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Philanthropy and Taxation

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"We hear all around us about practical religion, and analysing all that, we find that it can be brought down to one conception — charity to our fellow beings."

- *Swami Vivekananda*

1.1 Introduction

Morality represents the way we would like the world to work, and economics represents how it actually does work and this is not a new phenomenon. Since the very first economic or social barters were made by man, a disconnect has existed between the creation of individual and social wealth. This gap has been filled by 'giving.'

"At every stage of our species' development, 'giving' has been with us. Whether one sees this phenomena as evolutionary (manifest from pro-social behaviour) or spiritual (an urge from deep within our souls), the fact remains that giving 'in all its forms' has been one of the greatest factors in the success of humanity and spans all the domains of 'human' assets; the intellectual (knowledge, experience, emotion and insight), economic (wealth in all its forms), cultural (arts and language), social (time, group structures) and even biological (from simply strength to the very body in entirety).

In reality, there are few beings on our planet who have not been touched in some way by giving (regardless of whether that is a small act of generosity from a stranger, or being lifted out of poverty with a micro loan), and few who could argue-away the profound legacies left by the outcomes of man's urge to improve the present and future position of his society. Without some form of giving, many of mankind's greatest achievements simply would not have occurred. Giving is also one of the few activities mankind often undertakes without the geographic, cultural, social and political prejudices applied to other aspects of life."[1]

1.2 Importance of Philanthropy

"Global inequity both among people and nations is among the greatest challenges of our times. Severe disparities exist not only in wealth, but in health, education, economic opportunity, and access to new technologies. Less apparent but also troubling are inequities in human security, access to power, and democratic freedoms. Despite the urgency and importance, our understanding of the forces and consequences of severe inequity is critically limited.

[1] Charity, Philanthropy and Society, Articles and Interviews by Vikas Shah MBE

Philanthropy has a pivotal role to play in advancing global equity, acting beyond the broader concerns of government and the narrower interests of business. Social investing can contribute not only to monetary resources, but also new skills, fresh thinking, and innovative approaches to global problems. The unprecedented growth of global wealth, the globalization of the economy, the increased mobilization of individuals and the development of a global nonprofit sector are creating an encouraging environment. Most importantly, there is a growing recognition that political boundaries do not define our moral compass, our social responsibility or even our enlightened self-interest any more than geographical borders contain economic markets or cultural influence.

India has long established traditions of philanthropic and charitable engagement. Yet to date, philanthropy has not systematically addressed the country's most fundamental development problems. Philanthropy has provided charitable relief to those in need, but not sought to address the underlying causes of deprivation. While many individuals, families, and corporations give generously, many more need to become involved if philanthropy is to have a significant impact. The prevailing mindset that government should be the sole provider of social services and needs is to be radically changed.

This paper begins with an overview of India's development and equity challenges. It then explores philanthropy in India. Throughout, it seeks to explore the extent to which philanthropy does – or doesn't – support and accelerate a process of equitable social and economic development in India. Documentation and data on philanthropy is extremely limited. Much more research is needed in order to develop an accurate picture of philanthropic investors, their investments, and impact."

1.3 Philanthropic Traditions and Influences in India

The cultural roots of philanthropy in India are ancient and deep, and have given life to long established traditions of philanthropic engagement, social service, and voluntary work. Religion has always played a major role in philanthropic giving in India, and continues to be a profound influence on giving. However various other factors —social, economic, and political — have affected and accelerated the emergence of civil society in modern India and shaped the role and practice of philanthropy today.

A contemporary trajectory beginning in the mid-nineteenth century has built upon religious and cultural traditions and created a vibrant and innovative philanthropic landscape. While the ethos of 'giving' in India is clearly 'personal', in contrast with the institutionalized charitable giving practiced in the West, the last decade in particular has witnessed a trend towards more organized charitable giving.

The history and development of philanthropy in contemporary India is, in several ways, synonymous with the growth and establishment of the voluntary sector in India. Several major influences have strengthened, shaped, and defined philanthropy and the broader civil society in which it operates. The most significant influences are noted below.

1.4 Early Traditions

The worthiness of social service is deeply engraved in India's social consciousness; individual and unorganized giving has existed in various forms from time immemorial. The concepts of daana (giving) and dakshina (alms) in Hinduism, bhiksha (alms) in Budhhism, and zakaat (prescribed offerings) and sadaqaat (voluntary offerings) in Islam have been a part of Indian culture for many centuries. It was, however, with Buddhism, through the order of monks (sanghas) and later with Christianity, that serving the needy first became an organized institutional concern.

As in several other societies, the relationships between individuals and groups were established to ensure that the care of the under-privileged and vulnerable members of society was built into social institutions and structures. Social institutions provided mechanisms to help meet the needs of the old, the sick, and the handicapped, and well as other helpless sections of the community. For example, the joint family, caste members and community councils often took responsibility for individuals who needed support.

1.5 Growth of the Voluntary Sector in India

The contemporary non-government, non-profit, and voluntary sector in India owes its origin to Gandhian principles, philosophy, and practices. Inspired by Mahatma Gandhi, individuals established village-oriented community organizations throughout the country

Subsequently, many developed into powerful and effective organizations, capable of delivering social services in an efficient and cost-effective manner. Institutionalized philanthropy also gained momentum from the industrialization that gathered force from the late nineteenth century onwards. Gradually, corporate gains began to trickle towards welfare and development. Several business houses that emerged during rapid industrialization laid the foundation for a philanthropic tradition that have been followed and strengthened by succeeding generations. More broadly, with the spread of industrialization, there came a period of rapid economic and social change characterized by the transformation of villages into towns and of agricultural economies into industrialized ones. The economy of rural self-sufficiency was disturbed; the emphasis shifted to urbanization. The dawn of Independence in 1947 witnessed the beginning of an extensive era of development activities in the country, with the Indian government realizing that political freedom was incomplete without economic growth and social development. Planned development was envisaged through five-year plans, which made provisions for the welfare of people. Separate budget allocations were made in every five-year plan for development purposes.

1.6 The Philanthropic Landscape of Today

Philanthropy is traditionally practiced by private Trusts, family foundations, corporate donors, and intermediary agencies. While a variety of foundations and Trusts have made strategic and systematic investments in the social space, the inputs and supplements provided by the private sector have been minimal. Many Trusts established by corporate leaders are increasingly strategic in addressing societal challenges. The information technology revolution has had a significant and positive impact on philanthropic investment trends. There is the beginning of a philanthropic infrastructure to support and nurture philanthropic engagement. Increasingly, philanthropic and social investment capital in India targets such areas as education, healthcare, population, gender issues, natural resource management, energy, and enterprise development; many initiatives are focused on rural India.

1.7 The Non-profit or Voluntary Sector in India

The nature and character of non-profit organizations or voluntary organizations have undergone a noticeable change in the last decade and a half. A large number of organized, development-oriented, charitable and voluntary institutions have emerged that are led by professionals, and employ full-time, paid staff, who are trained to meet the needs and demands of the sector more effectively.

The factors that have contributed to this astronomical increase in the number of such organizations in the last few decades include weakening government delivery systems, widespread poverty and deprivation and increasing inequity, rising awareness and social concern about under-development and inequity, and the influx of increased funding both indigenous and foreign for development purposes.

The relationship between the non-profit sector in India and the government is one of collaboration more than competition. The government has set up central and state welfare boards to promote and fund the sector and to provide technical support. From the very first five-year plan, budget allocations have been made for providing assistance to the voluntary sector as policy-makers have felt that this sector can deal with socio-economic problems that the state is unable to address effectively. The government also grants tax relief to individuals and organizations that donate to the voluntary sector.

1.8 Philanthropic Investors and Investments

"A wide range of philanthropic giving takes place in India, ranging from individuals making modest gifts to international foundations hoping to influence the development and direction of civil society. Broadly, philanthropic resources can be classified under the following categories:

- Individual giving
- Foundations and Trusts
- International foundations and charities
- Regranting organizations
- Religious philanthropy
- Corporate philanthropy"[2]

Thus helping others takes countless forms, from giving money to charity to helping someone cross the road, springs from countless motivations, from deep-rooted empathy to a more calculated desire for public recognition. Indeed, social scientists have identified a host of ways in which charitable behavior can lead to benefits for the giver, whether economically via tax breaks, socially via signaling one's wealth or status or psychologically via experiencing well-being from helping. Charitable organizations have traditionally capitalized on all of these motivations for giving, from attempting to engage consumers with emotion-laden advertising to pushing governments to offer tax incentives. Also the CSR regulations under the Companies Act, 2013 has committed to corporate philanthropy, and the nonprofit sector must be ready to absorb the new resources to create maximum impact on the ground.

1.9 Income Inequality in India

"India is no stranger to income inequality, but the gap is widening further. Last year's survey by Oxfam had shown that India's richest 1 % held 58 % of the country's total wealth, which was higher than the global figure of about 50 %. According to the latest survey, the wealth of this group increased by over Rs 20.9 lakh crore during the period under review, which is an amount close to the total expenditure estimated in the Union Budget 2017. India's top 1 % of the population now holds 73 % of the wealth while 67 crore citizens, comprising the country's poorest half, saw their wealth rise by just 1 %.

The data sources for the Oxfam report include Forbes' Billionaire List 2017, World Bank data, and last year's edition of Credit Suisse's Global Wealth Databook, which brings together household balance sheets and survey data from around the world to estimate how wealth is distributed within countries and globally.

Oxfam furthermore makes several recommendations to start fixing the problem of income inequality. On the Government's part, it has asked for things like promoting inclusive growth by encouraging labour-intensive sectors that will create more jobs, imposing higher tax on the super-rich, implementing policies to tackle all forms of gender discrimination and sealing the "leaking wealth bucket" by taking stringent measures against tax evasion. The report reveals that the top

[2] Philanthropy and Equity: The Case of India by Priya Viswanath & Noshir Dadrawala, June 2004

1 % is evading an estimated $200bn in tax. More significantly, developing countries are losing at least $170 billion each year in foregone tax revenues from corporations and the super-rich."[3]

"While economic growth is absolutely crucial in raising living standards of India's vast population, the distributional effects of economic growth, as measured by income distribution, play a significant role in determining the long-term development trends and socio-economic well-being of the citizens. India is one the richest countries in the world, and yet, the average Indian is relatively poor as a result of highly-skewed income distribution.

Rising income inequality has developmental implications. The super-rich avoid taxes by using innovative schemes to shelter their wealth and manipulate the political system without repercussions. This impedes the Government's ability to raise revenues that contribute to slower poverty reduction and also adversely impacts social spending to reduce social inequalities of health, education and employment. India already fairs poorly in this area. Currently, 3 % of the GDP goes towards education and only 1.3 % towards health. By comparison, China in percentage terms of GDP allocated to education and health 4.3 and 5.4, respectively. The growing divide undermines democracy and promotes corruption and cronyism." [4]

2. Relationship between Tax and Charity

2.1 Is there a relationship between Tax and Charity?

"Income taxation policies normally provide a substantial price subsidy/tax deduction for charitable donations, and the degree to which people respond to this subsidy is a matter of considerable policy interest. Most state income taxes allow a deduction for charitable contributions, which effectively reduces the price of those contributions. In general, the case for providing tax incentives for charitable donations is stronger when charitable decisions are more responsive to the incentives.

Private giving to charitable causes has significantly grown in the past several decades. Experts predict that the combination of increased wealth and an ageing population will lead to an even higher level of donations in the coming years. The economics of charity has been well studied on the "supply" side, critical gaps remain on the "demand" side (James Andreoni, 2006).

In an effort to better understand the economics of charity; several studies have been made which use a direct mail solicitation to explore whether, and to what extent, "price" matters in charitable fundraising. There is a rich and interesting literature that examines price effects via rebate

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[3] Income inequality gets worse; India's top 1% bag 73% of the country's wealth, says Oxfam, (BusinessToday.in)
[4] India's rising inequality is taking the shine off it growth story even in the worlds eyes – Riaz Hassan *(Scroll.in)*

mechanisms (such as changes in tax deductions) through which charitable contributions can be used to reduce one's tax burden.

Overall, it is fair to say that the four decades of empirical estimates of these supply-side effects vary widely, and it is difficult to make strong inference from the various price effect estimates obtained (Gerald Auten et al., 2002). Laboratory experiments, on the other hand, typically find that the level of giving to others increases as price decreases (Andreoni and John Miller 2002)."[5]

"Supporters of tax expenditures point out that it is efficient to encourage certain kinds of economic behaviors instead of using direct expenditures to achieve similar objectives. They argue that tax expenditures such as charitable giving have positive external effects and are very responsive to tax incentives. Therefore, the government should promote these types of activities by providing a tax break. A common argument is that if the elasticity of charitable contributions with respect to its tax price if higher than one, allowing the deduction of these expenditures from taxable income generates more contributions than what is lost in tax revenue because of the subsidy. This narrow "efficiency" concept is often mentioned to argue in favor of the use of tax expenditures by empirical studies that find large elasticities.

Opponents emphasize that the external effect of such tax expenditures is too small to justify a complete tax exemption. Moreover, as tax expenditures are likely to be much more responsive to taxation than labor supply, they point out that allowing tax expenditures may both reduce the size of the tax base and increase significantly the elasticity of taxable income, thus increasing significantly the total deadweight burden from the income tax."[6]

"However, the Charities Aid Foundation has found that the amount people donate to charity is not affected by whether they live in a high-tax or low-tax country. The foundation analysed tax returns and statistics from 24 countries representing 75 per cent of world gross domestic product, found no correlation between tax levels or government spending and donations.

A good example is the Netherlands, which is a fairly high-taxation country, as is Italy, and they both outperform countries that are low-tax, such as China and Mexico .Other factors, including religion and the state of the individual countries' charitable sectors, clearly influenced levels of giving. The UK leads Europe in individual giving as a percentage of GDP but at 0.54 % ranks fourth behind the US at 1.44 %, New Zealand at 0.79 % and Canada 0.77 %.

While the tax rates that people face may not be correlated with charitable giving however specific incentives in the tax system for donations did have an effect. A 2014 report from the foundation

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[5] How does charitable giving respond to incentives and income? New estimates from panel data – Jon Bakija and Bradley T. Heim *(National tax Journal, June 2011, 64 (2, Part 2), 615-650*

[6] The optimal treatment of Tax Expenditures – Emmanuel Saez (Working Paper 8037, NBER Working Paper Series)

in association with Nexus, a global youth movement, and McDermott Will & Emery, a law firm, noted that countries with higher levels of tax relief saw correspondingly high levels of donations. For philanthropists themselves, tax is often a benefit, but not the main reason for giving."[7]

2.2 Rationale for Tax Concessions and Role of NPOs

"The major effect of tax concessions for charitable contributions is through the tax-price. The tax-price is defined as unity for those who do not itemize deductions from income when calculating taxes and one minus the marginal tax rate for those who itemize their deductions. An increase in marginal tax rates lowers the "price" of giving and therefore may increase contributions. How much they increase will depend upon the price elasticity of giving, defined as the percent change in contributions caused by a one percent change in the price. If this elasticity is greater than unity then allowing a tax deduction for contributions is "efficient" in the sense that less is lost to the exchequer than is gained by charities through increased contributions. Moreover, tax concessions for charitable contributions have "equity" implications, depending upon the magnitude of price and income elasticity of donations across income groups. Empirical analysis reveals that tax concessions for charity have been efficient. However, price elasticities are higher in higher income groups implying serious equity implications.

2.2.1 Two main characteristics of NPOs are as follows:

1. Public benefit purpose: The first characteristic is that the organisation operates primarily for some purpose other than private gain. The emphasis here is not on avoiding the generation of profit (in the sense of an excess of revenues from all sources over expenses of all types), but rather on the existence of a substantial public benefit purpose. This is often referred to as the "principal purpose" test.

2. Non-distribution of surplus: It is barred from distributing its net earnings, if any, to individuals who exercise control over it, such as members, officers, directors, or trustees. This characteristic is popularly referred to in the literature as the "non-distribution constraint".

The proliferation of NPOs in certain areas of activity and not in others can be explained by numerous factors. Some important factors are described below.

- Response to government failure (Public Goods argument): In a democracy, which makes choices by voting, a significant proportion of the population believes that the level of public services is too low. As a consequence, some of the dissatisfied people make charitable contributions to private organisations willing to produce incremental units of the collective

[7] Tax link to charity giving ruled out – Hugo Greenhalgh, Wealth Correspondent (Financial Times)

goods or services. In effect, the NPOs are mainly conduits that efficiently convert donations into services demanded by donors.

- Response to contract failure: Subject to certain conditions, profit-seeking firms will supply goods and services at the quantity and price that represent maximum social efficiency. Among the most important of these conditions is that consumers can, without undue cost or effort,

  (a). Make a reasonably accurate comparison of the products and prices of different firms before any purchase is made,
  (b). Reach a clear agreement with the chosen firm concerning the goods or services that the firm is to provide and the price to be paid, and
  (c). Determine subsequently whether the firm complied with the resulting agreement and obtain redress if it did not. In many cases these requirements are reasonably well satisfied.

However, either because of the circumstances under which the product is purchased and consumed or due to the nature of the product itself, consumers may be incapable of accurately evaluating the goods promised or delivered. As a result, they will find it difficult to locate the best bargain in the first place or to enforce their bargain once made. In such circumstances, market competition may well provide insufficient discipline for a profit-seeking producer; the producer will have the capacity to charge excessive prices for inferior goods. As a consequence, consumer welfare will suffer considerably. NPOs are granted exemption because they have no income/profit in the sense in which that term is used in tax laws. It is argued that any effort to use ordinary tax accounting to define taxable income for an NPO leads to complications. The concept of taxable income developed for business organisations simply cannot be carried over to NPOs in any meaningful way. However, these difficulties are often overstated.

To begin with, many NPOs derive all or nearly all of their income from sale of goods or services that they produce. For such organisations it would be possible to use the same tax accounting that is applied to business firms, i.e. taking receipts from sales as the measure of gross income and permitting the usual deductions for expenses incurred in producing the goods or services sold. The resulting net earnings figure could be taxed just as in the case of a business firm. Another argument against taxing the income of NPOs is that, in the long run, NPOs will necessarily have no net profits, since, by virtue of the non-distribution constraint, they must ultimately spend all of their income for the purposes for which they were formed, and hence their total expenses must ultimately equal their total income. The strength of this argument depends on several factors, including the detailed accounting conventions employed.

Tax exemption serves to compensate NPOs for the difficulties that they have in raising capital, and such a capital subsidy can promote efficiency when employed in those industries in which non-profit firms serve consumers better than their for-profit counterparts. This is an efficiency rationale for exemption. NPOs lack access to equity capital since, by virtue of the non-distribution constraint; they cannot issue ownership shares that give their holders a simultaneous right to participate in both net earnings and control. Consequently, in raising capital, NPOs are limited to three sources: debt, donations, and retained earnings. These three sources may, in many cases, prove inadequate to provide an NPO with all of the capital that it needs.

It is argued that if tax exemption is to be administered, three conditions should be satisfied before exemption is granted to an NPO in a given industry:

1. Non-profit firms in the industry must not have expanded to the point at which the productivity of the capital they employ is lower than the before-tax rate of return being earned on capital in other industries. This is known as the technical efficiency criteria.

2. From the consumers' viewpoint, non-profit firms must be more efficient producers of the service than the firms motivated by profits because of contract failure. This is known as the economic efficiency criteria; and

3. The non-profit firm should be able to generate investible funds through internal sources.

As a practical matter, it is not feasible to condition tax exemption for NPOs on the basis of the tax administration's judgment as to whether capital investment among non-profit firms in particular industries has exceeded the efficient level. Such a criterion would be extremely difficult to administer. Consequently, the best that can be done in this area is to focus primarily on the last two criteria."[8][9]

3. Measuring the Tax Cost of Charitable Contributions

3.1 Tax price and the Global Outlook

The idea that the state should subsidise giving to good causes is resilient, but not easily justified,

> "*It must be borne in mind that in every case exemption means a relief to A at the charge of B. It is not fair, on the fathers of families, men labouring to support their wives and children." - Britain's Chancellor of the Exchequer told the House of Commons in his budget speech,*

[8] This note draws heavily on the report An Analysis of Tax Concessions for Charitable Contributions and Trusts/Institutions (NIPFP, October 2000) prepared by Arbind Modi and Hiranya Mukhopadhyay.

[9] Report of the Advisory Group on - Tax Policy And Tax Administration For The Tenth Plan

This was, indeed, the heart of his case for taking away a tax break that benefited charities. This was all the more important because the gifts encouraged by the exemption were largely designed to bring a wealthy donor "credit and notoriety" which "otherwise he might not have enjoyed.

In Europe, some countries in which generous state provision of services has been the norm, such as Sweden, have recently begun to experiment with tax incentives to boost the charitable sector. But this change, and established tax incentives elsewhere, may be under threat. In France there has been discussion of confining tax breaks, which can be quite generous, to charities that spend the money they receive inside the country.

In hard times, it is not surprising that exchequers take are cautious to confine tax breaks. In Britain, the Treasury had estimated the total cost to the state of the various tax breaks to donors and charities will be £3.64 billion ($5.5 billion) in the tax year 2012; in America, the Treasury had estimated that the total cost to the federal government in 2012 of charitable tax breaks will be $39.6 billion, rising to $51.6 billion in 2014.

There was little debate over exempting charities from income tax when it was first introduced in Britain, supposedly as a temporary measure to finance war with France, in 1798. This seemed fitting, as charities had already been largely exempt from earlier taxes on property since the Elizabethan age. Likewise, there was little opposition in America when in 1917, four years after the federal government gained the constitutional right to levy an income tax, American taxpayers were allowed to deduct charitable donations from their taxable income (again, extending precedent established in the 19th century).

President Barack Obama has made a number of attempts to limit the amount of giving that the rich can deduct from their taxable income, still US has the most generous tax incentives for charity, and has the highest giving as a proportion of GDP, at 1.67 %, according to a rare comparative study by Britain's Charities Aid Foundation. Britain's tax breaks for charity are the next-most-generous, and it had the second-highest share of charity to GDP, 0.73 %, followed by Australia, at 0.69 %, which also has significant tax breaks. By contrast, the relatively weakly incentivised Germans give only 0.22 % of GDP. The correlation is not perfect, though; despite their generous tax breaks, the French give just 0.14 % of GDP.

Within countries one can look at changes in the "tax price" — the cost of a donation to the donor— for an indication of the effects of tax policies. If a taxpayer faces a marginal tax rate of, say, 28 %, an extra dollar given to charity reduces the tax bill by 28 cents: the tax price is thus 72 cents. For a higher-rate taxpayer, say one paying a marginal tax rate of 50 %, the tax price falls to 50 cents.

At first glance it would appear that the tax price is irrelevant. Dropping marginal tax rates on the wealthy in US has meant that the tax-price of donation there has soared over the past decades.

But the rate of charitable giving, too, has increased. This seems to be because wealth matters too. As America's rich have become much wealthier, they have given more to charity even though the cost of doing so has risen. Surveys suggest that tax rules affect the size and timing of gifts, but not the initial decision to give, which depends largely on being moved by the cause or being asked directly to support it.

The idea that growing wealth offsets high tax prices fits with evidence from a biannual survey of charitable donors by Bank of America and the Center on Philanthropy at Indiana University. In the 2007 survey 7 % of high-net-worth families said they would "dramatically decrease" their giving, and a further 39.6 % would "somewhat decrease" their giving, if changes in rules on exemption put up the tax price of their donations.

Feeling less flush after the financial crisis, in 2009 the numbers had risen to 18.7 % and 48.3 %. Economists have been trying to work out how, other things being equal, changes in the tax price will affect behaviour. In the 1970s, early econometric studies by Martin Feldstein of Harvard, among others, suggested that the "tax-price elasticity" was more than one—that is, if the tax price were cut by 10 %, giving would increase by more than 10 %. If you assume that the public benefits more or less equally from charitable spending and taxable spending, that sounds like a good deal.

However, as these studies have become more sophisticated, the consensus estimate of the tax-price elasticity has diminished to significantly less than one. This shift matters: at less than one, an additional dollar in incentives for giving generates less than a dollar's worth of donation. In such a situation charities need to produce more bang for the buck than state spending to justify their perks.

That said, the elasticity need not be stable from country to country, or the same for all types of donor. Sarah Smith of the University of Bristol and Kimberley Scharf of Warwick University recently carried out a series of experiments for the Treasury to gauge how sensitive higher-rate taxpayers are to changes in tax incentives. She found that for donors who had previously made relatively large gifts of between £25,000 and £50,000, the tax-price elasticity was 1.19, well up into the-everyone-wins realm. But for higher-rate taxpayers as a whole the elasticity was just 0.33.

Especially if elasticity is low, policymakers should be seeking assurance that charities spend money in a particularly wise, effective way. There is a growing effort around the world to develop better performance measures for charities that might help. But it has a long way to go before it can provide answers to whether the tax breaks for charity pay. A more practical measure is that many governments use charities as contractors to provide various social services, paying them to help the homeless, care for the elderly and so on. Around a third of the money going to charities in America and more than half the money they get in Britain are in the form of direct payment from government for services. That governments are choosing to do this more and more suggests they think these services represent value for money. That said, there is a risk that subsidised charitable service-providers may be squeezing out innovative for-profit alternatives.

Cost alone may not be the whole story. One of the arguments for subsidising charities through the tax system is that bringing in donors adds something to the mix. Spending decisions by government are often bureaucratic and risk-averse, not to mention captured by the vested interests of public-sector unions and the lobbying process. Proponents say the charitable tax deduction opens up new avenues, paying for itself by providing a pluralism that would otherwise be unavailable.

3.2 Importance of tax policy for charitable giving

"There is enough evidence that suggests that people and corporations are responsive to incentives. The presence of incentives has been shown to positively influence the frequency of donations by individuals with people in countries with tax incentives. Both experimental data and analysis from historical records in the United States show that when the marginal cost of giving falls (i.e. the value of incentives increases) people tend to increase the size of their donations.

However justifying incentives for giving on the basis that they can expand the provision of services that might otherwise be provided by government misunderstands the value of giving and could lead to negative unintended consequences for civil society. Though incentives can be articulated as a tax expenditure the idea that incentives for giving are merely an alternative funding mechanism for state services mischaracterises the strengths and weaknesses of civil society which cannot be understood as a proxy for government service provision.

Tax incentives are not the most important policy lever in motivating charity. Factors such as the legal environment in which civil society operates, the range of causes which are incentivised, administrative barriers to charity and the ability of organisations to fundraise publically are likely to be more important in motivating giving than tax incentives alone.

The politicisation of tax incentives whereby legitimate causes which do not align with the government's agenda are ineligible for or receive less favourable donor incentivised status, is damaging to the independence of civil society.

A number of countries offer tax incentives exclusively, or at a favourable rate to organisations which are delivering government projects, are affiliated to government or are wholly government controlled. This undermines the very independence of a society that allows it to build trust with the public.

Higher tax nations offer more compelling incentives (assuming that deductions or credits are equal to the rate of taxation). There is evidence that as the rate of income tax increases (assuming incentives rules stay the same) people are likely to give more as the marginal cost of giving decreases. This is particularly true for those in the highest income categories. Behavioural sciences may provide the most cost effective solutions to motivating greater giving.

The effectiveness of tax incentive regimes in many countries is undermined by the difficulty that many donors face in claiming them. Complex procedures for claiming, a lack of guidance, the requirement to fill in detailed tax returns, regional variations and complex systems whereby causes receive differing tax treatments can harm donor responsiveness.

Tax deductions are the preferred method of incentive globally. A number of countries offer incentives in the form of tax deductions. The deductive approach has several perceived advantages including simplicity from the point of view of the tax authorities and a natural weighting towards higher income audiences where a higher responsiveness is assumed. However, this assumption does not necessarily stand up to scrutiny and in any case may lead to a system that lacks progressiveness.

Most countries weigh pragmatism above concerns about progressiveness in designing their incentive regime. A pragmatic approach to a policy which favours efficiency and perceived responsiveness in wealthy individuals and corporations has led to inequality in both the value of incentives and the ability to claim them which might have a chilling effect on mass engagement in giving. A system where those with the greatest ability to afford to donate receive the greatest incentives to do so may lead to a civil society that rather than representing those interests which are crowded out by the powerful in society, actively reinforces the existing socio-economic structure.

Tax credits are the most progressive model for incentivising giving. Offered at a flat rate at the highest level of income tax, tax credits ensure those with the lowest incomes do not endure the highest marginal cost when donating.

Hybrid systems – which mix deductive and credit based incentives – introduce unnecessary complexity. This complexity makes them more difficult for donors to comprehend and more expensive to administer. This undermines the benefits of both a deductive system – which benefits from simplicity and pragmatism, and a credit system – which should be progressive and accessible.

Corporations see, on average, more favourable tax conditions for giving than individuals. Globally, according to the Rules to Give By Index, 77 % of the nations offer some form of incentive to corporate donors whilst 66 % of the nations offer some form of tax incentive to individuals. This study finds that the terms of those incentives tend to be – though not exclusively – more favourable for companies too. There are a number of possible explanations for this, ranging from a perception of greater responsiveness, belief by government officials that companies are more likely to support government aligned causes or simply the desire to attract business through a favourable tax environment. However, such sectoral favouritism may actually undermine corporate giving, as the public may come to view more favourable conditions for companies than they themselves enjoy with suspicion and thus the reputational effect of corporate giving may actually become negative.

Cross border giving is poorly incentivised. Tax incentives for cross border giving to foreign civil society organisations are rare and even where they exist on paper they are often difficult or impossible to claim in practice. In many transitional economies donors are not allowed to claim incentives even for domestically registered organisations that operate abroad."[10]

4. Philanthropy - The International Experience

4.1 United States

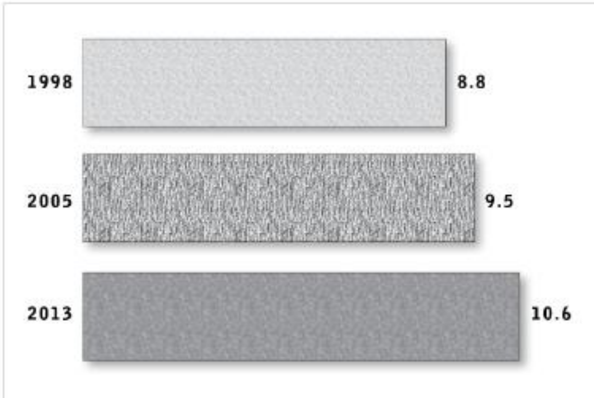
The U.S. has a strong, long-standing tradition of philanthropy, consistently ranking first worldwide in terms of dollars given. "Charitable giving hit a record high for the third straight year in 2016, reaching $390.1 billion, according to "Giving USA," an annual study that estimates American philanthropy."[11]

The section governing charitable contributions deduction is one of the oldest in the tax code, passed in 1917. The tax benefits for philanthropy have survived this long because of the perception that subsidizing incentivizes more giving than the amount spent to achieve it. However, at a time when government budget cuts, fiscal cliffs, sequesters, furloughs, and general austerity have made the need for charitable social services even more dire, the charitable contributions deduction has come under increasing pressure. The sheer size of the charitable tax deduction, which costs the federal government over $40 billion a year, makes it a tempting target.

Non-profits have grown faster than government and faster than the business sector over the last generation, even during boom periods. The figures charted here actually underestimate the fraction of American manpower that goes into charitable work—because they show only paid employment, while volunteers carry out a large share of the labor poured into these groups.

[10] DONATION STATES – An international comparison of the tax treatment of donations May 2016 – Charities Aid Foundation
[11] Donations Grew 1.4 % to $390 Billion in 2016, Says "Giving USA" By Timothy Sandoval

% of U.S. Workforce Employed in Nonprofit Sector



“A charity must be registered with the Internal Revenue Service (IRS) to be eligible for deductions on contributions, and charitable donations to qualify for non-profit groups are tax-deductible if one itemizes the return instead of taking the standard deduction.

As per the current laws the donor can deduct up to 50 %of the adjusted gross income in charitable contributions, but deductions can be limited to 30 %of the income in some cases.”[12]

“But according to ‘Rethinking’ the Deduction for Charitable Contributions, evidences that the tax deduction encourages people to be more charitable is inconclusive: A number of more recent studies, however, that use arguably better data than earlier research have resulted in estimates of the charitable contributions price elasticity that are both statistically and quantitatively less than unity. These lower estimates of the price sensitivity of giving have caused some to question the efficiency of the charitable deduction, [since new numbers imply] that a portion of the revenue foregone as a result of the deduction does not stimulate more charitable giving.

There is another element of the charitable deduction many find problematic: it consistently favors the wealthy, making it “cheaper” to give if you have more money than less. For example, if your marginal tax rate is 25%, then every dollar you donate to charity only costs you 75 cents thanks to the tax break the IRS offers. However, if your marginal tax rate is 39.6%, then each dollar you donate now costs only 60.4 cents. As Joseph J. Cordes notes in “It’s Time to Rethink the Charity Deduction,” if we want to “reward” individuals who give to charity, why should such rewards “be distributed disproportionately with respect to the income of the giver?”

Interestingly, The Chronicle of Philanthropy found that the wealthy were actually significantly less generous than those less fortunate even though they benefit the most from the deduction.

[12] The tax advantages of charitable giving – Jessica Dickler (CNBC)

According to a study by the Chronicle of Philanthropy, the median American household gives approximately 4.7 % of their discretionary income to charity. This ranges quite significantly by state (as high as 10.6 % in Utah to a low of 2.5 % in New Hampshire), metropolitan area, and income level.

The non-profit community has been up in arms fearing a decline in giving if this deduction is reduced or abolished. We may think giving to charity is driven by altruism, but much charitable giving may be compelled instead by generous tax incentives. United Way Worldwide reported that 62 % of respondents from their Charitable Tax Deduction Poll would reduce their giving by a significant amount (25 % or more) if the deduction was scaled back or eliminated.

At the heart of the issue is also a debate about the role of government versus philanthropy—which is better at delivering critical social services? In the Chronicle of Philanthropy's analysis, "blue" states (Republican States) generally contribute more taxes to fund generous government social programs and tend to give less to charity. But blue states have better health and social outcomes than red states, which must rely more on private donations to fund social programs. Over a third of charitable giving in the U.S. goes to religious institutions, and groups such as the National Rifle Association receive the same tax treatment as donations to feed the poor."[13]

4.2 United Kingdom

"Charitable Trust is a significant area of law in the United Kingdom, as charitable Trusts enjoy some advantages over other Trusts. For tax relief charity must be recognised by HM Revenue and Customs (HMRC). Above all, UK charities do not pay income tax on their investment income devoted solely to charitable purposes under section 505 of the Taxes Act 1988.

Charities may claim exemption from tax on most forms of income and capital gains, if they're applied to charitable purposes. Charitable Trusts do not pay capital gains tax on the disposal of assets provided they are devoted to charitable purposes only, under section 256 of the Taxation of Chargeable Gains Act 1992. However, charities are required to pay Value Added Tax on goods and services purchased. Tax breaks relating to philanthropy in the UK are discussed below:

- **<u>Gift Aid</u>**

The premise underlying gift aid (ITA 2007, Part 8 Ch 2) and its predecessors is that charities registered with HMRC can reclaim tax <u>on a donation made by a UK taxpayer</u>.

This, in effect, increases the value of the donation, while allowing the taxpayer to obtain UK income tax relief.

[13] Philanthropy selfless or tax-incentivized – Hui Wen Chan *(Hipporeads)*

By making the declaration, the amount donated is treated as being made net of basic rate income tax. The charity can then claim back the corresponding income tax credit attached to the donation from HMRC, increasing the total value of the donation received.

- **Additional relief for donors**

Donors who pay income tax at the higher or additional rates may claim further relief for their gift aid donations on their self-assessment return each year.

The basic rate band is extended by the gross value of donations made during the year, thereby increasing the amount of income taxable at the basic rate, resulting in relief at the donor's marginal rate. Donations made under gift aid may also be carried back to the previous year, as long as this is done no later than the date at which the tax return for that year is submitted.

As an alternative to the gift aid scheme, payroll giving – or "give as you earn" – is a simple way of donating through salary or pension

In the case of higher or additional rate taxpayers, this allows the full relief to be received during the tax year rather than waiting until the return has been prepared and submitted or by adjustments to PAYE codes.

- **Gifts of assets**

An under-utilised charitable tax relief applies when certain assets rather than cash are given. This relief (ITA 2007, part 8 ch 3) can apply in respect of:

- a qualifying interest in land or buildings; and
- Shares and securities (generally where listed on UK or recognised overseas exchanges, including AIM-listed companies).

The relief applies when assets are gifted to charity or sold to the charity at less than their current market value. The value of the asset is deducted from the individual's total taxable income for the year and can reduce their income tax liability to nil.

Finally, any assets gifted are treated as having been disposed of on a no gain/no loss basis for capital gains tax purposes. This relief can therefore be much more generous than gifting cash, and individuals should review their asset base when considering making significant lifetime gifts.

- **Cultural gifts scheme**

The cultural gifts scheme (FA 2012, Sch 14) has existed since April 2012 and is intended to encourage the lifetime giving of pre-eminent objects, other than buildings or land, to public collections in return for a tax reduction.

Assets are initially assessed by a panel to determine whether they qualify as pre-eminent. If so, the subsequent gifting of such assets will entitle the owner to a reduction in their income tax or capital gains tax liability for the tax year of the gift (and up to four subsequent tax years) of 30 % of the value of the asset. The panel also decides to which national institution the asset should be gifted, although the donor may express their own preference. Any gain arising on the gift of the asset will not attract capital gains tax.

- **Inheritance tax relief**

The relevant UK laws provide for a reduction in the rate of inheritance tax from 40 % to 36 % where at least 10 % of the net value of the estate is given to charity.

- **Tax relief for companies**

Corporation tax relief is available for donations to charities and, since 1 April 2014, relief is obtained by deducting the qualifying donation from total profits when calculating the company's corporation tax liability.

Recently published figures suggest that the wealthiest UK individuals are donating more money to charity than ever before, with more than £1bn last year being in the form of individual donations in excess of £1m each. It is strongly hoped that the existing provisions continue to grow in robustness, application and, not least, used by the public."[14]

5. Cross Border Philanthropy

5.1 Introduction

"In many ways, the study of the tax treatment of cross border giving offers the best glimpse into how tax incentive regimes are, or were in the past justified politically. It is perhaps the most extreme basis on which a conversation can be had about the extent to which governments should balance the moral imperative of the citizenry and commitments to pluralism in civil society against the natural desire of policy makers to ensure that they are incentivising in line with the domestic public interest.

[14] Charity begins at home By Edward Emblem *(Taxation.co.uk)*

Most policy makers have a natural desire to control the impact of offering tax benefits for charitable gifts; in order to ensure to ensure that the primary benefits are felt domestically. The extent to which this desire can be tempered in order to allow incentivised cross-border giving depends on a range of factors.

5.2 Arguments for and against incentives for cross-border giving

Accordingly, it will likely be argued that lost tax revenue will not be mitigated by an equitable or greater benefit to the nation. This was indeed the case in the United States when lawmakers decided to extend the geographical limitation on deductibility to individual donors in the 1938 Revenue Act. In relation to the earlier 1935 Revenue Act which placed geographical restrictions on corporate deductibility, the House of Representatives Ways and Means Committee stated in its report that:

> *"The exemption from taxation of money or property devoted to charitable and other purposes is based upon the theory that the Government is compensated for the loss of revenue by its relief from financial burden which would otherwise have to be met by appropriation from public funds, and by the benefits resulting from the promotion of the general welfare. The United States derives no such benefit from foreign institutions, and the proposed limitation is consistent with the above theory."*

Clearly, this is an argument that is likely to have some traction with any government that imposes taxes. Also no country has a truly open policy that offers tax incentives on the same basis to foreign organisations of any country as it does to domestic organisations.

Despite this, it is noteworthy that many countries do allow, to differing extents, some means of donating for the benefit of beneficiaries abroad, whilst claiming tax incentives on their donation. As we will discuss, these options range from narrow and specific domestic vehicles that are affiliated to the government, to tax treaties and regional agreements which allow incentives to be claimed on direct donations to foreign organisations. Given that tax authorities would ordinarily see this as a straightforward tax loss, we might reasonably ask how this can be justified.

One potential explanation is the desire to extend a nation's "soft power" through cultural and economic influence. Many in government have long understood that military power has its limitations and that "persuasion through soft power can yield more concession, cooperation, and enduring support than coercion alone."

The unique nature of philanthropy is recognised as having particular relevance in this realm. Being a product of society, rather than government bestows a sense of cultural freedom and unshackled human endeavour which often results in a less cynical response abroad, and hence enables philanthropy and the organisations it supports to be more effective. Paradoxically, allowing independent altruism to leach through national borders has the effect of enhancing the national reputation and hence soft power.

Put differently, "international philanthropy—precisely because of its independence from the state— offers a direct, tangible, and genuine manifestation of culture, values, and people through action on the ground. This production of attractive cultural values, in turn, produces benefit—in the form of soft power—that inures to the state writ large." Indeed, while some policy makers have worried that large donors such as the Bill & Melinda Gates Foundation and the Ford Foundation essentially have a foreign policy profile in and of themselves and thus retain soft power rather than passing it on to the state, these are extreme outliers. Even if we limit ourselves to talking about foundations, the collective efforts of all but the largest organisations "are more likely to create cumulative soft power to the government rather than for those organisations individually."

The scale of resources necessary to address the continuing human suffering and inequity that persist around the world is difficult to overstate. The United Nations Conference on Trade and Development has estimated that the world will have to overcome a US$2.5 trillion investment shortfall to deliver on the Sustainable Development Goals.

For philanthropy to play a significant role as a partner in delivering these goals, it must seek to be as effective as possible. However, many thinkers in the development sector believe large international NGOs (INGOs) have, often by virtue of being headquartered in wealthy nations, become far too dominant as deliverers of development initiatives at the expense of local/national organisations with ties to the community and an understanding of the context. This is exacerbated by official aid flow from governments. The OECD estimated in 2013 that only about 1 per cent of Official Development Assistance (ODA) from Development Assistance Committee (DAC) member countries goes to Civil Society Organizations registered in the destination country.

Policy makers are, in spite of globalisation, as likely as ever to see the world through the lens of national interest. A narrow reading of the realpolitik foreign policy might well lead one to assume that a policy of limiting incentives for giving to organisations and activities which benefit people and communities within the national border is inevitable. However, a broader reading explains the variety of practice that we see in our study. Firstly, as stated above, there are legitimate reasons to allow donations to be incentivised for domestic organisations operating, and even grant making, abroad that are in line with considerations of the national interest. Secondly, extending cultural and economic "soft power" through philanthropy can help to advance national interest. Furthermore, it could be argued that meeting multilateral commitments and investing in the security and development of other nations can have both preventative and causal benefits at home.

However, we should also note the primacy of public demand in advanced democratic societies. Citizens are increasingly connected to networks outside of their country through social media and global news coverage and their strong desire to help others can weigh heavily on the hand of politicians as they pull policy leavers."[15]

6. Abuse of Charitable Institutions for Tax Evasion, Money-Laundering and Terror Financing

"Tax evasion and tax fraud through the abuse of charities is a serious and increasing risk in many countries although its impact is variable. Some countries estimate that the abuse of charities costs their treasury many hundreds of millions of dollars and is becoming more prevalent.

While the studies are limited, some countries like Canada report that the abuse of charities is costing their treasury millions of dollars in terms of misappropriated tax relief such as the overpayment of refund claims or fraudulent claims. In other countries, similar abuses are reported with serious consequences on tax revenues and the integrity of the charitable sector.

6.1 Schemes involving abuse of Charitable Institutions to facilitate Tax Evasion, Crime And Money Laundering

There is evidence to suggest that the abuse of charities for tax evasion and money-laundering purposes is organised in many cases, and is not only individualistic, particularly when it involves unscrupulous tax return preparers. Once the tax crime is perpetrated, money-laundering techniques are used to hide the proceeds of the tax crime. There is also evidence that electronic tax filing methods, used increasingly by tax administrations to speed up the processing of tax returns and better serve taxpayers, provide significant challenges for tax authorities to quickly detect and deter the abuses of charities. The level of sophistication also increases the difficulty of detection of this type of crime and the apprehension of the offenders.

Tax authorities have detected several methods and schemes involving the abuse of charities to facilitate tax evasion, crime and money laundering. The most commonly detected methods and schemes are listed below:

a. An organization poses as a registered charitable organization to perpetrate a tax fraud;
b. A registered charity willfully participates in a tax evasion scheme for the personal benefit of its organisers or directors;

[15] DONATION STATES – An international comparison of the tax treatment of donations May 2016 – Charities Aid Foundation

c. A registered charity is involved willfully in a tax evasion scheme to benefit the organization and the donors, without the assistance of an intermediary;
d. A registered charity is involved willfully in a tax evasion scheme to benefit the organization and donors with the assistance of an intermediary;
e. A charity is abused unknowingly by a taxpayer or a third party, such as unscrupulous tax return preparer who prepared and presented false charitable receipts;
f. Tax sheltered donations as part of a tax evasion scheme;
g. Salaried employees concealed as volunteer workers;
h. An organization registered as exempted from the VAT that is performing taxed activities;
i. The issuance of receipts for payments that are not true donations;
j. The issuance of receipts to individuals working for the beneficiary organization;
k. Criminals use names of legitimate organizations to collect money;
l. Terrorism financing scheme using charities to raise or transfer funds to support terrorist organizations;
m. Misuse of charity funds by charities; and
n. Manipulation of the values of donated assets.

6.2 Quantifying the risks associated with the abuse of charities

Few countries have yet attempted to quantify the economic cost and/or the level of tax evasion and money laundering associated with the abuse of charities. Most countries do not have a mechanism to capture the overall economic cost associated with the abuse of charities. In the countries that have made such estimations, the amounts are significant.

<u>Examples of economic cost and/or level of tax evasion and money laundering associated with the abuse of charities:</u>

- In Canada, just in terms of revenue losses, for the current cases under criminal investigations, such abuse represents an amount of $200 million (€125 million) in tax revenue at risk.

- Spain has detected €40 million in offshore accounts. In tax revenue, the loss is approximately €15 million.

- UK cannot accurately quantify the total economic cost but the schemes relating to direct tax that they have found and challenged have been in the £tens of millions. In the case of indirect taxes the tax at stake is of the same order. There has been some negative publicity but the integrity of the charity sector has not yet been seriously damaged.

- The US cannot quantify the economic cost; however, based upon their related investigations, there are consequences on tax revenues and on the overall integrity of the charitable sector.

6.3 Detection strategies and techniques employed in suspected cases of tax evasion and money laundering involving the abuse of charities

Some countries use a combination of intelligence gathering, risk analysis, risk profiling and data matching to detect cases of tax fraud and/or money laundering in the abuse of charities. Several countries report that data matching and other information sharing activities between tax authorities and other government agencies are carried out to detect and investigate suspected cases of tax evasion and/or money laundering involving the abuse of charities.

Detection strategies and techniques:

Belgium: Generally speaking, these abuse cases are detected during an in-depth audit of an organization's bookkeeping, performed during a registration application or registration renewal application. If an organization has already been certified in the past, the competent tax department also verifies if it has followed the directives with respect to tax receipt preparation and issuance. Abuse cases may also be detected by the tax departments when verifying the donors‘ tax status. The tax authority may also be aware of abuse cases when, after opening a legal investigation, it receives authorization to consult legal records.

Canada: There is no matching system for charity donations; however, the Canada Revenue Agency (CRA) has identified several key characteristics which facilitate the detection of possible abuse of charities. The CRA‘s risk assessment systems use primarily information from internal sources.

Czech Republic: Cases of tax evasion involving charities are detected through the conventional means.

Italy: In order to detect charities tax abuses, the same tools are generally used as for the other economic agents. Regarding ONLUS, the Special Unit for Tax Revenue has in place risk criteria for tax purposes which are related to the recurrence of tax abuses or crimes or to the failure to submit a tax return.

Portugal: The control of income tax deductions/tax credit, due to donations made to NPO‘s, includes data matching. This data matching process is made using information from tax returns/declarations submitted by donors and by beneficiaries NPO‘s: 1. - Those who make donations and obtain tax deduction/tax credit must identify the amounts as well as beneficiaries of donations. 2. - The beneficiaries of those donations (NPO's) must identify the donors as well as the amounts.

UK: HMRC Charities tax team issues and reviews charity tax returns and accounts. The repayment audit team identifies most of the abuse by charities by identifying patterns and unusual items. Abuse of the donor relief is discovered by local compliance officers who deal with the donor's tax return and has also been identified, in the case of large donations, by the repayment team in HMRC Charities. HMRC also has a tax avoidance scheme declaration process.

Most of the countries surveyed use multiple sources of information, available within and external to their tax authority, to detect and investigate possible cases of tax evasion and/or money laundering involving the abuse of charities. Effective information sharing between tax authorities, other domestic agencies and law enforcement authorities is also crucial to detecting and investigating such cases."[16]

6.4 Indian NGOs and the risk of money -laundering

"Voluntary organizations in India receive more than Rs 11,500 crore ($1.9 billion) in foreign funds annually, the Home Ministry has indicated that the NGOs could be vulnerable to risks of money laundering and terror financing. A total of 43,527 NGOs are registered under the Foreign Contribution (Regulation) Act, as of March 31, 2012.

Indian NGOs are targeted for laundering the money because of several reasons, though one of the most significant reasons is the Income tax benefit that is available for doing the charitable activities. Many of the Indian NGOs are also registered under the Public Trust Act, though there are possibilities to get registered under the Companies Act as well as Societies Act. A Trust can be registered in one state, but the same has the scope to operate in any number of states. In the state of Maharashtra and Gujarat, all organizations that are registered as 'Society' are by default also registered as Public Trust. Some of the other reasons that Indian NGOs are targeted for money laundering are:

- NGOs in India enjoy high levels of public confidence because of their work in the areas like relief of the poor, education, medical relief and the advancement of any other object of general public utility

[16] Report on Abuse of Charities for Money-laundering and Tax Evasion – OECD

- NGOs in India often have complex financial operations including multiple donors, investments and currencies, often receiving and using cash, having to account for high volume of small transactions and using informal money transfers

- Some NGOs may work within or near those areas that are most exposed to terrorist activity or the money laundering activity

- NGOs may have unpredictable and unusual income and expenditure streams, so suspicious transactions may be harder to identify."[17]

6.5 Corporate Philanthropy – Abuse of CSR

Annual spending on CSR:

Every financial year, at least 2% of the average net profits made during the three preceding financial years. Schedule VII of the Act indicates activities that may be included by a company in their CSR policies. Under the Income-tax Act 1961, Explanation to Section 37 provides that no expenditure on account of CSR shall be allowed. CSR if approached as a 'tick-in-the-box' process, may expose an organization to a variety of fraud risks (some of which are elaborated below), all arising from ineffective due diligence and poor monitoring.

- Conflict of interest
- Advertising/Marketing fraud
- Related or fraudulent entities/charitable Trusts
- Bribery/ Corruption
- Inflated projects
- Fictitious projects
- Financial Frauds

[17] Money laundering Through Indian NGOs – By Mayur Joshi *(Indiaforensic.com)*

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