
H The impact of extending deductible gift recipient status to all charities

In assessing the proposal to extend deductible gift recipient (DGR) status to all charities, the Commission examined the likely impact on tax expenditures of extending DGR status in 2006-07 (the year of the ABS survey of not-for-profit organisations (NFPs) and the latest available year of data for gifts claimed as tax deductions to the Australian Taxation Office (ATO).

This appendix details the data and methods used in the Commission's estimates.

H.1 Data and methodology

Data sources and underlying assumptions

The main data sources used in estimating the cost of extending DGR status are:

- estimates of the value of donations (including bequests) to NFPs from individuals as reported by organisations in the ABS Survey of NFPs (2006-07)¹
- ATO data on the value of claimed gift deductions by individual taxpayers in 2006-07 (McGregor-Lowndes and Newton 2009)
- the percentage of bequests as part of all donations, sponsorships and fundraising to NFPs (Wallace 2009)
- the value of donations and bequests to universities (DEEWR 2008).

However, much of the data required to reliably estimate the potential impact of extending DGR eligibility to include all charities is not collected. For example, there is little information about the level of overall donations to DGRs, endorsed charities, or the sector more generally. Almost all of these entities are not required to lodge annual income tax returns nor regular financial statements with the ATO. The only reliable information relates to Private Ancillary Funds (PAFs) which are required to lodge annual returns to the ATO. Incorporated associations may be

¹ ABS estimates of giving have standard errors of between 25 per cent and 50 per cent (ABS 2009).

required to submit a financial statement to the jurisdictional body responsible for their regulation but most of this information is not collated.

In chapter 7, it is proposed that DGR status be extended progressively, incrementally adding charitable institutions and funds according to the heads of charity. While ABS data separate out the religion and the education and research heads, disaggregated data is not available for the other two heads — the relief of poverty and other purposes beneficial to the community.

Due to these data and other limitations, a number of simplifying assumptions are made to estimate the tax expenditure implications of expanding eligibility for DGR to all charities. These assumptions are that:

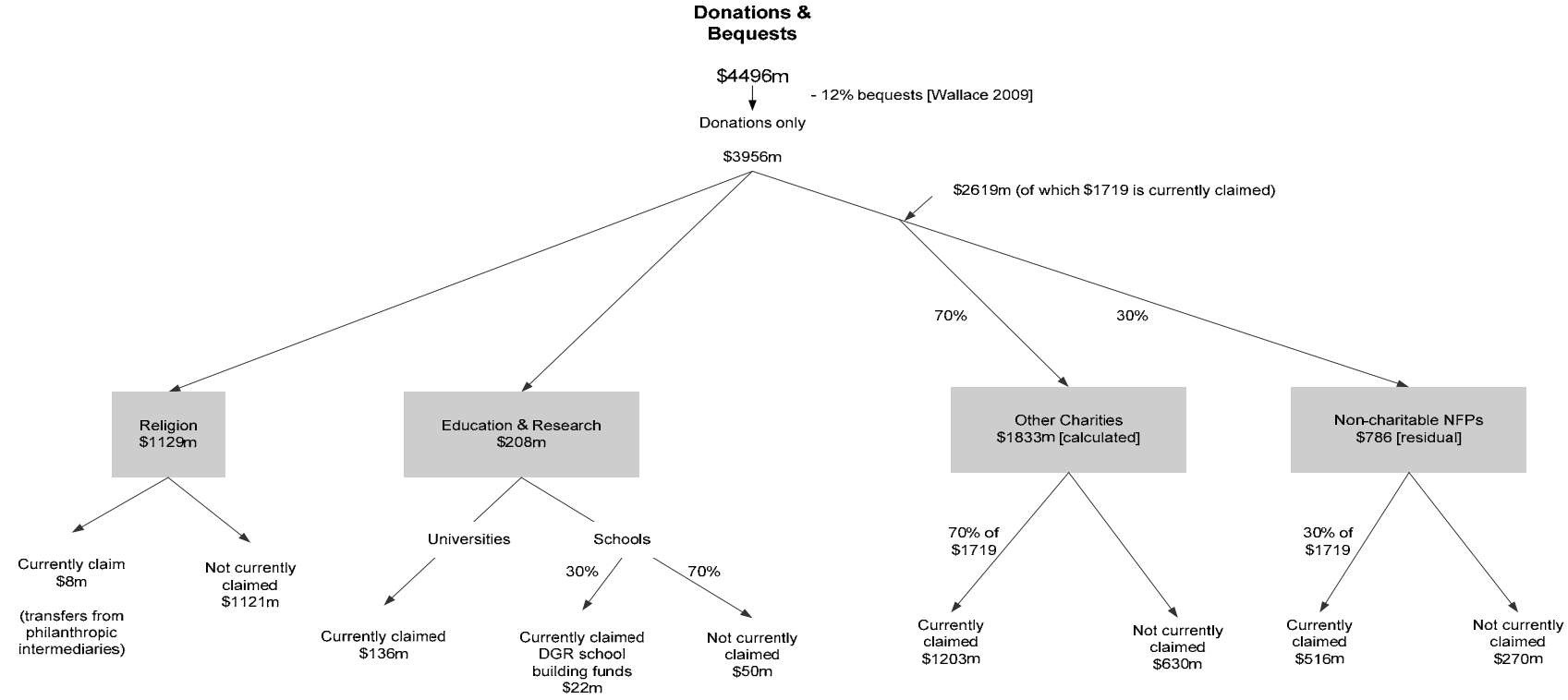
- the proportion of bequests in total donations is uniform across all NFPs
- donations to school building and library funds (already DGRs) make up 30 per cent of donations to education NFPs (other than universities). (Donations to school building and library funds may actually account for much more than 30 per cent of all donations to schools. If this is the case, the estimated increase in tax expenditures from donations to education NFPs will be overstated)
- the share of donations (both total and claimed) between ‘other charities’ and non-charitable NFPs is split 70:30 — roughly in line with the proportion of DGRs (excluding education) that are charitable and non-charitable
- all distributions from philanthropic intermediaries to NFPs are claimed
- all donations which are eligible or will become eligible for a tax deduction are claimed
- all donors face the same marginal tax rate — taken to be the weighted average rate of 32 per cent.

Further, it is assumed that individuals do not alter the total amount they donate in response to DGR status being extended to all charities. However, the implications for tax expenditures of relaxing this assumption and potential behavioural responses are discussed in the final section of this appendix.

Methodology

Given the assumptions, an accounting framework is appropriate. The approach to estimating the expected increase in tax expenditures from extending DGR status to all charities is illustrated in figure H.1. To the extent that the level of donations can be distinguished in the data the estimates are calculated for each head of charity.

Figure H.1 Estimating the cost of extending DGR status to all charities



Share of donations currently not claimed that would be with expended DGR status	100%	100%	100%	0%
Donations claimable with expended DGR status	\$1121m	\$50m	\$630m	\$0m
Estimated tax expenditure (@ 32% marginal tax rate)	\$359m	\$16m	\$202m	\$0m
Total = \$577m				

Total value of donations

The total value of donations to charitable and non-charitable NFPs was sourced from *Not For Profit Organisations 2006-07* (ABS 2009). Donations, bequests and legacies from individuals were combined with donations from philanthropic trusts and foundations to arrive at a total value of donations and bequests of \$4496 million in 2006-07.

The proportion of bequests was assumed to be 12 per cent as reported in *Managing in a Downturn: A Survey of the Impact of the Economic Downturn on Australian NonProfit Organisations* (Wallace 2009). Excluding bequests (which generally are not tax deductible), the estimated total value of donations was \$3956 million.

Donations to religious institutions

The value of donations (excluding bequests) to religious institutions was \$1129 million as derived from *Not For Profit Organisations 2006-07* (ABS 2009). Religious institutions are not currently eligible for DGR status, however, philanthropic intermediaries may offer gift deductibility.² For simplicity, it is assumed that the \$8 million in transfers from philanthropic intermediaries to religious institutions are currently deductible and fully claimed.

As a result, the total value of donations to religious institutions that are not currently claimed but would become claimable if DGR eligibility was extended to include religious institutions is \$1121 million.

Donations to education institutions

The value of donations (excluding bequests) to education and research institutions is \$208 million as derived from *Not For Profit Organisations 2006-07* (ABS 2009). Education and research institutions principally comprise universities and schools (most approved research institutes as associated with universities).

The value of donations and bequests to universities in 2007 was \$155 million as reported in *Finance 2007: Financial Reports of Higher Education Providers* (DEEWR 2008). Adjusting for bequests (12 per cent), the value of donations is

² Gift deductibility is available for philanthropic intermediaries that raise money for religious instruction in schools. As such, it is assumed that funds raised for this purpose are transferred to religious institutions to undertake this activity.

\$136 million. As universities (and their associated research institutes) are currently eligible for DGR status, it is assumed that all donations are deductible and claimed.

Subtracting donations to universities, the value of donations to schools (and their associated funds) is \$72 million. A proportion of these donations are already deductible through school building and library funds. In the absence of reliable data on the value of donations to such funds in 2006-07, it is assumed that 30 per cent (or \$22 million) of donations to schools are to building and library funds. As these funds are already DGR eligible, these donations are deductible and are assumed to be claimed.

Under these assumptions, the total value of donations that are not currently claimed by education institutions, but would become claimable if DGR status was extended to include all education institutions, is \$50 million.

There is information to suggest that donations to school building and library funds could have been much larger than \$22 million. For example, parental/community donations (including fundraising) for capital development in independent schools was reported to be \$160 million in 2004 (ISCA 2008b). Further, for 2006, it was reported that parents provided \$421 million to capital expenditure (ISCA 2008a). While these numbers may include income from fundraising in the former, and fees in the latter, both suggest that the ABS estimates of total donations to education and research are low. It may be that some of the surveyed schools classified donations to building and library funds as another form of income.

This would result in an underestimate of both donations and the amount already claimed, but would not necessarily alter the amount currently donated that is not claimed. As this is the critical number, and in the absence of any more conclusive data, the ABS data is used for the tax expenditure estimate.

Other charities and non-charitable NFPs

Overall donations to other charities and non-charitable NFPs (\$2619 million) is estimated by subtracting donations to religious and education institutions from the total value of donations.

As there is no reliable information on the breakdown of giving to other charities and non-charitable NFPs, it was assumed that giving (both total and claimed) is split 70:30, roughly in accordance with the number of DGRs (excluding education) that are currently charitable and non-charitable (ATO pers. comm., 24 June 2009). Using this split, total donations to other charities was estimated to be \$1833 million while total donations to non-charitable NFPs was \$786 million.

A total of \$1885 million in donations was claimed by Australian taxpayers in 2006-07 (McGregor-Lowndes and Newton 2009). Adjusting for deductions that are already accounted for (in education and research and in transfers from philanthropic intermediaries to religious institutions — \$166 million), the value of claimed deductions for other charities and non-charitable NFPs was \$1719 million.

However, there is no information available to suggest how the \$1719 million is split between other charities and non-charitable NFPs. Using the 70:30 split outlined above, other charities and non-charitable NFPs are estimated to have received \$1203 million and \$516 million respectively in donations that are currently claimed.

Using the above values, it is estimated that other charities receive \$630 million in donations that are not currently claimed but would become claimable if DGR eligibility was expanded to all charities. Non-charitable NFPs receive \$270 million in donations that are not currently claimed. However, donations to these NFPs would still not be claimable under the proposed expansion of DGR eligibility.

The tax expenditure estimate of extending DGR status to all charities

An estimate of the impact on tax expenditures from extending DGR eligibility to all charities can be calculated by multiplying the value of donations that will become claimable by the weighted average marginal tax rate. It is assumed that all donors face the weighted average marginal tax rate (weighted by the number of taxpayers³ in each income bracket in 2006-07) of 32 per cent.⁴

H.2 Implications for tax expenditures

Using the method outlined above, the Commission estimates that the cost of extending DGR status to all charities would have increased tax expenditures by \$577 million in 2006-07 (table H.1). This number is referred to as the accounting estimate and assumes that individuals do not alter the total amount they donate.

³ Alternatively, the average marginal tax rate could have been weighted by the value of donations to existing DGRs. However, relative to low and middle income taxpayers, higher income taxpayers (who tend to donate larger amounts) may be more sensitive to tax incentives (appendix G) and therefore may be more likely to donate to existing DGRs over non-DGR charities. In this case, the average marginal tax rate weighted by the value of donations would not be representative of the marginal tax rate of taxpayers donating to non-DGR charities.

⁴ The weighted average marginal tax rate is calculated using 2006-07 taxation data on taxable income by income bracket and the number of individual taxpayers in each bracket (Australian Government 2006; McGregor-Lowndes and Newton 2009). The marginal tax rate for each income bracket takes into account the Medicare levy and low income tax offset.

Religious institutions would have accounted for \$359 million of the estimated increase in tax expenditures, while education only represents \$16 million. Extending DGR eligibility to include other charities would have increased tax expenditures by \$202 million.

Table H.1 Estimated increase in tax expenditures from extending DGR status (accounting estimate), 2006-07

By type of charity

<i>Head of charity</i>	<i>Increase in claimable donations</i>	<i>Increase in tax expenditures</i>
	\$ million	\$ million
Religion	1 121	359
Education	50	16
Other charities	630	202
Total	1 801	577

These estimates assume that all donations which will become eligible for a tax deduction as a result of extending DGR status will be claimed. However, as outlined in appendix G, only a proportion of philanthropic gifts are claimed. This may be due in part to donations being below the \$2 minimum, individuals failing to keep their tax receipts for donations, or deciding that claiming is not worth the effort. To the extent that some taxpayers will not claim a tax deduction for all newly eligible donations, the accounting estimate will somewhat overstate the increase in tax expenditures.

These results do not take into account any change in giving behaviour as a result of gift deductibility becoming available to a larger number of charities.

Potential behavioural impacts

As discussed in chapter 7 and appendix G, individuals are likely to respond to tax incentives to give. With an expansion in DGR eligibility a number of impacts can arise. These have different implications for tax expenditures.

First, there may be a reallocation of donations from existing DGRs to new DGR charities. This has no impact on overall tax expenditures. It does, however, have potential to reduce donation funding to current DGRs.

Second, there may be a reallocation of donations from non-DGRs to new DGR charities. This is most likely to occur where the organisations have similar purposes but some organisations obtain DGR status while others do not. Given the relatively distinct purposes required for being endorsed as a charity, this effect is likely to be very small. However, there may be a number of NFPs that have not bothered to seek

charity status despite meeting the criteria, and the change in DGR eligibility may make it worth their while to seek endorsement as a charity. While it is not possible to determine the number of NFPs that would seek and gain charity status as a result of widening DGR status, it is expected to be small. Overall, the Commission expects there to be minimal impact on tax expenditures through this reallocation effect.

Third, as the price of giving to newly eligible DGRs would fall as a result of the proposal, the overall level of giving might rise. To estimate the effect it is worth considering two categories of donors: those who previously did not donate to newly eligible DGRs; and those who donated to these organisations before extending DGR eligibility.

Lowering the price of giving to new DGR charities may induce some individuals, who previously did not donate to these organisation, to donate. However, given the current opportunities to donate to existing DGRs, it would only be individuals who favour the newly allowable purposes over those currently allowed, and are strongly influenced by the tax concession that would increase their giving. Therefore, increased giving by these individuals is expected to have only a small impact on tax expenditures.

The greatest effect is likely to arise from individuals who donated to new DGR charities prior to the policy change. The cost of their giving falls by an average of 32 per cent (that is, the assumed marginal tax rate). These donors may react to the policy change by either: increasing their donation by the exact value of the tax subsidy ($\epsilon = 1$), effectively maintaining the value of their individual contribution; increasing their donation by more than the tax subsidy ($\epsilon > 1$); or increasing the amount they donate but by less than the tax subsidy ($\epsilon < 1$) (appendix G).⁵ In all cases, other than no change in giving ($\epsilon = 0$), this will increase overall donations to new DGR charities and hence overall tax expenditures (above the accounting estimate). For example, if donors maintain the value of their individual contributions ($\epsilon = 1$), then the tax expenditure would be higher by around \$271 million (table H.2).

⁵ The price elasticity of giving (ϵ) is expressed in absolute terms throughout this appendix.

Table H.2 Estimated increase in tax expenditures from extending DGR status, assuming the value of individual contributions are maintained ($\epsilon = 1^a$), 2006-07

By type of charity

<i>Head of charity</i>	<i>Increase in claimable donations</i>	<i>Increase in tax expenditures</i>	<i>Increase above accounting estimate^b</i>
	\$ million	\$ million	\$ million
Religion	1 649	528	169
Education	74	24	8
Other charities	926	296	94
Total	2 649	848	271

^a The price elasticity of giving (ϵ) is expressed in absolute terms. ^b The 'increase in tax expenditures above the accounting estimate' is calculated as the differences between the estimated increase in tax expenditures assuming $\epsilon = 1$ (column 3) and the estimated increase in tax expenditures under the accounting method (table H.1).

References

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