

Chapter 17

The Rich/Poor Divide

For Richer or For Poorer?

In our capitalist world, the rich get richer, the poor get poorer. Charity is meant to redress this uneven balance between rich and poor. Unfortunately, the gravitational forces that favor the well-off continue to do so in the charity world.

The dice seems to be loaded on both the supply (donors) and the demand (charities and their beneficiaries) side of the charity equation.

A large part of this is because the definition of charity has been broadened from being about helping the poor and needy (what most people understand it to be) to being about the community good.

The rich get richer, the poor get poorer. It is a hard reality of our capitalist world. In an increasingly globalized world, the gulf is widening. In recent years, the Gini coefficient, a measure of income equality, has been slowly rising, indicating a widening gap, in countries like the U.S., U.K. and Singapore.¹

Charity is meant to help rebalance this uneven status between rich and poor. Yet, it seems that even in the charity world, there are similar

forces that favor the better-heeled over those who are less so. This theme applies to both the supply (donors) and demand (charities and their beneficiaries) side of the charity equation.

The Supply Side

Let us start with donors—those who fund charities.

It should be apparent that rich donors get better treatment from charities compared to those who are less well off. They are courted and showered with attention because they have more to give. They get more recognition when they do give because they tend to give more in absolute terms.

What's more, most income tax regimes favor the rich when it comes to charitable donations. In most countries, income tax is imposed on a progressive basis, that is, the richer you are, the higher the percentage tax rates on your income. To encourage charitable giving, donations are generally tax deductible, that is, there is a tax savings on the donation which would not have occurred if the tax authorities had not allowed the deduction. Due of the progressive income tax structure, the tax savings is computed at the highest marginal tax rate which the taxpayer is subjected to.

To illustrate, a wealthy American taxpayer who is paying income tax at the top marginal tax rate² of 35 percent would be receiving a tax savings of \$35 on every \$100 of donations. In other words, he only effectively pays \$65 for every \$100 he donates. In contrast, a taxpayer whose highest marginal rate is only 10 percent would pay \$90 for every \$100 he donates. For a wage earner who has no taxable income (after various deductions), a \$100 donation actually sets him back by \$100.

In the U.K., the savings are even greater for the rich because the top marginal tax rate is higher, at 40 percent. Therefore, for the wealthy Englishman, a £100 donation will only cost him £60. The situation is even better in Singapore for the wealthy because, while the top marginal tax rate is only 20 percent (less absolute taxes for the wealthy), there is a generous double tax deduction for charitable donations (more tax savings for donations). Thus, a \$100 donation costs a taxpayer, who is at the top marginal tax rate of 20 percent, only \$60 (rather than \$80 if it had only been a single tax deduction). In Singapore, two-thirds of the workforce do not pay income tax so they would have to fork out the full \$100 for every \$100 of donation.

So, who makes up for the \$40 benefit (in the above British and Singaporean examples) that the wealthy taxpayer gets? Assuming that the total tax revenues remain unchanged, the shortfall must come from other taxation sources. Where these include income tax, the income tax net must be stretched wider to catch and thus penalize those earning less.

Alternatively, it could come from raising consumption tax revenues, such as sales tax, value added tax, and goods and services tax. In fact, this is the trend. Free-market economists and governments favor indirect taxes such as consumption tax, over direct taxes such as income tax.³ Direct taxes are seen as harmful to the economy as they lessen the incentive to work, whereas indirect taxes have little or no impact on the incentive to work.

Where consumption tax is increased to make up for the fall in income tax, the poor must shoulder a greater tax burden again since the same rate applies to everyone regardless of one's income level. The lower a person's income, the higher the consumption tax as a proportion of his income. That is why consumption tax is regarded as regressive.

Of course, the rich can make up for their greater benefit by simply donating more. Yes, they do give more, but in terms of absolute and not relative dollars. We had seen previously⁴ that surveys in several countries show quite consistently that the higher-income earners give less as a proportion of their income compared to the lower-income earners.

Therefore, from the donors' standpoint, the better-off give proportionately less than those who are less well-off, and yet they are better treated by charities and the tax authorities.

The Demand Side

Let us now look at the charities and their beneficiaries.

Not unlike for-profit organizations, charities also have to compete for resources. It should, therefore, not be a surprise that the larger players within the charity sector are richer and better off than the smaller ones. They have more resources and reserves, are able to attract funding more easily and enjoy economies of scale in their activities.

In a recent survey by nfpSynergy, big charities in the U.K. were perceived by small charities to have an overall negative effect on the charity sector.⁵ Their feeling of being overwhelmed might be understandable. According to the National Council for Voluntary Organizations, the

income of the U.K. charity sector is concentrated in a relatively small number of organizations.⁶ Over two-thirds of the total sector income in 2004 was generated by two percent of the charities. The study pointed out the emergence of 14 “super-charities”: brand-name organizations with an annual income of over £100 million (US\$200 million), generating 10 percent of the sector’s income. At the other end of the spectrum, 87 percent of charities have incomes of less than £100,000 (US\$200,000) and they generated less than eight percent of the sector’s total income. While the total number of general charities increased by more than 40 percent over a 10 year period, the larger charities have more than doubled in number during that time.

Size aside, charities serve a broad spectrum of beneficiaries. Those that serve the poor and the needy tend to be classified under the social service, or social welfare, or human services umbrella. The other charity segments such as arts, education, environment, sports, religious may have their share of poor beneficiaries, but their focus is on promoting their respective segment needs rather than alleviating poverty.

In general, the social service segment does not get the lion share of donations. In the U.K., the number one cause supported by donors in 2006 was medical research. Overseas disaster relief came in second, with social welfare and disabled people ranked fifth and sixth respectively.⁷ In Singapore, the social service segment only gets about 25% of tax exempt donations, while the education sector gets 39%. For non-tax exempt giving from individuals, the bulk goes to religious causes.⁸ In Canada, only 10 percent of total donations from Canadians go to social services, while the religious charities get 45 percent.⁹ Similarly, in the U.S., only 10 percent of 2006 charitable donations went to human services, while nearly 33 percent went to religious causes.¹⁰

A more focused study conducted by the Center on Philanthropy indicates that less than one-third of all charitable giving by individuals in the U.S. in 2005 was directed towards the needs of the economically disadvantaged.¹¹ Further analysis showed that a mere eight percent of donated dollars were reported as contributions specifically to help meet basic needs such as providing food, shelter and other necessities. The rest went to programs that provided direct benefits ranging from medical treatment to scholarships, or to initiatives that created opportunity and empowerment through literacy, job training programs and so on.

So, from a beneficiary’s standpoint, the majority of charitable giving does not go towards benefiting the poor, but to other causes that improve the community.

The Definition of Charity

A key reason for this state of affairs lies in the definition of charity.

The Oxford dictionary defines charity as “the voluntary giving of money to those in need,” harking back to the Christian tradition of alms-giving. Ask the man in the street and he will likely define charity in similar terms: helping the poor and the needy of society.

However, the industry and legal definition of what constitutes charity or charitable purpose is much broader than that. The legal definition of “charitable purpose” in common law jurisdictions derives from the Charitable Uses Act 1601 of Elizabethan England, as interpreted and expanded by case law.¹² As a result, the modern definition of charitable purposes covers four main areas: the relief of poverty, the advancement of education, the advancement of religion and “other purposes beneficial to the community.” Over time, the last catch-all clause has been interpreted to include areas such as health, arts, heritage, environment, animal welfare and sports. These other “miscellaneous” areas, which are generally beneficial to the community and would usually lessen the government’s burden, are often explicitly added into the definition of charity by tax and charity legislation.

When the meaning of charity is stretched from alms-giving to promoting the community good, quirky outcomes with respect to the precept of closing the gap between rich and poor can arise. For example, the biggest donor in Singapore is the Singapore Totalisator Board, commonly known as the Tote Board. Annually, it gives out more than S\$300 million (US\$207 million), representing a third of total philanthropic giving in Singapore.¹³ It also provided most of the S\$600 million (US\$414 million) funding needed to build the Esplanade, Singapore’s center for the performing arts.

Now, the Tote Board’s income comes from the very legitimate gambling operations of Singapore Pools (lottery) and the Singapore Turf Club (horse racing). The large proportion of gamblers comprises working class people, many looking for the windfall that can lift them from a mundane life or poverty. The arts, on the other hand, is typically associated with the more refined of the populace. Surely unintended, but this looks like a case of the less well-off helping to fund the more well-off. Sensitive to such possible perception, the Esplanade has, to its credit, worked hard to make the arts more accessible by showcasing a multitude of programs that reach out to the masses. To be fair, the Tote Board also channels a significant proportion of its giving to social services.

Singapore is not alone in its use of gambling proceeds to fund programs of national interest. Following the U.K.'s winning bid to host the 2012 Olympic Games, the National Lottery (its largest lottery) committed to initially provide £1.5 billion (US\$3 billion) towards part of the infrastructure costs. About £750 million (US\$1.5 billion) of that commitment was diverted from money that would otherwise have gone towards existing good causes between 2006 and 2012.

In early 2007, the charity sector learned about the possibility of the government dipping further into the National Lottery to fund the escalating costs of the Games. The National Council for Voluntary Organizations, as the umbrella body for the voluntary sector in the U.K., led a campaign to tell the Chancellor of the Exchequer: "Don't raid the Lottery to fund the Olympics." However, the government later announced that a further £675 million (US\$1.35 billion) would be diverted from the National Lottery good cause funds for the Games. After further lobbying by the National Council for Voluntary Organizations and three other charity umbrella groups representing the sports, arts and heritage sectors, the U.K. government finally announced in January 2008 that there would be "no more diversion of funds away from lottery good causes to fund the Olympics."¹⁴

The question of whether charity should be about narrowly helping the poor and needy, or be broadened to serve the common good, goes beyond the matter of mere definition. By putting them under the same umbrella of tax breaks and government support, charitable giving to the poor, rather than being preferentially enabled, has to compete with community programs instead. The net result is that charity for the poor and needy will lose out; first, by having to compete and, secondly, by the glamour attached to (and the greater appeal of) some of these other causes.

Moreover, the degree of accountability is also impacted. The fundamental basis of charitable giving is generosity. Despite a ground swell of support for greater accountability of charities, the allocation of resources in the charity "marketplace" will continue to be driven less by economic value than by relationships between donors and beneficiaries, and their fundraisers.¹⁵

The basis of government programs, on the other hand, is rigorous cost-benefit analysis and public accountability. Having broad-based community programs funded under the aegis of charity reduces that level of public accountability.

In sectors such as education and healthcare, some observers have asked whether some of the programs funded through public donations

should not be funded by, and remain the responsibility of, the government. Education, in particular, gets an extra boost from donations. In addition to tax exemptions and the intrinsic appeal of education, there are opportunities for naming rights and the government's encouragement through matching grants for donations (sometimes by as much as 3:1 in Singapore). Consequently, many universities around the world have amassed staggering endowments and other donations from loyal alumni and philanthropists. Their reserves will provide for current and future needs to no end. For example, Harvard University, which has close to a breakeven net operating budget, has more than US\$35 billion in its investment portfolio.¹⁶

A Preferential Option for the Poor

In summary, it seems that the well-off are not just generally favored in life but in the charity space as well. To be true to the spirit of charity in providing for the poor and needy, we need to be vigilant of the gravitational forces that favor the well-off. Reviewing what constitutes charity and who is more deserving of the charity support mechanisms could be one big step towards this objective.

Endnotes:

Adapted from: "For Richer or For Poorer?" *SALT*, July-August 2007; and "In aid of the poorer or richer?" *The Straits Times*, September 4, 2007.

- 1 The Gini coefficient is the most widely used summary measure of the inequality of distribution of income. It represents an overall measure of the cumulative income share against the share of households in the population. It is expressed as a value between 0 (perfect equality) and 1 (perfect inequality—one person has all the income and all others have zero). The Gini coefficients for developed countries are: Singapore 0.49 in 2000, and 0.52 in 2005; U.K. 0.51 in 2000 and 0.52 in 2005; U.S. 0.462 in 2000 and 0.469 in 2005.
- 2 All tax rates used here are as of year of assessment 2007 in the respective countries. Thus, top tax rates are as follows: U.S. 35 percent, U.K. 40 percent, and Singapore 20 percent.
- 3 Singapore, for example, had progressively reduced its individual and corporate income tax rates since 2000, from 26 to 20 percent, and increased its goods and service tax (GST) rate since 1994 from 3 percent to 7 percent. However, each time the government raised the GST rate, it introduced an offset package to reduce the impact of the hike on the poor. See Audrey Tan, "7% GST / 2-point hike," *The Straits Times*, February 10, 2007.

- 4 See Chapter 11, "Elite or e-Lite Giving."
- 5 Chris Greenwood, *The State of the Third Sector 2007* (nfpSynergy, 2008). The survey polls senior executives of charities. Unsurprisingly, the majority of the respondents who felt that the statement "I think very big charities have a negative effect on the sector as a whole" was true, were from small charities.
- 6 Karl Wilding, Jenny Clark, Megan Griffith, Veronique Jochum and Susan Wainwright, *The UK Voluntary Sector Almanac 2006: The State of the Sector* (National Council for Voluntary Organizations).
- 7 Natalie Low, Sarah Butt, Angela Ellis Paine and Justin Davis Smith, *Helping out: A national survey on volunteering and charitable giving* (Office of the Third Sector, Cabinet Office, Prepared by National Center for Social Research and the Institute for Volunteering Research, 2007.) Since each survey respondent identified multiple causes, the report could only provide a sense of the relative ranking of the sectors.
- 8 *The State of Giving* (National Volunteer & Philanthropy Center, 2005).
- 9 *Caring Canadians, Involved Canadians: Highlights from the 2004 Canada Survey of Giving, Volunteering and Participating* (Imagine Canada, 2006).
- 10 *Giving USA 2007, The Annual Report on Philanthropy for the Year 2006*, (Giving USA Foundation, researched and written by the Center on Philanthropy at Indiana University, 2007). The report provides target of contributions. Apart from the sectors, 10 percent went to foundations and 8.8 percent related to contributions that were not tracked, deductions carried over and unallocated giving.
- 11 *Patterns of Household Charitable Giving by Income Group, 2005* (Google, prepared by The Center on Philanthropy at Indiana University, Summer 2007).
- 12 Common law legal systems are in widespread use and include the U.K., most of the U.S. and Canada, and the Commonwealth countries. The landmark case from which the modern definition of charitable purposes comes from is *Commissioners for Special Purposes of Income Tax v. Pemsel* (1891). In this case, Lord McNaughten identified the four heads of charity.
- 13 The last official figure (of more than S\$300 million) on the Tote Board annual giving was provided in a parliamentary debate. Industry sources suggest that, in recent years, the Tote Board's grants have increased significantly. The amounts relative to total philanthropic giving is from *The State of Giving* (National Volunteer & Philanthropy Center, 2005.) For Tote Board, view www.singtote.gov.sg. For Esplanade, view www.esplanade.com.
- 14 See "Olympic Lottery Campaign" and related links at NCVO website www.ncvo-vol.org.uk/policy/index.asp?id=3852. The other three U.K. charity umbrella groups in the campaign are Voluntary Arts Network, CCPR and Heritage Link. National Lottery is at www.national-lottery.co.uk.
- 15 Chapter 1, "The missing hand of Adam Smith" and Chapter 20, "Doing good better," cover, in greater detail, the issues of the charity marketplace and the demand for greater accountability.
- 16 *Harvard University: Financial Report, Fiscal Year 2007*.