

Doing Good Better? The Differential Subsidization of Charitable Contributions

Calum M. Carmichael
School of Public Policy and Administration, Carleton University
Ottawa ON K1S 0V6 Canada

Abstract

In many jurisdictions, governments subsidize private financial contributions to civic activities that are identified as charitable or publicly-beneficial. The subsidies reduce the price to the donor of transferring a certain quantity of funds to an eligible donee, either by providing the donor with a rebate, a deduction from taxable income, or a credit on taxes otherwise payable, or by providing the donee with a matching grant. Typically, governments that subsidize contributions do at uniform rates. In recent decades, however, several governments have introduced differential subsidies, whereby the subsidy rates differ according to characteristics of either the contributions (their timing and form, and the donee organizations), or the services financed at least in part by those contributions (their recipients, their type).

This paper performs three tasks in the hope of addressing three gaps in the public policy literature on third-sector finance. First, it summarizes an economic case for differential subsidies as a means of making the financing of publicly-beneficial activities more efficient and more effective. Compared to uniform subsidies, differential subsidies could make that financing more efficient by encouraging a higher level of contributions for a given quantity of subsidy outlay. They could make it more effective by generating a greater amount of public benefit from a given quantity of contributions. Although an economic case for differential subsidies can, to some extent, be inferred from strands of the optimal tax and expenditure literature, that case has not been made explicitly or formally, let alone summarized for a non-specialist audience (King 1986, Cremer and others 1998). Indeed, the literature that models the optimal tax treatment of charitable contributions typically precludes making the case from the outset by assuming all charitable spending to be the same in terms of contributors, services, and service recipients (Feldstein 1980, Andreoni 1990, Saez 2004).

Second, the paper outlines practices by which eight governments apply differential subsidies, focusing on the criteria used to identify which contributions to which categories of civic activity receive higher subsidies. To date, differential subsidies remain atypical aspects of the overall legal and fiscal treatment of the third sector. Across countries, this treatment is diverse; within many countries, it has undergone recent and extensive reform. Given this complexity and flux, one can understand why the various practices for applying differential subsidies have received, at most, passing comment in national or international compendia of government policies toward the third sector (Salamon 1999).

Third, the paper offers observations on the evaluation of the practices and criteria, with reference to their potential for making the financing of civic activities more efficient and more effective. Given the other two gaps in the literature, there has been little attempt at such comparison and evaluation, in spite of the importance both to governments that apply differential subsidies, and to those debating or considering them.

References

- Andreoni, J. (1990). 'Impure altruism and donations to public goods: a theory of warm-glow giving', *The Economic Journal*, 100, 464-77.
- Cremer, H., Gahvari, F. and Ladoux, N. (1998). 'Externalities and optimal taxation', *Journal of Public Economics*, 70, 343-64.
- Feldstein, M. (1980). 'A contribution to the theory of tax expenditures: the case of charitable giving', in H.J. Aaron and M.J. Boskin, eds., *The Economics of Taxation*. Brookings Institution, Washington, pp. 99-122.
- King, M.A. (1986). 'A Pigouvian rule for the optimum provision of public goods', *Journal of Public Economics*, 30, 273-91.
- Saez, E. (2004). 'The optimal treatment of tax expenditures', *Journal of Public Economics*, 88, 2657-84.
- Salamon, L.M. (1999). *The International Guide to Nonprofit Law*. John Wiley & Sons, New York.