

Taking Public Funding Away from Government:

A proposal to replace the direct funding of charities by the federal government with income tax donations

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This paper will present a simple but bold proposal. It proposes to end most direct funding by the Canadian federal government of the charitable sector. Instead, it is proposed that Canadian taxpayers be given the option to donate a small amount of their federal income taxes *directly* to charities. This proposal aims to be revenue neutral. That is, it would not cost the federal treasury any more money than is currently spent on charitable sector funding or deprive it of any more revenue than is currently “lost” through charitable tax deductions. Rather, it would roll almost all federal spending and tax concessions to the charitable sector into one direct tax deduction and let individual taxpayers to decide how this money should be allocated. This is a radical but entirely workable solution. The two fundamental questions surrounding this proposal are: Why and How? That is: Why is this a desirable reform? And how would it actually work?

The ideological underpinnings for this proposal rest on the conception of liberal democracy as the founding principle of the Canadian polity. While liberal democracy is a broad and often contested concept, it is loosely defined as a political system which does the following: 1) highly values and protects civil liberties, such as freedom of expression and association and freedom from arbitrary arrest and detention; 2) allows individuals to choose governments, through periodic elections, that are responsible to the majority will;ⁱ 3) respects and protect minorities and dissenting views from the potential “tyranny of the majority.” These conditions would appear to accurately describe contemporary Canadian values. In keeping with the first point, it is asserted that a liberal democracy should be a form of government in which citizens enjoy maximum freedom from state control. The state should perform only essential functions or provide services that individuals cannot

provide or afford by themselves. None of this should be taken to mean that a liberal democracy cannot also be a generous welfare state whose size and scope may be the subject of legitimate political debate. Even the very concepts of “essential functions” and what, indeed, government alone “must” do are essentially contestable concepts. However much room this may leave for debate, though, one principle still remains: if a society is to conceive of itself as liberal, it must, whenever possible, establish clear boundaries between state and citizen.

It is asserted that the role of the third sector in a liberal democracy should still be rooted in classic liberal theory. Although the modern state is far larger than the classic liberal model, this paper contends that the fundamental values of liberalism still apply to the modern, democratic welfare state. In classic liberal theory, the third sector exists to meet an “unsatisfied demand” for “public goods.”ⁱⁱ That is, to supply goods and services that neither the market nor government will supply. The reason the market doesn’t supply them is simply that it is not profitable to do so. For example, laudable as giving food to the poor might be, there is obviously no money to be made from doing so. However, the reason that government does not supply such services is that there is no democratic consensus that they are legitimate core functions of the state. For instance, the state supplies roads and sewers, and in modern times even education and health care, because there is widespread consensus – in fact, nearly unanimous consensus – that it should. However, there is no similar consensus that the state should provide such specific services as Christmas gifts for poor children, clean needles for intravenous drug users, or extra food for those on social assistance. However laudable such activities might be, they are still not considered quite worthy enough for the state to undertake, and hence use its

coercive power of taxation to make everyone fund them.¹ This is why a distinction between the state and third sector remains critical in modern free societies, even for those that, like Canada, have embraced a larger social welfare state. This distinction still ensures that the coercive power of the state is not used to promote projects for which there is not yet democratic consensus.

Direct funding of charities is clearly inconsistent with the liberal values of a limited state whose functions should be matters of social consensus. But what, then, is the alternative? The truly liberal – i.e. libertarian – alternative would be to simply eliminate all government funding of the third sector and any tax deductibility for charitable donations, on the grounds that all such decisions are personal. But such a solution, however ideologically consistent, is simply too austere and too extreme for Canada today. While believing in the general principles of a liberal state, Canadian citizens also want the state to play some role in supporting the third sector. The state simply relies on charities to do too much, and too many charities rely on the state for too much of their funding, for this relationship to be suddenly terminated. For example, 57 percent of all registered charities' budgets come from government.ⁱⁱⁱ The social disruption of completely severing these ties would simply be too great. Also, Canadians want to foster the social and political capital that the third sector provides. Therefore, third sector support has overarching social and cultural value. This paper accepts the premise that getting government out of third sector support altogether is neither socially responsible nor politically feasible. Accordingly, the goal must be to address some of the problems

¹ This is not to say that consensus on such matters cannot shift, as it often does over time. In fact, the third sector often serves as a social laboratory that prompts the state to take over projects that prove successful or are deemed necessary.

and inconsistencies associated with government's role in the third sector while acknowledging that it must still maintain some sort of role.²

A preferable substitute for direct funding is, indeed, the use of the income tax system. It has become accepted in modern Western liberal societies that taxation, and especially income taxation, is also an appropriate tool of social policy. As Boone explains: "The general consensus...appears to be that a tax system should do more than raise revenue and has significant social and economic policy implications...Public policy goals can be achieved through the use of tax incentives, which are designed to affect the behaviour of taxpayers."^{iv} Boone adds that, in addition to raising revenue, secondary purposes of the tax system include redistributing resources, influencing economic decisions and delivering benefits.^v Tax deductions for charitable donations certainly appear to meet these criteria, as they influence citizens' economic choices by making it less costly to give to charity, thereby redistributing resources to the third sector, to the benefit not only of recipients of charity but of society's social capital as well. Finally, Boone notes that the income tax system is also an excellent tool because it is so far reaching, as the vast majority of Canadians file income tax returns.^{vi} It is also, however, incredibly individualistic, leaving far greater leeway for individual choice and autonomy. Therefore, the best way to co-ordinate government involvement in the third sector in a liberal-democratic state appears to be through the income tax system.

This paper now turns its attention to the question of how such a policy could be made to work. Subsequently, this paper will also address some legitimate concerns raised about its proposals, such as the fear that they would disadvantage low-profile charities

² This paper will only focus on federal government involvement in the charitable sector, as opposed to the third sector as a whole. However, the principles remain the same.

and marginalize some legitimate projects. Answering the question of how essentially lies in devising a way to distribute some \$4 billion in charitable tax deductions through Canadian citizens. This figure is derived from the following considerations. The Canadian government gives some \$3.3 billion³ annually to interest groups.^{vii} Furthermore, the Canadian government foregoes some \$850 million in tax revenue because of charitable deductions.^{viii} The sum of those two figures is \$4.15 billion. Accordingly, this will be taken as a rough estimate of the federal government's annual financial commitment to the charitable sector.

This paper proposes that Canadian income tax laws be changed to allow taxpayers to deduct some of their charitable donations *directly* from their federal income tax, rather than from their taxable income. Essentially, taxpayers would have the choice of paying money to the government or giving it directly to charitable organizations. It is presumed that most taxpayers would prefer to give as much as possible to charities of their choice rather than to Revenue Canada. The amount of these direct deductions would obviously have to be capped, as the government cannot afford to let charities claim most of its revenues. This cap would be based on the amount of money the federal government currently spends on charities and the revenue it currently foregoes from charitable deductions – the \$4.15 billion mentioned above. As there are approximately 20 million taxpayers in Canada, this would work out to an average of just over \$200 per taxpayer. This, then, is the crux of this paper's proposal: allow Canadian taxpayers to deduct up to two hundred dollars from their federal income tax and, instead, give it directly to charity.

³ It is acknowledged that this figure represents the federal government's funding of *all* third sector organizations, not strictly charities. As this figure is a broad estimate, a more detailed breakdown was not available. However, it is assumed that most of this spending would go to registered charities or to organizations that could broadly be considered charitable, as the point of the article cited was that the federal government needs these organizations to provide public services.

It should be noted that \$200 is an approximate average and not necessarily an exact, universal amount. For instance, as the income tax system is progressive, it may prove wise to make this amount similarly so. That is, the amount of direct deduction could vary with the amount of overall tax paid. It would also be important to index this figure to inflation, as all other tax brackets and deductions currently are. This amount might also have to be adjusted, up or down, to keep these reforms revenue neutral. Although it should be fairly easy to predict the costs, some adjustments may prove necessary. However, none of these matters is at the heart of this proposal. Rather, they are simply administrative measures which may have to be used to fine-tune it. It is beyond the scope of this proposal to consider such minute details. It will simply be assumed that the federal finance department would be capable of devising an administrative plan that meets these overall objectives.

This paper will now address some concerns about its proposals. The potential weaknesses of this plan, most of which were raised during its presentation in class, are as follows: 1) It would favour high-profile charities with glitzy marketing campaigns over important, smaller charities. 2) Consequently, it would narrow the range of third sector options and perspectives by marginalizing low-profile organizations. 3) It would provide no “back up” policy for worthwhile causes that failed to elicit sufficient donations. 4) It assumes too much, i.e. that citizens would take the time to properly educate themselves about the charities to which they donate. 5) It leaves those who do not pay federal income tax no opportunity to influence the socio-political shape of the charitable sector. This paper will now address these concerns.

The biggest concern raised about this proposal is that it would favour high-profile and savvy charities that promote popular causes over lower-profile ones that may not have an easily saleable message but nonetheless do valuable work. This proposal recognizes this as a legitimate concern and has made several modifications to address it. However, to put such concerns into the proper context, it is necessary to consider some mitigating facts and figures. First of all, it should be stressed that this proposal applies only to the federal government. Provincial and local governments would still have the option of directly funding charities. It is provincial governments that are directly responsible for health and welfare, meaning that much of the third sector funding in these areas comes from this level and would not be affected by changes in federal policy. Provincial governments also control gaming revenues, through such institutions as the Ontario Trillium Fund. This represents an opportunity for arms-length organizations to evaluate the needs of lower-profile charities and provide funding. Finally, provincial and municipal governments are simply closer to the people. They are more responsive to local concerns and are in a better position to evaluate when to “bend the rules” of liberal-democratic theory and engage in direct funding. Therefore, a proposal that aims to curtail direct charitable funding by only the federal government would not alter the relationship between government and charities in Canada as much as one might think.

A closer examination of the numbers is also revealing. There are approximately 76,000 registered charities in Canada which generate about \$90 billion in annual revenues.^{ix} Government provides 56 percent of these revenues, individual and corporate donations provide 11 percent, other charities and foundations provide three percent and so-called “other” sources, such as fees, provide the remaining 30 percent.^x However,

these figures are for the entire charitable sector and are actually heavily skewed towards a few large charities in the health and education sector. Webb notes that 60 percent of all charitable revenues are generated by teaching institutions and hospitals with charitable status.^{xi} While it is impossible to isolate such revenues entirely, most hospitals and universities receive most of their budgets from provincial governments. Therefore, it is fair to conclude that much of the current government funding of the charitable sector is actually spending on the public delivery of education and health, as opposed to the subsidizing of truly independent and charitable undertakings. Furthermore, Webb notes that only one third of charities receive government funding, and that 60 percent of these, that is 13,000, have annual revenues of less than \$250,000. Collectively, these 13,000 charities account for less than five percent of all government funding to the third sector.^{xii} This is consistent with the hypothesis that most government funding of registered charities actually goes to a handful of large institutions that function more like government agencies. Therefore, it would appear that small, lower-profile charities actually receive little direct funding from the federal government anyway.

Under this proposal, direct deductions from payable income tax would only be granted if taxpayers submitted a legal receipt from a registered charity. They would not simply be allowed to check a box on their tax form. The logistics of checking a box are prohibitive anyway, as there is simply no way that the names of thousands of registered charities could all fit onto a single tax form. However, there is an even better reason for rejecting the “check a box” option: it makes it too easy for citizens to make an uninformed donation. Citizens would not be allowed to simply check a box and deprive the federal government of tax revenue. Only those who had taken the time to make a

charitable donation and submit the receipt(s) would be allowed direct tax deductions. This addresses the concern that not all citizens would be informed enough to effectively exercise such an option. This system would be optional, not mandatory – and optional *only* for those who had taken the time to make legitimate charitable donations. While this system is designed to allow for greater individual choice among taxpayers, it is not designed to force them to make choices on matters on which they are not informed. Those who did not submit any charitable donation receipts would simply pay their full income taxes to the federal government. Such a system would go a long way towards ensuring that direct deductions encouraged only active and informed choices.

In light of the proviso explained above, it is fair to assume that not all citizens would take advantage of the direct deduction option. Therefore, the federal government would still collect some revenues that it had budgeted for charitable deductions. This paper proposes that these funds be earmarked for the charitable sector and not simply put into general revenues. Instead, the federal government would grant this money to charities. This would be done for two reasons: 1) to ensure that the charitable sector does not lose any public funds as a result of this proposal; 2) to give lower-profile charities a second chance to appeal for public funds. This might seem inconsistent with this paper's overall proposal because it does still involve some direct funding of the charitable sector by the federal government. However, it should be noted that the federal government would be giving only that money to charities which citizens themselves did not bother to donate. Individual citizens would still be given the first chance to direct this money as they wished. Only when they declined to exercise this option would the state step in. Therefore, this is still broadly consistent with this paper's liberal ethos of individual

choice and less government involvement in charitable donation decisions. Secondly, such a back-up plan, under which the federal government would still allocate unclaimed tax deductions directly to charity, also presents an ideal opportunity to give important but lower-profile charities a second chance. This paper acknowledges that its plan places much faith in the good sense of informed citizens to choose deserving charities.

However, there will always be some risk that savvier marketing will win out over important but less glamorous charitable missions. To address this issue, the federal government would target its unclaimed tax deduction allocations at charities it deemed to be deserving but lower profile. The fact that not all taxpayers would avail themselves of this proposal actually serves as an important social insurance policy. It allows the federal government to maintain the charitable sector's funding while addressing inequalities within it.

While this paper will not propose specific rules as to how the government should allocate unclaimed charitable donations, it will present some recommendations. Specifically, it suggests that charities which serve the following client bases be considered prime candidates for residual federal funds: the mentally and physically disabled, recent immigrants, and low-income and socially disadvantaged people. The mentally and physically disabled obviously have legitimate special needs but do not, by definition, have the numbers or the resources to compete for political attention. Many immigrants, especially from poorer countries, often don't speak the language, are not eligible to vote, and have not yet established themselves economically or socially. Again, these are people with legitimate needs but who are not as able to communicate them to the mainstream. Finally, low-income and socially disadvantaged people are usually

simply too poor and/or too isolated to put their concerns on the public agenda.

Accordingly, charities that serve any of these groups would be prime candidates for “back-up” funding under this plan. In this way, the liberal democratic values of freedom of choice and accountability are advanced while also preserving another fundamental liberal-democratic value: that of respect and protection for political minorities.

The final concern is that this proposal does not allow those do not pay federal income taxes to make subsidized donations to charities. It is acknowledged that this is true, but also respectfully submitted that this is the least important of the concerns raised. The most obvious rebuttal, of course, is that neither does the status quo. The current system of charitable donations being deductible from taxable income is an option similarly limited to those whose incomes are high enough to be taxable. It is conceded that, by taking more funding decisions away from governments, which are elected by all citizens, and leaving them with income-tax payers, there is some loss of influence by the lowest-income voters. This paper contends that such a loss of influence is marginal and, in fact, impossible to quantify. It asserts that the advantages of such a system would still outweigh this minor setback. However, this paper also remains open to any proposals which might allow those who do not pay income tax to still register their preferences for charitable funding. Perhaps the government could issue anyone whose income was not high enough to be taxable an official “charity preference ballot” on which they could indicate their recommendations for deserving charities. These ballots could then be used to help the government allocate unclaimed tax deductions, as explained above. Whether such a proposal would be practical, or even popular, is hard to say and is beyond the scope of this paper. However, it is an issue which this paper is open to addressing.

In addition to the ideological reasons for adopting this plan, there would be several other advantages to it. First of all, it would help restore core funding to charities. Instead of competing for government grants to undertake certain projects, charities could appeal directly to citizens for core funding. Such a system would also likely raise the profile of charities and encourage them to become more accountable and transparent. Taxpayers would suddenly have an incentive to learn more about charities, as many more would likely choose to donate to them. This increased attention would represent an opportunity for charities to solicit even more support. It could also encourage citizens to give more to charities, as at least part of their donations would be deducted from their taxes. The psychological affect of such a direct relationship should not be discounted. However, charities would also have to ensure that their missions remained relevant and understandable to the general public, as it would be citizens, and not the government, who would decide their funding levels.

In conclusion, this paper's proposals rest on three main objectives. 1) Taking decisions about charitable funding away from the federal government and placing them with individual citizens. 2) Maintaining the current level of federal public funding allocated to charities. 3) Ensuring that such reforms do not unduly hurt low-profile charities. If this can be accomplished, it will represent a very positive step for the Canadian state and society. It will mean that the Canadian government will have a relationship with the charitable sector that is more consistent with Canada's liberal democratic values. It will also mean that the valuable roles of the charitable sector – its direct provision of social services, its advocacy and its building of social capital – will be strengthened. A result so positive would indeed make such a proposal worth considering.

Endnotes

ⁱ McPherson, pp. 53

ⁱⁱ Gidron et al, pp. 7

ⁱⁱⁱ Sharpe, pp. 24

^{iv} Boone, pp. 45-46

^v *ibid*

^{vi} *ibid*

^{vii} Pross and Webb, pp. 65

^{viii} *ibid*

^{ix} Webb, pp. 17

^x www.charityvillage.com, Frequently Asked Questions (FAQs)

^{xi} Webb, pp. 18

^{xii} *ibid*

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