity.

Is there a silver bullet to encourage giving? Would changing the tax system help?

Data on charities and individual giving suggest that, over the last two decades, the bulk of the growth in giving has come from individuals from higher income neighbourhoods, and has been directed to larger charities and foundations. This may be partly attributable to changes in federal tax policy, which has provided increased tax incentives for individuals donating publicly traded securities and other types of donations that are more likely to be held by higher income individuals. Whether there is a causal link, however, requires more research. But if this hypothesis is true, does it mean that if we create incentives for lower income individuals to donate more (e.g. through a "stretch" tax credit), they will respond accordingly?

The theoretical basis for thinking about how tax policy might affect giving is based on the notion that, if a tax credit is given for a donation, it effectively lowers the price of giving. If giving is treated like a standard good (e.g. a cup of coffee, a house, or any consumable item), a lowering of the price should result in greater demand for the good. For charities, this would

¹⁴ Kryvoruchko, Iryna, "Does Foundation Giving Stimulate or Suppress Private Giving? Evidence from Canadian Charities" (Mimeo, McMaster University, 2012).

mean that lowering the price of giving should motivate individuals to give if they have not given previously or, if they have historically given, to give more. Bakija and Heim¹⁵ summarize the research that studies how changes in the price of giving impacts giving (most of this research uses American data). In contrast, however, Rehavi¹⁶ documents that in the U.S. there is an underreporting of donations on individual tax returns, which suggests that a change in the price of giving through the tax system does not impact all donors. For the most part, a reduction in the price of giving results in an increase in giving. This then raises the question of whether a reaction to a change in the price of giving is due to a permanent or a transitory shift in giving by the individual. A transitory shift is effectively one where a donor has already planned to give, but shifts their giving to favour tax policy incentives, and is mostly attributable to fluctuations in her income. A permanent shift is one where tax policy encourages an individual to smooth their giving out over time, and a change in policy encourages them to re-optimize their preferences about giving.¹⁷

In a recent working paper, Charles Clotfelter¹⁸ discusses issues related to charitable giving and tax policy in the United States. One important insight he provides on the U.S. system that is equally true in Canada, is his consideration of whether our tax system should favour individuals of one income group over another. Unlike the U.S., our system of providing tax credits for donations, instead of a tax deduction, does indeed mean a more equitable treatment of donations across all taxpayers. But where we fall short from a tax-equity perspective is the more favourable treatment of non-cash donations such as gifts of publicly traded securities and land. If higher income individuals are more likely to hold these assets, then they receive a greater benefit from their donations than those that do not hold these types of assets.

But is a change in tax policy a costless endeavour? Presumably not. Assume the government chooses to introduce a policy that increases the tax credit given for a charitable contribution. A specific credit that is targeted at any cash donation would surely reduce tax revenue collected by the government. On the other hand, a credit that is targeted at an instrument such as a publicly traded security, may or may not represent lost revenue to the government. If an individual owner of a security was planning to sell it in any case, and instead decides to avoid the potential capital-gains tax by giving that security to a charity, rather than selling it on the market, then that would result in lost revenue for the government. If, however, the individual had no plans to sell the security, but is induced by tax incentives to give it to charity, then there would be no immediate foregone government revenue. Any foregone revenue would be tied to the ultimate sale of the security that would have happened at some undetermined point in the future.

¹⁵ Jon Bakija and Bradley Heim, “How Does Charitable Giving Respond to Incentives and Income?” (2008).

¹⁶ Marit Rehavi, “Partial Reporting: An Example from Charitable Giving” (Mimeo, University of British Columbia, 2010).

¹⁷ Raj Chetty, “The Simple Economics of Salience and Taxation,” NBER Working Paper #15246 (2009).

¹⁸ Charles T. Clotfelter, “Charitable Giving and Tax Policy in the U.S.” (Mimeo, Duke University, 2012).

For the sake of argument, assume that any new tax policy results in a loss of revenue to the government. Is this a good thing? On one hand, the donor who takes advantage of the tax policy is able to direct her donation to the charity and, ultimately, the type of good and service she is most concerned about. On the other hand, if the government sees a decline in revenues from the foregone taxes, this reduces its ability to directly support charities through government grants and contracts. If the government has better information about, or can better monitor, charity activities than private donors, then the shifting reliance by charities to private individuals for support may not be a good thing. Ultimately, we are seeking a balance between private and public support of charitable goods and services.

Clotfelter¹⁹ compares the private and public expenditures on social goods as a percentage of GDP based on data from 2011 OECD Social Expenditures statistics for seven countries (Australia, Canada, France, Germany, Netherlands, the United Kingdom, and the United States). On a scale of highest to lowest public expenditures, Canada ranks fifth and looks very similar to the United States and Australia. With respect to private expenditures (i.e. those generated by charities and non-governmental units), Canada ranks third, just below the Netherlands and the United Kingdom, and well above the fourth-ranked country, Australia. Overall, however, Canada ranks sixth out of the seven countries. Thus, while we can boast that Canada has a relatively high level of givers if we analyze data from different sources, it seems that Canada still falls in the lower end of the distribution when it comes to overall levels of giving, despite the growth in our charities over the last decade.

It is likely that there is no silver bullet that will help charities. Our knowledge of charity operations and charitable giving remains relatively primitive. We have data, theories and many testable hypotheses. The government is an important player in supporting charitable goods and services. But there are other important players.

CONCLUSION

The purpose of this report was to highlight the changing landscape for giving over the last two decades to better understand charitable giving and charity operations, using the rich data sources that we have. While the landscape has changed, the policies we should implement to strengthen and improve the provision of charitable goods and services is less clear. Overall giving has increased, as has the number of registered charities and foundations. The sources for private giving, however, have shifted to Canadians with high incomes. Moreover, not all types of charities have benefited from this growth in giving.

At this stage, most, if not all, of the proposed changes to the treatment of donations and charities lack serious evidence-based analysis that should serve as a foundation for implementing change. Conjectures and unsubstantiated beliefs should not be the basis for making decisions. As we move forward in developing policies to help charities, some key guiding principles should include the consideration of:

- The balance between private and public support for charitable goods and services.
- The benefits of tax incentives for different groups of taxpayers.

¹⁹ Charles T. Clotfelter, “Charitable Giving and Tax Policy in the U.S.” (2012).

- The differences in the operations and needs of charities based on size and mission, and how charities may be differentially affected by changes in tax policies.
- The importance of striking the right balance between promoting the long-term sustainability of charities and addressing their short-term needs or fluctuations.

Overall, this report highlights the importance of engaging in more analysis on giving and on charity operations, prior to the adoption of new policies or the revocation of existing policies.

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