Charity, Philanthropy and Stewardship: A Philosophical Perspective on Tax Reform*

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Introduction

The White Paper on Tax Reform was released in the House of Commons on June 18, 1987. Since the Government has not yet released the specific amendments in draft legislation, this article will attempt a philosophical analysis of the White Paper and of how the charitable sector interacts with the tax system and donors. Having taken that liberty, let me make it clear that these views are personal and not intended to represent the position of the Canadian Council of Christian Charities.

My view is that the marketing philosophy behind the tax credit, most fundraising endeavours, and religious giving programs, is the belief that the primary competition for the charity seeking the potential donor's dollar is that person's need or desire to spend that dollar on personal consumption. Without denying the validity of that hypothesis, I believe that it inhibits a tax policy and marketing emphasis which would encourage larger gifts during donors' lifetimes as well as testamentary bequests. Annual giving campaigns solicit gifts out of the donor's income, whereas large endowments, "bricks-and-mortar" gifts, and testamentary bequests of estate residues, are gifts out of a donor's capital. Canadian charities need a tax policy, marketing strategy and understanding of donor motivation which will facilitate and encourage gifts out of capital.

White Paper Proposals

Whether or not one agrees with the proposals regarding charitable giving put forward in the White Paper, the Minister of Finance is to be commended for attempting to respond positively and constructively to representations made to him by segments of the charitable sector. It is very clear that powerful voices in the charitable sector lobbied hard for the shift from deductions to tax credits for charitable contributions. While I am philosophically opposed to that shift, I do believe that the changes result from the Minister of Finance responding in good faith to these representations rather than from the government unilaterally setting out to change the basis upon which charities interact with the tax system in Canada. Some segments of the charitable sector are obviously far more active and effective lobbyists than others.

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Once the Minister accepted the shift to tax credits, the conversations I have had with "anonymous officials" in the Department of Finance make it clear that the Minister himself lobbied hard and effectively with his Cabinet colleagues to achieve the new financial tax incentive given to low- and middle-income donors donating more than $250. The $250 threshold was selected by the Minister over the protests of some of his staff who felt that it was too low. In a letter dated July 31, 1987 to the Chairman of the Coalition of National Voluntary Organizations, the Minister of Finance stated:

> . . . I believe the $250 threshold is reasonable and generous. For example, it is less than half the value of the average donation of $520 and over 40 per cent of donors already give at least this much. As you were informed in the June 30 meeting with my officials, consideration was given to setting the threshold at $400. The federal revenue cost of the $400 threshold would have been $20 million more than a deduction post-reform. However, my sense was that $400 was too high and I anticipated a similar response from the NVO. Moreover, I was willing to demonstrate in no uncertain terms the government's commitment to a financially strong charitable sector. Accordingly, the threshold was moved down to $250 . . .

The letter goes on to state that the Minister's financial estimates indicate that the cost of the new tax credit with a $250 threshold will be $50 million in 1988. This $50 million is in addition to the $530 million in foregone revenues already estimated for 1988 under the existing deduction system.[1] The question which needs to be asked is: what level of new and additional giving will result from this increased expense to the public Treasury? The charitable sector also needs to be assured that the government does not plan to recover $50 million in new sales taxes in stage two of tax reform so that it can achieve its stated objective of tax reform being "revenue neutral".

Marginal Rate Changes

Tax reform proposes that there be only three marginal rates of federal tax for individuals: 17 per cent up to $27,500 in taxable income, 26 per cent from $27,501 up to $55,000 and 29 per cent for $55,001 and over. The Department of Finance estimates that 66 per cent of the taxpayers who file returns will be in the 17-per-cent bracket, 29 per cent will be in the 26-per-cent bracket and only five per cent will be in the 29-per-cent bracket.[2] Assuming a 55 per cent provincial tax (as does the White Paper) the combined federal and provincial tax rate at the lowest marginal rate will be 26.35 per cent and at the top marginal rate will be 44.95 per cent.

It is safe to say that a major factor in the timing and political imperative of the tax reform was the *Tax Reform Act of 1986* in the United States. Tax reform in the United States will reduce their top marginal rate of taxation from 50 per cent to 38 per cent beginning January 1, 1988. Fearing a huge movement of capital and entrepreneurs to the United States if the differential between our tax rates becomes too high, Canada attempted to accomplish tax reform by

January 1, 1988 even though the draft legislation has not yet been produced. (mid-January, 1988).

In the charitable sector in the United States there has been a tremendous debate about the impact of lowering marginal rates on charitable giving. One segment of the charitable sector believes that if the after-tax cost of a donation goes from $.50 to $.72 per dollar, people will give less. The other segment believes just as strongly that because donors now have an extra $.28 of *every* dollar in their own jeans after-tax, they will have even more disposable income to donate to charity so donations should increase. The debate turns on whether this extra disposable income will be consumed by the taxpayer or donated to charity.

There is no doubt that knowledge of the impending changes affecting the tax cost of giving influenced many Americans to give more money that they ever had before in one year in 1986, prior to tax reform. Even in Canada we experienced this phenomenon as Canadian charities with United States subsidiaries and active capital campaigns found many American donors prepaying, prior to the end of 1986, full amounts which had originally been pledged over three years. Given the distortions introduced by this prepayment, it is premature to make any assessment of the impact of marginal rate changes on charitable giving in the United States until the early 1990s as any fall-off in donations in 1989 and 1990 may simply reflect people adjusting their giving to average out the excess amounts given in 1986 and 1987.

While the debate on the impact of lowering marginal rates in the United States is of philosophical interest, it is primarily an academic debate as far as Canadians are concerned. When provincial tax is added to the federal tax rate, the effective drop in a taxpayer's marginal rate is not likely to exceed five per cent. This is far short of the 22 per cent experienced in the United States where state taxes are deducted from federal taxes rather than added to them. This five per cent will probably be more than made up by the increased cost of consumption taxes which will come forward in stage two of tax reform.

Canadian charities which get caught up in the debate about the potential negative impact on charitable giving resulting from lower marginal rates are participating in a debate on an American issue which will have little financial impact in Canada. In fact, participating in, and giving a high profile to, the American controversy has some potential for a negative effect on Canadian donors who may assume that a similar real reduction in marginal rates has been achieved in Canada.

Philosophical Basis of Reductions

The debate in Canada with regard to tax reform should not become a financial analysis of the impact of lowering marginal rates. It should be a philosophical analysis of the implications of shifting from tax deductions to tax credits for charitable contributions and the philosophical core of the debate is the question: whose money is being given away? The proponents of charitable deductions have a very strongly held belief that taxpayers are giving away their own money. It follows that they also hold that the tax deduction simply removes the tax penalty which would otherwise result if taxpayers had to pay taxes on income which they had voluntarily chosen not to receive personally but to redirect to registered charities or other qualified donees.

This philosophical belief is fundamental to the motivation of many charitable donors, especially those giving large amounts cognitively as philanthropists. Philanthropists must believe that this philosophical premise is going to be respected by the government if they are to believe that there is any guarantee or reasonable expectation that charities will maintain their independence from government in the future and continue to play their present critical role, i.e., providing services which are best not provided by either the government or the commercial private sector.

In the religious sector, this philosophical premise is necessary if churches are to expect to continue to have freedom from government interference in their religious activities. Unlike the United States, where the constitutional guarantee of separation of church and state has been interpreted to mean that churches which are charities need not even file annual public information returns, churches in Canada have no special legal status beyond being registered charities and must file public information returns and accept government scrutiny like any other charities. However, the manner in which a taxpayer's gift to charity is characterized and the consequent characterization of the nature of the support or benefit which charities receive from the state may have a bearing on whether or not the *Canadian Charter of Rights and Freedoms* can be invoked to regulate all charities, religious or otherwise.

The conversion of the tax deduction to a tax credit or a tax preference may or may not have any significant financial impact on charities, depending on the extent to which tax credits are matched to the marginal rate of the donor. However, it accomplishes a fundamental philosophical shift by implicitly stating that a portion of all taxpayers' incomes actually and primarily belongs to the government. The totality of Canadians' incomes is no longer private property with a legal requirement to pay legislated financial obligations to the government; the property is now the government's and the citizen's possession and use of it is dependent upon the extent to which the government refrains from taxing it away. Treating a charitable donation as a tax preference is consistent only with this latter view of property.

Public Perception

A debate about the philosophical basis of a tax deduction versus a tax credit seems to be highly academic and esoteric and therefore irrelevant. However, in a society where tax privileges and policy depend on how issues are perceived by the people who elect politicians, this issue is of fundamental importance. On June 24, 1987, *The Globe and Mail* published a long editorial supporting the proposed tax-reform changes as those which would encourage charitable giving.

Describing tax credits, the editorial said:

> In technical terms, the government is making a tax expenditure, or foregoing revenue, each time it gives taxpayers a credit. In practical terms, society believes so strongly in encouraging the support of charities that it gives taxpaying donors a form of matching grant. This practice is undeniably expensive for the Treasury. It forces Mr. Wilson to look elsewhere to make up the budgetary shortfall.

The problem presented by this type of editorial is that it provides equal ammunition to those who oppose tax incentives for charitable giving and those who support them. Taxpayers who believe that the the government is allocating too much money to charity will say that government should not provide a "matching grant" to donors to churches or other charities which other taxpayers do not support. Since these donations are now characterized as "tax expenditures", it is a legitimate policy argument which must be addressed. If the donation were simply characterized as a gift of a citizen's property to charity which the government abstained from taxing, the problem would not arise.

Fairness

A great deal of the emphasis in the marketing of tax reform has been placed on bringing "fairness" to the tax system. Consistent with the shift to tax credits and tax preferences, "fairness" is now measured by the cost to the public Treasury of the donations. Under the tax-deduction system, the measurement of "fairness" is whether taxpayers of all marginal rates have an equal opportunity to donate their money to charity without attracting tax. This standard of fairness will no longer be achieved for high-income donors giving below the $250 threshold. Nor will it apply to low-income donors giving above the $250 threshold as they will have a financial incentive not provided to high-income donors.

Arguing that tax credits achieve greater "fairness" for low-income donors, tax reform proposes that all donors, irrespective of their particular marginal rates, receive a 17-per-cent federal tax credit on the first $250 of their donations. This provides no additional tax incentive for small donors over the old tax deduction system but they can be assured that the first $250 donation from even the wealthiest donor in the land is costing the public Treasury an equal amount. In an income tax system based on progressive taxation and individual marginal rates "equal treatment" is not normally expected to be synonymous with, or produce, "fair treatment".

Proponents of the tax deduction, operating from the premise that the money to be donated belongs to the donor, believe that "fairness" lies in the fact that donors in any of the marginal rate categories have an equal right to give their money to a charity of their choice without the state demanding a portion. To argue that donors with a high marginal rate have an unfair tax advantage when they make charitable donations under the deduction system is to argue that it is unfair that taxpayers with low marginal rates get back a higher percentage of each dollar of income after taxes for personal consumption. Yet the government would consider it absurd if a low-income self-employed taxpayer were to ask it to return, by way of tax credit, the difference in after-tax costs of an equal amount of legitimate business expenses deducted by a high-income self-employed taxpayer so there would be an equal cost to the public Treasury.

If the charitable credit does indeed achieve greater "fairness", the government should be challenged to explain why it has not extended the tax credit system to corporate donations. Retaining the charitable deduction system for corporations has the potential to create distrust in the minds of individual taxpayers who are being educated to believe that deductions are unfair.

The $250 Threshold

The result of the proposed tax credit system is that donors paying the top marginal rate can argue that they have been treated unfairly with regard to the first $250 of their donations. They pay federal tax at the 29-per-cent tax rate while receiving only a 17-per-cent credit and therefore do pay tax on income which they are giving to charity. The loss of tax incentive to the high-income donor is the spread between 17 per cent and 29 per cent up to the $250 threshold. This amounts to a maximum of $30 federal tax, or $46.50 with 55 per cent provincial tax, so is very small in dollar terms. This loss of tax saving does not increase above $250. It does not change if the donor has an income of $100,000 or $1,000,000 or if the donation is $256 or $1,000,000.

Any other comparison between relative tax savings for high-income donors using credits as against deductions is necessarily a study of the financial impact of the tax reform's lowered marginal rates on charitable giving. That is a different issue and the debate over the impact of lowering marginal rates should not be confused with the philosophical debate about the merits of tax credits versus tax deductions. As indicated earlier, that debate has little relevance in Canada because of the very small reduction in the proposed marginal rates.

It is my view that a tax credit which is calculated by matching the rate of the credit with the marginal rate of the donation is a deduction masquerading as a credit. Therefore a low-income donor continues to have a deduction rather than a credit up to the $250 threshold and the high-income donor continues to have a deduction over the $250 threshold. However, while this analysis of the similarity of deductions and credits may be true in financial terms, it does not apply to the philosophical difference between the two.

The proposed tax credit does provide a positive tax incentive to individual donors with 17 per cent and 26 per cent marginal rates who give over $250. Once the donations of the donors with a 17 per cent federal marginal rate exceed $250, they receive a uniform 12 per cent federal tax incentive until their marginal rate jumps to 26 per cent. This percentage incentive does not vary whether they give $256 or $10,000. However, as the credit is non-refundable it has a practical upper limit. It also disappears when the donor's federal marginal rate climbs to 29 per cent.

How Large Donors Are Perceived

The White Paper and publicity about tax reform and its effect on charitable giving have focused on the enhanced financial incentive for low-income taxpayers to give because of the 29 per cent tax credit. While any changes which bring a perception of greater fairness in the tax system are to be applauded, publicity of this kind creates the impression that large donors and corporations claiming deductions were somehow ripping off the tax system. In a system of progressive taxation of income it is not a moral aberration that a donor paying a higher marginal rate receives more tax relief from a donation than a low-income person. Charities require the political influence of their supporters if they are to maintain their favoured standing in the tax system and the community at large. The charitable sector's interests are not well served by pitting different segments of donors against each other.

An analysis of the tremendous negative effect that the *Tax Reform Act of 1969* had on the formation and operation of private foundations in the United States shows the harm which can result when the populist low-income donor segment of the population refuses to protest when government attacks the politically vulnerable private foundation segment. In Canada we experienced the trauma of a similarly pejorative perception of private foundations and large donors when MacEachern introduced his budget of November 1981. Those reading the White Paper with a residue of paranoia from MacEachern days need to be reassured that tax incentives for high-income 20-per-cent-limit donors are not being sacrificed either in the quest for "fairness" or to reduce revenue loss.

The government needs to perceive that the broadly based charitable organizations, supported primarily by small donors, recognize the importance to the charitable sector of private foundations, large donors and corporations. Governments are always ready to apply the sledgehammer to any alleged abuses of politically vulnerable groups like the funders of private foundations and endowments. The rhetoric of some segments of the charitable sector suggests that they would prefer to take government money from the public Treasury rather than donations from private philanthropists.

Philosophy of Tax Reform

While one may not be happy about the shift from tax credits to tax deductions, one can take some comfort from the fact that the government is intending to create provisions which will enhance charitable giving and is responding positively to representations made by a segment of the charitable sector. This is in noted contrast to the government policies towards charitable funding which seem to be evolving in the United States. Tax reform in both countries is supposed to be "revenue neutral", i.e., the revenue losses resulting from reduced marginal rates for those who pay tax should be matched by new revenues gained from closing tax loopholes which have enabled some wealthy taxpayers to avoid paying any tax. However, although tax reform as a whole is supposed to be revenue neutral, the provisions affecting charities are a definite exception. This is evidenced by the Minister of Finance's acknowledgment that there will be a $50 million additional cost to the Treasury for the $250-threshold tax credit proposal.

While there has been much debate about the fiscal implications of the reduction in marginal rates in the United States, there has not been significant attention paid to the extent to which United States tax reform represents a radical shift in the philosophical underpinnings of their tax system. United States tax reform reflects the philosophy that tax law should be neutral in terms of social policy. Taxation is a necessary evil to pay for government but government should confine its activities to only the most essential services and defence.

If the Reagan revolution had succeeded, the United States federal government would have almost no role to play in solving society's problems. Reagan believes that if only the government would get off the backs of the private sector, that sector would produce sufficient jobs to take people off welfare and create the wealth necessary for society to function. It is not clear how the wealth was to be redistributed but the general charitable impulses of the American public were apparently presumed to be adequate to justify phasing out and abandoning the safety net for the less fortunate provided through the tax system and federal assistance programs.

Tax reform in both the United States and Canada gained much of its momentum from those who support the philosophical position that economic resources are more productively and efficiently allocated by individuals and corporations than by governments. It follows that economic transfers and income redistribution accomplished through the tax system should be radically curtailed. This change was accomplished much more significantly in the United States than in Canada because the American political culture allowed a much more genuine and radical tax reform to go ahead once the politicians were able to convince the public and Congress that tax reform would be revenue neutral.

While many people in Canada share the belief that the government should minimize its involvement in the economy, it must be recognized that tax reform of the American kind runs directly counter to the philosophical basis of either the charitable deduction or credit. The charitable deduction is not neutral in terms of social policy as it is a mechanism which is designed to encourage the allocation of private funds to public purposes. Given the differences in the political environment and culture in Canada and the United States, the government did not have the political will to achieve genuine tax reform. Special interest groups in all sectors of the Canadian economy have been far more successful than their American counterparts in arguing that genuine tax reform and the consequent reduction in the artificial allocation of economic resources through specific tax policies should apply only to other groups, not to themselves.

Tax-Driven Donations

Tax reform in Canada has very definitely not extended its philosophical shift towards the position that the tax system should be neutral in social policy to the provisions effecting charitable giving. At the same time that the federal government is trying to create an environment in which business decisions become less tax-driven, the marketing of the tax credit encourages donors to charities to become more tax-driven. While one may have reservations as to whether this policy is in the long-term best interests of the charitable sector, the government should be applauded for its recognition of the importance of the charitable sector and its attempt to encourage Canadians to contribute to it.

The White Paper and proponents of the tax-credit incentive argue that the way to increase donations from low-income donors is for the government to offer increased tax incentives for giving. This argument implies that the charitable sector will be strengthened when low-income donors are educated to become as tax-driven as, it is assumed, high-income donors are. How it can possibly be in the charitable sector's long-term interest to reduce altruism in giving and become more dependent on the public Treasury is beyond my understanding. To foster a primarily tax-driven motivation among low-income donors is to advocate the corruption of the essential dignity and altruism of a simple gift of charity and to allege that large donors are primarily tax-driven is to insult and deter genuine philanthropy.

Only a very unsophisticated analysis of the charitable marketplace would assume that all those who do not file charitable donations receipts with their income tax returns make no charitable donations. Or, if donors are as tax-driven as the proponents of the tax credit assume, that all married donors file both the husband's and wife's donations on the return of the spouse with the higher marginal rate to take advantage of the deduction on the higher marginal rate and in future will file all donations on one return to get the increased tax credit above the $250 threshold.

(Incidentally, charities holding this view of philanthropy and marketing tax credits as a big improvement, should not begin marketing until the new year since tax-driven low-income donors will want to hold back on their traditional year-end giving in 1987 and delay it to 1988 with the hope that a combined donation will surpass the $250 threshold and receive the increased tax credit.)

In fact, many small donors simply do not take the trouble to retain and file their tax receipts so do not claim the deduction with resulting savings for the Treasury. Large donors, on the other hand, usually have more sophisticated systems for preparing their tax returns which require the retaining and filing of car and other expense vouchers so are more likely to retain and file charitable receipts. The primary factor in the retention of receipts is the size of the donation, not the marginal rate of the donor. If donors are encouraged to become tax-driven rather than driven by altruism when making a $15 gift and they know they will not retain and file the receipt, they may refrain from making the gift at all since a tax-driven donor knows that no matter how generous the tax credit, it is worth nothing if the receipt is not filed. If donors retain and file more receipts the cost to the public Treasury is increased without necessarily triggering a corresponding increase in money actually donated to charity.

Non-Receiptable Donations

Millions of Canadians make small gifts to community groups which are not registered charities. The government must not create such a tax-motivated environment that small donors stop giving to these worthy causes simply because the law does not recognize them as "charitable". How is my child's soccer team to raise money for its uniforms, tournament fees and exchange programs if, in addition to the handicap of being unable to issue charitable deduction receipts, it finds that prospective donors want the positive tax incentives provided by enhanced tax credits? The government should be more cautious about the possible peripheral negative effects when it is marketing tax credits as a huge step forward.

Donor Motivation

Having complained about the White Paper's proposed direction, it is incumbent on me to propose a better option. In doing so, I will attempt to provide the philosophical and empirical analysis necessary to support my contentions. This will involve an attempt to define the charitable sector and donor motivations in ways which differ from those which underlie the White Paper. The Department of Finance's analysis of donor motivation assumes that donors are tax-driven. In a letter to the editor of *The Globe and Mail* in response to the June 24, 1987 editorial quoted above, the Minister of Finance wrote:

> The effect of the proposal will be to provide an incentive for people to increase donations above the $250 threshold, especially for those in the two lower tax brackets. This group includes 95 per cent of all taxpayers who make about 75 per cent of total deductions.[3]

My analysis leads me to believe that the government should not be primarily concerned with promoting tax-driven charitable donations by low- and middle-income taxpayers but testamentary and lifetime gifts of capital from taxpayers of all income ranges. Unless the government is prepared to encourage and authorize the unbridled plundering of the public Treasury for charitable-contribution tax credits that it allows for political-contribution tax credits, it is not going to increase charitable giving by tax-credit incentives. No cost-benefit analysis would justify the increased cost to the public Treasury of the White Paper's proposals.

My analysis will exclude those components of a charity's activities which are primarily funded by the people who benefit from them because their funding does not rely on charitable motivation. For example, if I donate to the independent school my child attends or to an academy of music or a youth orchestra because my child is enrolled in their programs, it is safe to assume that self-interest is a greater motivator than charitable altruism.

This is not to argue that music and education are not legitimate charitable activities but to recognize that the law allows me tax incentives to fund indirectly my child's music education in the youth orchestra in a way it does not allow me tax incentives to fund indirectly another child's sports education in a soccer team. I fund my child's soccer team without tax incentives because I believe the experience is teaching lessons about teamwork and the importance of working hard in practice which are as least as valuable as the identical lessons being learned through the orchestra experience. (However, it is not the purpose of this paper to explore why the orchestra is "beneficial to the community as a whole" while the soccer team allegedly is not.)

Categories of Charities

This analysis will divide the charitable sector into three broad categories: operating charities, grant-making foundations and religious organizations.

Operating charities have a readily identifiable role in delivering services which relieve poverty, advance education, the arts and health and are beneficial to the community as a whole.

Religious organizations deliver many of the same charitable services. It is important to separate religious activities from the charitable activities carried out by religious organizations. Religious activities are justifiably "charitable" on the basis that they are beneficial to the community as a whole because they contribute to bettering the conduct and character of citizens. They are not justifiably charitable simply because they are "religious" and engaged in the propagation of a particular faith. Indeed, the law rejects monastic contemplative prayer as not being charitable because it is perceived as an entirely private religion without public benefit.[4]

While Canada has strong charitable and religious organizations, it does not have an adequately developed grant-making foundation sector. Foundations can provide the funding to develop innovative and unique solutions to fill the gap between existing government and private-sector services. Their secure financing gives them the independence needed to experiment with new programs, survive those that fail and refine successful ones so they can be adopted by operating charities and governments. Canada needs strong foundations to identify needs and pursue solutions to social problems before they become so widespread and entrenched that government has to respond.

Emotive Giving

Operating and religious charities are funded primarily by gifts out of donors' incomes rather than from gifts out of donors' capital. Large endowments or "bricks-and-mortar" gifts, testamentary bequests of the residue of estates and the funding of foundations come primarily from gifts of capital. (There is a fundamentally different thought process when a donor is giving capital rather than income.) Annual campaign fund raising, the religious tithe and the tax credit are all aimed at gifts from income.

Giving to operating charities from income is primarily an emotive form of giving. The donor is responding to an emotional appeal to reduce someone's suffering or enhance something beautiful in art and culture or contribute to the betterment of society through increased education. An analogy would be parents who will indulge themselves and their children because of the emotion surrounding Christmas, buying gifts in December which they would have known they could not afford in October. They do this in spite of any misgivings they might have that the gifts might spoil the child. They also know they can tighten their belts in January and "rose-coloured glasses" enable them to overcome all the non-financial hesitations they have about making the gifts. Similarly, an annual charitable solicitation campaign may elicit an emotive gift, even though the charity and the appeal may fall short of the donor's ideal standard.

Cognitive Giving

Giving to charity from capital is primarily a cognitive form of giving. The donor wants to accomplish something which will both fundamentally and permanently affect the calibre of services delivered by the charity and provide a suitable monument to the donor's financial accomplishments. It is facile and pejorative simply to attribute such gifts to ego or guilt and say they are primarily tax-driven. However, the appeal and charity must meet the higher standards required of the cognitive donor.

An analogy is the difference between giving to your child in your will and giving at Christmas. Parents preparing their wills apply a different standard of analysis and prudence when they are contemplating a large legacy than they apply to a Christmas gift. For example, will a substantial legacy destroy the child because the child does not have the maturity to handle such a gift? The competing factor in the parent's mind is not the parent's or family's consumption needs but the best utilization of the capital and the best form and terms of the legacy. Deep loyalties and a cognitive sense of duty ultimately determine the size and terms of the gift rather than emotion arising from the state of the relationship with the child on that particular day.

Religious Giving

Giving to religious charities is motivated primarily by religious teaching. Religious charities have chosen to draw primarily on income gifts by focusing their teaching on the tithe prescribed in the Old Testament, i.e., a percentage of income. A fund-raising program focusing on the tithe, like one emphasizing tax credits, is based on the premise that the competition for the donor's charitable dollar is the donor's interest in personal consumption. Certainly the debate in the United States as to the impact of lowered marginal tax rates on charitable giving and the impact of tax costs on giving clearly assumes that giving and personal consumption are competitive.

Charitable Giving Patterns of the Wealthy

In Eugene Steuerle's important study, "Charitable Giving Patterns of the Wealthy", published in *America's Wealthy and The Future of Foundations*, he puts forth the hypothesis that "for the very wealthy, charitable giving may compete less with consumption than with wealthholding itself".[5] He points out that tax incentives for charitable giving are related to income recognition whereas major wealthholders hold their wealth in capital-appreciating assets and try not to recognize more income than they need for personal consumption. Since recognition of capital income at the individual level is largely a discretionary event, tax incentives to give will only apply to that income for which such discretion is exercised.

In his summary Steuerle writes:

> Wealth is an important factor in deathtime giving, but it plays only a limited role in determining the amount of giving during life.[6]

He bases this conclusion on a study of a sample of 4,143 estate tax returns for estates having assets worth over $60,000 filed in 1977 and matched with the income tax returns of the decedents in the years just prior to their deaths. He writes:

> One important inference from Tables 7–3 and 7–4 is that wealth seems to play only a limited role in determining the amount given during one's life, except perhaps to the extent that is increases realized income. Nonetheless, it is an important determinant of charitable bequests, as those with greater amounts of wealth tend to give both greater absolute amounts and larger percentages of their estates to charitable causes.
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> Table 7–5 displays the distribution of charitable amounts given during life by size of charitable bequests. Many persons who are very generous in death can clearly be seen to have given little or nothing in the way of lifetime gifts. For instance, 13 of 21 persons bequeathing $1 million or more to charity actually gave less than $10,000 in annual gifts. In contrast, many who were relatively generous during life made few or no contributions at time of death. Thus, of the 24 individuals who contributed more than $25,000 in annual giving, 11 made no charitable bequests whatsoever.
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> Table 7–6 presents charitable contributions and bequests as percentages of income and net worth, rather than in dollar amounts. The results of both Tables 7–5 and 7–6 are broadly similar. For instance, of 32 persons who made annual contributions of over 40 percent of their income, 19 left no charitable bequest. At least in percentage terms, however, Table 7–6 indicates that givers may be more likely to give a high percentage of their estate than of their income to charity. Thus, 101 (or 3.4 percent of these returns) gave away 40 percent or more of net worth at death, but only 32 (or 1.1 percent) gave away more than 40 percent of their income.
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> Both Tables 7–5 and 7–6 confirm that the pattern of large bequest and small annual contributions is the prevalent behaviour for most taxpayers who make large bequests. Thus, lifetime giving and bequest giving are not great predictors of each other.[7]

The Affluent Canadian

I am aware of no comparable research available in Canada, however Decima Research Limited conducted a national study entitled *The Affluent Canadian* in 1987 which was based on in-depth personal interviews averaging over one hour with Canadians whose annual income or gross wealth placed them in the top seven or eight per cent of wealthy Canadians. I commissioned a series of carefully worded questions designed to determine attitudes to charitable giving. Based on a sample size of 845 in English Canada,[8] 85 per cent of those surveyed had made total donations in the past 24 months which did not even amount to $2,500. While 58 per cent of these people preferred to hold their estates intact for their families and future generations, 19 per cent were disposed to make major charitable donations after their deaths. More significantly, 22 per cent preferred the idea of making significant charitable gifts prior to their deaths (after assuring adequate provision for themselves and their spouses), so they could see the results of their giving.

These data would seem to confirm the Steuerle hypothesis that, for the wealthy, charitable giving competes less with personal consumption that with wealth holding itself and supports his empirical data that large testamentary givers are frequently extremely small annual givers.

In analyzing the giving patterns of the wealthy, the Steuerle study concentrates on the difference between testamentary and lifetime giving. *The Affluent Canadian* study supports my hypothesis that it is more useful to determine whether a donor is giving from capital or income than to determine whether it is a testamentary or lifetime gift. Analyzing the distinction between annual and testamentary giving is a useful starting point but does not acknowledge the potential for obtaining a large gift that exists with the proper approach to a donor, i.e., seeking prepayment of a testamentary bequest rather than soliciting a contribution to an annual giving campaign. My belief is that the donor's thought process is the same for a lifetime gift of an endowment or funding a building program or making a large testamentary bequest.

The ability to convert a planned testamentary bequest into a lifetime gift is dependent on success in offsetting donors' fears about a future "rainy day" and financial reversal with donors' desire to get their affairs in order before their deaths and to see their charitable purposes accomplished while they are still alive. This is a subtle and delicate balancing act which requires an approach far more sophisticated than saying: "You gave to us in your lifetime so do not forget us in your will." At this stage, the competition for a charitable gift is again consumption but only to the extent of the donors' need to protect themselves against the expenses of catastrophic illness or future financial reversal.

It is not the purpose of this paper to develop a marketing strategy for capital giving. However, let me at least put forward my hypothesis that, just as lifetime giving and bequest giving are not great predictors of each other, neither is the fact that a person gave out of income to a particular charity a great predictor that the same charity will be the recipient of the primary capital gift. My experience has repeatedly been that the cognitive thought process leads donors to select different charities for a capital gift then for an annual donation, for reasons not related to the motivation for giving but to donors' analysis of the best long-term utilization of their capital.

Analyzing donors' motivations is easier than analyzing how specific charities are selected once the decision to make a capital gift has been made. Having advocated for some time that charities should be pursuing "out-of-left-field" money for capital gifts rather than confining themselves to their annual campaign mailing lists, I tried to obtain some objective empirical data in *The Affluent Canadian* study[9]. Given the choice of education, health care, medical research, religious activities, arts and culture, and social services as the primary focus for their charitable giving, only two per cent selected arts and culture. This would challenge the assumption that since, during their lifetimes, wealthy Canadians are presumed to give most heavily to arts and culture, they can be expected to follow the same giving patterns in their testamentary bequests and capital gifts.

Tax Policy

It follows that the tax policy which should be advocated to encourage capital gifts is not a tax credit which is designed to compete with personal consumption by increasing disposable income. It will be no surprise that wealthy Canadians frequently share the philosophical view that their assets should be viewed as their own property rather than the state's. Knowing that they cannot consume it or take it with them after death, they find an acceptable form of continued wealth holding by putting their capital into a charitable foundation. If operating charities want to benefit from these capital gifts they need to develop a more sophisticated understanding of the role of both "parallel foundations" and "private foundations".

Philanthropists are not primarily tax-driven. However, when a person is giving cognitively, especially a gift of capital, it is both normal and prudent to do the degree of tax planning appropriate to the size and nature of the gift. People doing estate planning and preparing their wills can get tax advice without the assumption being made that they are tax-driven. The folly of tax reform is that it is trying to introduce a tax-driven motivation into giving. An additional folly is the potential for corrupting religiously motivated giving.

Philanthropy is encouraged by tax provisions which reduce the tax cost or penalty on income which is voluntarily transferred to charity. If tax reform would allow a 100-per-cent deduction up to 100 per cent of net taxable income for charitable donations it would eliminate many economic disincentives to giving. This would bring far more money into the charitable sector at far less cost to the public Treasury than the $50 million tax-credit proposal. It would also benefit Canadians who are not wealthy but *are* faced with the 20-per-cent-of-net-taxable-income limitation on deductions when they want to make a capital or testamentary gift.

It is also important that the government retain rules for charitable foundations which are not hostile to private foundations. In his learned analysis of the impact of the *Tax Reform Act of 1969*, "Congress and Foundations: Historical Summary",[10] John A. Edie details how a hostile United States Congress had a negative effect on the formation and operation of private foundations. While Canada's laws governing the funding of foundations have not been as good as the American tax laws, our rules regulating the operations of private foundations are much better.

Religiously Motivated Giving

Having advocated a tax policy which would encourage capital gifts, it remains for me to address whether religious motivation can foster such gifts. Religious motivation is an important factor when charitable gifts are being made from income but it is generally accepted that religious giving is not significantly motivated by tax considerations. In his book on charitable giving in Canada, *An Essential Grace*, Dr. Samuel Martin wrote:

> Our second probing of the influence of religion on family donations measured the *degree* of commitment to their stated religion. One can belong to a church, but is one committed? The findings are perhaps the most important insight into people's motives for giving.
>
> Those families claiming strong religious ties, 20 per cent of the sample, were the most generous givers in both absolute and relative terms, not only in donations to support their church, *but in donations to non-religious causes as well*. They also joined more humanistic organizations and contributed the largest number of hours of personal service to their community. Generosity declined systematically with the decrease in a family's stated religious commitment.
>
> Families claiming no religious ties (including some who claimed nominal affiliation with a religious sect) were decidedly the least generous in both dollars and time. In a statistical sense the conclusion was most significant. The variable for religious commitment registered as the most powerful of any in the model, whether in predicting the absolute or relative level of family donations.
>
> Furthermore, families who specified that their religion was the most important influence on their generosity were almost three times as generous as those identifying other primary influences. Families with strong religious ties demonstrate the highest level of generosity to their community. Not only do they give to their church, but they also are the most generous contributors to non-religious causes. The linkage is strong, consistent and profoundly relevant.
>
> If charitable donations come primarily from families with strong religious ties, and if it is true that the influence of the church on the lives of Canadians has diminished over the past number of decades, then it is understandable why donations have suffered a secular decline. As fewer Canadians maintain strong religious ties, these non-adherents forego their church's formal indoctrination to a religious-moral philosophy that emphasizes responsibility, compassion and sacrifice, and they avoid the weekly reminder that they should give generously of their substance.[11]

If one is to accept the significance which Dr. Martin attributes to religion in charitable giving (the emphasis added is Dr. Martin's, not mine), it is necessary to recognize the extent to which religious traditions influenced the development of charitable giving. The Old Testament concept of tithing and the Hebrew tradition which teaches that charity is justice were converted from religious duties to civic duties as the United States and Canada became increasingly secular. Among the wealthy the tradition of "noblesse oblige" required the successful to accept that they had a duty to devote time and money to those who were less fortunate. This tradition represents a secularization of the religious concept of stewardship and stewardship also provides a basis for understanding the concept of trusteeship as developed in the law of charities, especially as it applies to private foundations.

Stewardship

The authentic Christian teaching on giving is to be found in the concept of stewardship. Unfortunately, the term "stewardship" has been corrupted so that it is now a synonym for "fund raising". It is difficult for the church to preach about the meaning of stewardship in its Biblical context when the people automatically assume that it is a religious code word for soliciting money. If stewardship is to be understood, the word must necessarily be reclaimed and rehabilitated.

The first image of the steward in the Hebrew scriptures is the steward through whom Joseph's brothers had to deal in Genesis 43 and 44. The steward is a servant but has great authority and speaks as one who has the complete confidence of his master. The image of the steward being in the service of, and accountable to, a very high—and even royal—personage is reinforced in I Chronicles 27 where the names and responsibilities of the stewards in charge of King David's property are listed. The steward in Daniel 1 had charge, not of property, but of persons—the royal Hebrew prisoners of King Nebuchadnezzar. He had authority over Daniel and the other prisoners and reported directly to the king.

This image of the steward as a key player in the social hierarchy of wealth and power made it easy to adapt the concept to the secular tradition of "noblesse oblige" and the role of the squire in medieval times or the conduct expected of "gentlemen" in more modern times. However, with secularization this role became the exclusive domain of the wealthy philanthropist holding vast assets. Those who were not wealthy were left with the gift-out-of-income. Secularization did not incorporate the New Testament concept of stewardship.

The concept of the steward as "trustee" and the corresponding legal recognition that stewards/philanthropists do not have beneficial title to assets under their control, are also found in the Hebraic tradition. The prophet Isaiah severely rebukes the steward Shebna, who is in charge of the palace, for treating the property under his control as if it were his own rather than the master's.[12] Although the Hebrews developed the concept of the steward as one who is very close to a royal master and acts with his master's complete authority, the scriptural image also makes it clear that the steward remains a servant. The steward can have all his power taken away if he becomes arrogant and forgets who actually owns the property.

In the Gospels of the New Testament the role of the steward becomes interchangable with the role of the "servant". While the steward had greater standing than ordinary servants, that standing carried with it an increased level of responsibility. In Luke 12, Christ warns, in a way that is reminiscent of Isaiah, about the dire consequences to be faced by stewards who abuse their position:

> From everyone who has been given much, much will be demanded; and from the one who has been entrusted with much, much more will be asked.[13]

In the Pauline Epistles, the "master" becomes not an earthly king or lord but Christ Himself and Paul presents an image of Christ as the obedient "steward" of God rather than the "master":

> Who, being in the very nature God, did not consider equality with God something to be grasped, but made himself nothing, taking the very nature of the servant . . .[14]

The New Testament moves away from the obligation to tithe and make gifts out of income and applies the requirement of stewardship to ordinary believers, not just the wealthy. In particular, the New Testament holds that all property is given by God and held in trust for Him. As a result of this fundamental shift in perception about the ownership of property, gifts out of income are no longer emphasized. Instead, it would appear that charitable gifts are to be out of capital, although that characterization must be understood in a context where capital is held only in a stewardship capacity.

The most famous New Testament story involving a gift that was *not made*, is the story of the rich young ruler who refused to sell all that he had and give to the poor.[15] Clearly, this was a request to give capital. The prospective donor could not accept that radical disposition of property which he considered to be his own. The most famous gift *made*, is the widow's mite.[16] Again, however small, to the widow her gift was a gift of capital, not income. Similarly we are told that Zacchaeus gave half of his possessions to the poor;[17] Ananias and Sapphira sold their land to fund their gift;[18] and in Acts 2 we read that, after Pentecost, the Christians sold their possessions and goods and gave to anyone as the need arose.

While all of these gifts would appear to be out of capital, that characterization may be irrelevant if those transferring the property only held it as a stewards. Stewards should give income or capital, whichever is most appropriate to the need and occasion. As they have no beneficial interest in either the income or the capital, the kind of gift can be of little consequence to them.

When we reach the stage of analyzing exactly who owns the property which is being given, the radical nature of the stewardship concept becomes evident. Many are philosophically opposed to the use of tax credits for donations to charity because the concept presupposes that the state has some primary claim on a portion of an individual's property. It is even more radical to ask Christians to accept that God has a primary claim on *all* of an individual's property.

Presumably the radical nature of the stewardship concept is the reason the religious world has chosen to treat it as a synonym for fund raising and to focus on the tithe as a gift of income. Tithing is a far more comfortable concept than is stewardship for North Americans who put a high value of their proprietary interest in property. In today's world Christians expect their title to amassed property to provide them with the income required for consumption. Few, if any, remember that when the children of Israel were wandering for 40 years in the wilderness and all of their needs were met divinely through God's gift of manna, He commanded that each one gather only as much as was needed for the day and that no one should keep any for the next day.[19] Daily provision was secure, adequate, and tasty but any hoarded surplus was filled with maggots.

Conclusion

While Christians may choose a personal philosophy based on stewardship and beneficial ownership of all they own by their God, they are not prepared to substitute the "state" for "God" as the steward's master. For purposes of the tax system and society as a whole, retaining the present system of tax deductions for charitable gifts, rather than substituting a concept based on tax credits, is far more compatible with the appropriate philosophical analysis of whose property is being given to charity. Removing the 20-per-cent limit on deductions would remove a financial obstacle to the making of "large" charitable gifts by both wealthy and poor Canadians who are giving out of capital while at the same time adopting a tax policy consistent with the philosophical analysis of the property ownership issue. The government *should not* use the tax code to motivate charitable giving. It *should* remove any disincentives to charitable giving which exist in the code.

FOOTNOTES

1. Letter dated July 31, 1987 from Minister of Finance supplied by Department of Finance officials.
2. *Income Tax Reform*, Department of Finance, Canada, June 18, 1987, Chapter 3, p.17.
3. *The Globe and Mail*, June 30, 1987.
4. *Re Warre's Will Trusts* (1953), 1 W.L.R. 725, [1953] 2 All E.R. 99.
5. Eugene Steuerle, "Charitable Giving Patterns of the Wealthy", *America's Wealthy and the Future of Foundations* (Washington: Council on Foundations, 1987), p.215.

6. *Ibid*, p.218.

7. *Ibid.*, pp.208–209.

8. Custom Questions Charitable Giving, Decima Research.

9. *Ibid.*

10. John A. Edie, "Congress and Foundations: Historical Summary", *America's Wealthy and the Future of Foundations* (Washington: Council on Foundations, 1987), pp.43–64.

11. Samuel A. Martin, *An Essential Grace*, (Toronto: McClelland & Stewart, 1985), pp.191–193.

12. Isaiah 22:16–22.

13. Luke 12:48.

14. Philippians 2:6–7.

15. Luke 18:18–25.

16. Luke 21:1–4.

17. Luke 19:8.

18. Acts 5:1–10.

19. Exodus 16:15–21.