Centre for Social Impact and Philanthropy

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How India Can Encourage Charitable Donations

A Policy Brief

This study was commissioned by the Centre for Social Impact and Philanthropy (CSIP) and completed in a research partnership with Centre for Budget and Governance Accountability (CBGA).

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I: Why are Charitable Donations Important?

The sudden lockdown announced by the Indian government in late-March 2020 to stop the spread of the COVID-19 virus led to multidimensional socio-economic crises in the country. While these crises have had a devastating impact, the extent of the damage was stemmed somewhat by thousands of charitable organisations, which stepped forward to mitigate the situation in different ways. For instance, they arranged food for the needy, shelter homes for those rendered homeless, helped the government identify COVID-19 hotspots, delivered services to vulnerable groups, and addressed many other socio-economic challenges. Clearly, the situation would have been far worse had these charitable organisations not acted in time to lessen the impact of the pandemic.

Indeed, the crises spawned by the COVID-19 pandemic have reaffirmed the critical importance of charitable organisations.

However, it is imperative to emphasise here that charitable organisations make a difference not only during emergencies such as the COVID-19 pandemic but through every single day of the year. While their role in alleviating the hardships faced by the most underprivileged people in the country is well known, that role is not limited purely to addressing issues related to hunger, health, education, sanitation, violence, etc. Indeed, their efforts in advocating for excluded and marginalised groups, ensuring accountability from a range of institutions, shaping social norms, and serving as a watchdog have all been critical in strengthening both development and democracy.

The functioning of a charitable organisation, like any other organisation, requires resources. In fact, the scale and quality of the work that charitable organisations do depends, to a large degree, on the resources they have. Charitable donations or philanthropic giving by private entities, both individuals and businesses, constitute an important part of the resources that charitable organisations raise.

Need for a better understanding of the relationship between tax incentives and charitable donations

Given the importance of the charitable sector, governments across the world frame policies with the objective of increasing the resources available to the sector. One such prominent policy instrument is that of providing tax incentives for charitable donations. The basic assumption behind offering tax incentives for charitable donations is that they encourage taxpayers to donate more.

In this context, Centre for Social Impact and Philanthropy (CSIP), Ashoka University, and Centre for Budget and Governance Accountability (CBGA) conducted a study on the relationship between tax incentives and philanthropic giving. Focusing on 12 select countries, the study aimed to find what kind of tax incentives different governments provide for charitable donations. It also tries to assess what evidence exists about the effectiveness of tax incentives in influencing charitable donations.

This Policy Brief presents some of the main findings of the study as well as recommendations to help frame better policies for the charitable sector.

How do tax incentives influence charitable donations?

When an individual makes a charitable donation, she incurs a cost or a price. If there are no tax incentives, the price of giving is the same as the monetary value of a donation. Tax incentives reduce a donor's tax payable. The reduction in the tax payable by the donor, in turn, helps reduce the price of giving and thereby, arguably, motivates philanthropic giving.

It should be noted that several other factors, such as the culture of giving, level of economic development, and individual personality traits, influence charitable giving. Thus, tax incentives are only one of the several factors that can affect charitable giving.

The monetary benefit that donors can derive from such tax incentives depends on the following factors:

- The form of tax incentives
- Rates of taxes
- Rate of incentives
- Ceiling on incentives

The non-monetary aspects of tax incentives, such as the causes eligible for tax-incentivised donations, complexity and the fairness of the tax incentive regime, also matter in deciding the benefits of tax incentives derived by donors.

Each of these factors affects the generosity of the tax incentives offered in different ways. For example, when tax incentives are offered in the form of a deduction from taxable income or tax payable, the higher the tax rate the donor faces, the higher the level of monetary benefit that can be derived. However, if the tax incentive is in the form of credit, then the tax rate does not have any effect on generosity. The rate of incentive and ceiling also affect the generosity of the tax incentives offered. For Instance, the higher the rate of the incentive or ceiling, the higher the level of the monetary benefit a donor can enjoy. Further, the greater the number of causes eligible for tax incentivised donations, the higher the number of choices of causes to which donors can donate and avail tax incentives. In short, the generosity of a tax incentive structure is the combined effect of all of these factors.

'Another very important role played by tax incentives for charitable donations is that they have a 'signalling effect', such that their mere existence sends the signal to taxpayers that the government endorses charitable donations. Such signalling can also influence positively the level of donation.

II: How does India's Tax Incentive Structure Compare with Other Countries?

The cross-country comparative analysis of our study reveals some interesting insights about the tax incentive structure in India. Some of the main findings are presented hereafter.

Taxes on which incentives are provided for philanthropic giving

India provides tax incentives on personal income tax and corporate income tax, as do all the other 11 countries in the sample. However, other countries also provide incentives on some additional taxes (Table 1). The most notable of these taxes is inheritance tax. All the six countries in this sample that have inheritance tax provide incentives on it. To put that in context, it has been argued that the absence of an inheritance tax in India lowers the motivation to donate.

Table 1: Taxes on which Incentives for Charitable Donations are Offered

Countries	Personal Income Tax	Corporate income Tax	Inheritance tax	Wealth tax	Capital gains tax	Donation/ Gift Tax
Bangladesh	Yes	Yes	-	-	-	Yes
Brazil	Yes	Yes	Yes	-	-	Yes
China	Yes	Yes	-	-	-	-
France	Yes	Yes	Yes	Yes	-	-
India	Yes	Yes	-	-	-	-
Mexico	Yes	Yes	-	-	-	-
Norway	Yes	Yes	-	-	-	-
Singapore	Yes	Yes	-	-	-	-
South Africa	Yes	Yes	Yes	-	-	Yes
South Korea	Yes	Yes	Yes	-	-	-
UK	Yes	Yes	Yes	-	Yes	-
USA	Yes	Yes	Yes	-	Yes	-

Further, in the sample of 12 countries, nine countries also provide tax incentives for cross-border donations, i.e., when a citizen makes donation to a charitable organisation based outside the country. India (along with China and Singapore) stands out in this regard as it does not have such a provision.

Generosity of tax incentives

Broadly speaking,[1] France, Singapore, and the UK seem to have the most generous tax incentive structures in the sample of 12 countries, while Bangladesh, Brazil and Mexico seem to be on the other side of the spectrum. The extent of generosity of incentives is higher in these countries for different reasons. For example, in France, it is because the incentive is in the form of a credit. In the case of Singapore, it is because of the high rates of incentive and high ceiling, and in the case of the UK, it is the combination of the tax rate, form and rate. Bangladesh's lower level of generosity is mainly on account of its lower rate of incentive, while for Brazil and Mexico, it is due to low ceilings (Table 2).

India is somewhere in the middle in terms of the generosity of its tax incentives. Under its most popular tax incentive scheme (Section 80G of the Indian tax code), India allows a 50 per cent deduction for donations to charitable organisations. The distinctive feature in India is that it is the only country among the 12 surveyed where donations to government entities and funds also attract tax incentives. Further, the tax incentives provided to some government entities and funds are relatively more generous (with 100 per cent deduction allowed). This difference in the level of generosity holds even in the case of the ceiling that applies to donations to charitable organisations on the one hand and select government entities and funds, on the other. While donations to charitable organisations has a ceiling of 10 per cent of taxable income, that on donations to select government entities and funds has a much higher ceiling of 100 per cent.

Table 2: Structure of Tax Incentives on Personal Income Tax

Countries	Form	Rate	Ceiling
Bangladesh	Deduction	15%	Maximum donation allowed is 30% of taxable income or BDT 15 million, whichever is lower
Brazil	Deduction	100%	8% of tax payable with charity area-based exemptions[2]
China	Deduction	100%	30% of taxable income
France	Credit	66%	20% of taxable income
India	Deduction	50%, 100%	10% of taxable income in most cases, 100% when donating to select government funds and entities
Mexico	Deduction	100%	7% of previous year's taxable income
Norway	Deduction	100%	NOK 50,000
South Africa	Deduction	100%	10% of taxable income
South Korea	Credit	15%, 30%	100% of tax payable
Singapore	Deduction	250%	Annual taxable income, remaining amount can be carried over for the next five years
UK	Deduction & Hybrid model	100%	100% of tax payable
USA	Deduction	100%	60% of taxable income

Recent changes in tax incentives for donations

Tax incentives, like any other government policy, evolve over a period of time. Broadly, these changes can be divided into two categories: those that increase the benefit derived by the donor, and those that reduce the extent of the benefit.

In the case of India, tax incentives for donations, especially the 80G scheme, have remained more or less unchanged over the last four decades, except for the addition of certain government entities and funds to the scheme. However, overall, the tax incentive structure for giving to the charitable sector seems to have become less generous over time and has hence reduced the benefit that donors can derive. There are various reasons for this. One, the tax incentive scheme introduced in the 1990s (under section 35 AC of the tax code) was abolished in 2017. Two, in 2020, a new optional tax regime for Personal Income Tax was introduced, under which a taxpayer can choose between two tax structures. One tax structure, the older one, has higher tax rates and incentivises philanthropic giving. The other tax structure, the new one, has lower rates but does not incentivise donations. Taxpayers may choose which scheme they wish to follow. These changes, coupled with the lowering of rates of personal income tax and corporate income tax over time[3], have reduced the generosity of the tax incentive structure. Additionally, the abolition of wealth tax and inheritance tax means that there is no possibility of providing incentives for charitbale donations on these taxes.

During the COVID-19 pandemic, many countries changed tax incentives to encourage donations. In the sample of 12 countries, while the USA and China increased the level of benefit, India did not do any such thing. In India, the only change was the introduction of a new fund called Prime Minister's Citizen Assistance and Relief in Emergency Situations (PM CARES).

III: What Evidence Exists about Tax Incentives' Effect on Charitable Donation?

Whether tax incentives have any effect on donation, and if so, to what extent, is a subject of considerable interest for the research and policy community. There are a number of studies on this subject. However, most focus on the USA and the UK. Some studies also exist for France, South Korea, Singapore and India, but they are very few in number.

Given that a number of factors influence charitable donations, it is challenging to delineate the effect of tax incentives on such donations. This also means that learning from one country may not necessarily be applicable to other countries.

Notwithstanding these concerns, some broad pointers can be made about the effect tax incentives have on charitable donations. They are:

- Overall, tax incentives do seem to have a positive influence on the level of charitable donations. As in, an increase in tax incentives (i.e., a decline in the price of giving) leads to an increase in charitable donation.
- The extent of influence, however, is generally small for the average taxpayer. This means that a 1 per cent decrease in the price of giving leads to a less than 1 per cent increase in the level of giving.
- The influence of tax incentives on charitable donations is found to be higher for higher-income groups. In some cases, tax incentives are found to be helpful in also motivating giving in the future.
- Simple and accessible tax incentives generally have a positive influence on the level of giving.
- When a large number of causes are eligible for tax incentives, they can have a positive influence on the overall level of donation.
- Even when tax incentives are not a deciding factor in motivating charitable donations, they have a signalling effect, which can positively influence donations.
- The absence of taxes that affect the wealthy relatively more, such as wealth tax and inheritance tax, weakens the influence of incentives on donation.

While these findings are based on a cross-country survey of the available literature on this issue, it is important to note that not all countries have relevant studies. In the case of India, only two studies on the influence of tax incentives on donations could be found, but both are dated. There have been a number of changes in India since those studies were undertaken, such as an increase in the level of income, changes in tax rates, etc. Hence, there is a lack of evidence in India about whether, and to what extent, the current tax incentive structure influences philanthropic giving. In the absence of such evidence, policies governing tax incentives seem to be based on anecdotal understanding, rather than on evidence.

IV: What Can the Indian Government Do?

Governments have an important role to play in encouraging charitable organisations and this role involves two broad considerations: framing policies with the objective of encouraging the charitable sector, and designing policies such that they are effective. Given the fact that tax incentives for charitable donations already exist, India fulfils the first consideration. However, there is considerable scope to improve on the second aspect, which is to design policies that are effective in achieving the objective of increasing the resources of the charitable sector. The following steps can be taken for effective policymaking:

- **Rigorous studies for evidence-based policy making:** There is a need to carry out rigorous studies on the impact of tax incentives on the charitable sector in India to understand their role and effectiveness. Indeed, some recent studies are available for certain other types of tax incentives[4] that analyse whether these tax incentives helped in increasing employment and/or investment. These studies are important as they help provide a sense of whether tax incentives have been effective in achieving their intended objectives. However, there is an acute lack of literature that assess the effectiveness of tax incentives for charitable donations and how they impact charitable organisations. Hence, it is necessary to undertake studies to assess the importance of tax incentivised charitable donations from the point of view of charitable organisations.

- **Improve availability of tax data:** For informed policy-making, it is important that more disaggregated data (such as on the number of corporates/individuals donating, the amount donated by different tax slabs donors fall under, the sectoral composition of donations, etc.), are made available by the government. The government of India provides aggregate numbers on revenue forgone for charitable donations to charities in the statement "Revenue Impact of Tax Incentives under the Central Tax System" (earlier known as the Revenue Forgone statement) in the Union Budget. However, the reporting structure on tax revenue forgone does not provide any further details that can help understand the amount donated by different sets of donors and the nature of the donations. In the Financial Year 2012-13, the Income-tax Department introduced an e-filed return (ITR-7) for charitable entities in which information on the donations received by the entity has to be provided. Similarly, all persons with incomes above Rs 5 lakh are compulsorily required to file returns electronically. With regard to the 80G deduction, the tax return of the donor contains the details of the donee and her/his Permanent Account Number (PAN) along with the amount on which the deduction has been claimed. Therefore, data capturing the details of the donation made by a donor along with details of the recipient is available with the Tax Department. The government should consider making such data public, in line with good practices in other countries, such as the USA.

- **Raise the level of incentives provided:** In light of the massive gaps in India's achievement of the Sustainable Development Goals, which have been exacerbated by the impact of the COVID-19 pandemic, an increase in the rate of incentive provided as well as raising of the ceiling would send a strong message to donors on the desirability of philanthropic contributions.

- **Re-introduce taxes that affect higher-income groups:** Given the significant increase in inequality, particularly amid the COVID-19 pandemic, it is recommended that the government re-introduce wealth and inheritance tax, and provide incentives on them for charitable donations. The scale of recorded charitable donations in countries such as India and China is much smaller compared to countries such as the UK and the USA, even after accounting for differences in the level of income. The absence of wealth and inheritance tax is regarded as one of the reasons for the lower level of philanthropic giving. These taxes were removed on the ground that the administrative costs associated with collecting revenue outweigh the amount of revenue collected. However, this logic may not hold true anymore as with the digitalisation of tax returns as well as other measures, administrative costs are likely to have come down, whereas revenue collection from these taxes can be significant given the increase in wealth held by the rich. Reintroduction of these taxes, along with incentives on them for philanthropic giving, will not only result in additional tax revenue for the government, it will also increase the resources of the charitable sector.

See full report –
Tax Incentives for Philanthropic Giving: A Study of Twelve Countries
Click here

[1] As mentioned earlier, the amount of the benefit donors get depends on the combination of the form, rate and ceiling along with tax rate if the form is deduction or hybrid. Due to this, it is difficult to rank countries precisely on the basis of the level of generosity of tax incentives for charitable donations. And, only some broad insights can be drawn.
[2] This is the overall ceiling on donations to various causes, but the 'ceiling are different for different causes. While the ceiling is 4% for donations to certain cultural activities, the cap for funds used to support public policies for children and youth is 1% of the income tax due.
[3] I.e., when compared to the tax rates imposed in the 1980s.
[4] Such as the tax incentives provided to corporates for investment in backward areas, in special economic zones, etc.

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