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Unfair or Unwanted? Competition Between Charities and For-Profit Businesses in Canada

By Brian Emmett

Charities in Canada face a long-term crisis of financial sustainability. Their missions will become more challenging with continuing demographic and cultural change. There will be a growing gap between the needs Canadians expect charities to meet and the resources available to carry out their missions.[1]

These fundamental social, cultural, and economic trends are leading to more competition between charities and for-profit businesses as charities increasingly look to ways to finance their non-profit activities through business income.

A "market ecology" is rapidly developing in which for-profit businesses and charities co-exist in several markets, each bringing a different character and value. For-profit businesses tend to specialize in data, quantitative analysis, volume, and cost efficiency. Charities tend to specialize in compassion, links to community, inclusivity, and quality to the marketplace. The success of each will inevitably ebb and flow with economic, social, and cultural conditions – and of course with government policies and incentives. This means increased attention from businesses and policymakers concerned about "unfair" competition between for-profit businesses and tax-supported charities.

Tax concessions enjoyed by charities are neither particularly large nor unusual

Charities in Canada benefit from two important tax incentives: 1) exemption from corporate income taxation and 2) the ability to issue receipts which allow donors to claim non-refundable tax credits when filing personal income taxes. In 2014, these tax expenditures amounted to $2.3 billion.[2] In turn, the mission-driven sector provides a social benefit to society greater than the cost of the tax subsidy, with 86,000 charities producing 8.1% of GDP and accounting for two million jobs.

Business, too, benefits from government support. Funding for the small business sector – about $11 billion in 2014[3]– accounted for the bulk of federal spending, supporting an important sector with some 1.16 million firms employing more than eight million people and producing roughly 30% of Canada's GDP.[4]

Tax concessions have a modest affect, if any, on market share and earnings of for-profit businesses

Available evidence shows that charities would not participate in some markets without tax concessions. Tax exemptions can "significantly increase the market share of non-profit firms vis-à-vis their for-profit counterparts."[5]

But the consensus amongst economists is that ". . . tax considerations are probably far less important than is commonly thought."[6]

The social marketplace consists of people with different incomes, education, needs, and other demographic and cultural characteristics. Elimination of a tax concession may take a charity out of the marketplace – but the private sector may well not serve a set of clients it finds unprofitable or difficult. These market segments are likely to go unserved.[7]

Charities enjoy tax benefits, but for-profit businesses enjoy compensating structural advantages

Charities receive tax concessions, but this comes with a severe limit on financing options.

"Business[es have] access to capital . . . a charity cannot sell shares . . . few have the steady income streams or valuable assets against which to borrow. . .

"For-profit businesses have a degree of nimbleness and flexibility to respond to changes in the social marketplace and pursue innovative, often expensive solutions to emerging opportunities that allows them to grow faster in many growing markets… there is an 'uneven playing field' that advantages for-profits . . . If for-profits want to establish new facilities and operations in response to new opportunities, surges in demand, or technological change they can use . . . access to capital simply by selling stock. Not-for-profits and charities are confined to expensive bank financing at best."[8]

But this advantage may come with the social cost of underserving marginal or difficult segments of the population.

An increasing number of markets are opening to for-profits

Winning and losing in social markets depends on tax treatment, access to capital, the changing nature of government, the nature and quality of services offered, increased emphasis on efficiency and performance management, among other factors. Data shows market share of non-profits in the US shrinking across several social and health services sectors.

“[P]ublicly-traded firms have actively staked out a significant portion of the expanding charter school market. In welfare-to-work services, several large defense contractors have begun to compete for and win contracts.”[9]

For example, with respect to social service provision, while non-profits continue to dominate these markets, for the 20-year period from 1977 to 1997, employment in for-profit business grew 273% while employment in non-profits expanded by 134%.[10] Other data show this trend continuing across an array of social and health care markets to at least the year 2013.[11]

Unfair or Unwanted?

But there is a fundamental difference.

“. . . between ‘unwanted’ competition and ‘unfair’ competition. Any time a charity competes in the marketplace with a for-profit provider, such competition might be unwanted . . . The issue, however, is not competition per se; rather, ‘unfair’ competition presupposes that the exempt organization is somehow unfairly using the economic benefits of exemption to subsidize their commercial activities.”[12]

Competition is a fact. Tax support for charities is broadly comparable to subsidies provided to for-profit business activities; tax policy has little, if any effect on the market shares and earnings of for-profit businesses; and the relative positions of charities and for-profit business in social markets is determined by the nature of the market, the people in it, and the character of the services brought to it. The levelness, or lack of it, of the playing field is not a major or even important factor.

“Legal academics and economists who have examined the issue have reached an almost remarkable consensus that unfair competition in the form of predatory pricing or predatory market expansion is not a serious policy concern.”[13]

The key question is not unfair competition. It is the worry about what society loses when charities are in decline relative to for-profit firms reducing “. . . their unique commitments and value-laden missions, [and] . . . innovative approaches to public problems that are linked to community needs and standards.”[14]

The constructive policy question is what mix of action on tax incentives, earned income, social investment, program design, and data is needed to preserve a highly beneficial mixed “ecology” in the era of a social deficit.

Read Brian Emmett’s full article.

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[13] Columbo, op. cit.

[14] Frumkin, op. cit.