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Research Insights

Can tweaking tax treatment of donations support disaster relief?

The rising incidence of natural disasters in Australia prompts a rethink on how the tax treatment of donations can incentivise greater giving and increase support for communities in crisis.

Meaningful insight backed by high-quality academic research

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Timing is everything

Donations made to Australian charities of $2 or more can be claimed as a tax deduction on your income tax return, provided you keep the receipt and the donation is made to a registered charity — also known as a deductible gift recipient (DGR).[i] An exception, however, exists for when a disaster, such as the recent Townsville floods, is declared by the Australian Tax Office (ATO).[ii] In these cases, donations between $2-10, such as those often given in 'bucket appeals', can be claimed without a receipt.

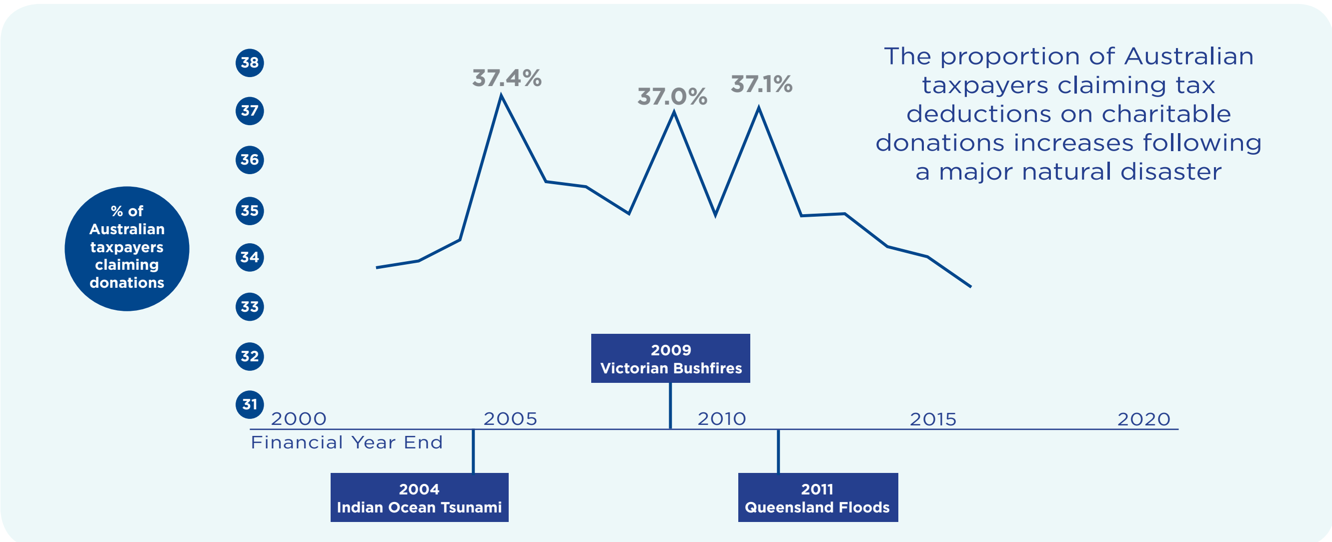
Overall, the share of Australians claiming deductions for charitable donations on their income tax returns has remained steady and low between 2002-2016. Reported donations account for a small percentage of GDP* each year.[iii] Following disasters, however, we observe spikes in the data as Australians tend to donate and subsequently claim more. This is evident from studying the tax returns submitted after notable crises.

The data suggest that people donate more following major disasters, but how much does the oft-referenced 'Average Australian' think about the tax treatment of donations when giving? Realistically, not much. People tend to give when asked, and requests often come from charities at certain times of year when we are likely to be more aware of those less fortunate, such as Christmas and Easter. Australia's tax year runs from 1st July to 31st June, and in most cases individual's need to lodge their returns by 31st October for the previous tax year.[iv] This system means that come time to submit your income tax return, donations may have been made up to 16 months prior — plenty of time to lose receipts, forget the donation was made or simply deem it more hassle than it's worth.[v] It is also likely that some Australians may not be aware of the tax deductions available for donations to DGRs. By forfeiting the tax deduction available on charitable donations, many Australians are not getting the best 'bang for their buck' – also known as the 'tax-price of giving'.

Could we help benefit charities by encouraging more taxpayers to report their donations on their income tax returns? If Australians could better time their donations to match when they are lodging their tax returns, would they give more to charity? And would more taxpayers choose to donate? Studying a temporary policy change in Quebec, Canada following the disastrous Haiti earthquake on the 12th January 2010, gave us the opportunity to explore these questions.[vi]

The Canadian individual tax year runs from 1st January to 31st December, with the due date for filing the tax return falling on 30th April of the following year. As part of a mass appeal to encourage relief support after the Haiti earthquake, the Quebec government allowed residents to claim donations made to the disaster relief efforts in early 2010 against their 2009 tax year return.[vii] Without this concession, the taxpayers would have had to wait a full year (until April 2011) before recognising their contributions to support the Haiti relief efforts. This made the time of claiming a donation on one's tax return effectively immediate to the time of providing the donation.

The change in the tax treatment of charitable contributions in Quebec compared with the rest of Canada provides two interesting insights on how the timing of claiming donations affects the community's contributions. Quebec households were more likely to donate and, on average, donated more than households across other provinces in Canada.



Authors' calculations. Source: ATO tax statistics 2001-2002 to 2015-16 available at: https://data.gov.au

Key Insights

1 Timing influences the number of people donating

Perhaps unsurprisingly, people are more likely to do something if they are aware of the benefit in doing so. This is particularly true if the benefit is received quickly. Immediacy keeps the benefit in the front of people's minds — what economists call 'salience'. To illustrate, 28% of our Canadian friends living in Quebec were aware of the special treatment their provincial government was offering and were 2% more likely to donate to the Haiti disaster relief. By comparison, just 1.8% of residents across other Canadian provinces were aware of the tax treatment of their donations. In this case, timing was everything. Quebec residents knew they could claim their donations up to a year earlier than usual, and a dollar gained today certainly seems better than a dollar gained a year from now. The salience of the tax benefit increased the likelihood of a Quebec household choosing to donate because the value of the benefit was, more or less, immediate.

2 Timing affects how much people donate

Economists often refer to people's sensitivity to prices as the 'law of demand'. The term emphasises how common it is for people to consume more of a good as its price goes down and vice versa. The tax-price of donations across Canada, and Australia for that matter, is lower than the original price of a donation so 'law of demand' should, in theory, apply to all donors to some extent. The key difference in this study, again, is timing. Being able to act at the time of a donation kept the link between donating and receiving the credit salient in Quebec residents' minds. The tax price appeared more tangible and therefore attractive as the credit could be received earlier than usual. Seeing this immediate benefit, Quebec residents gave up to 9 percentage points more per household than their counterparts in other Canadian provinces.

What this means for Australia

Like Canadians, Australians are generally consistent donors and are increasingly generous in crises. On average, GDP in Australia increases 2.85% annually and reported donations have remained small but constant as a percentage of our GDP.[viii] This suggests that we are consistently donating a relatively similar amount each year compared to our national wealth. We can, however, always do more to support charities and the great work they do.

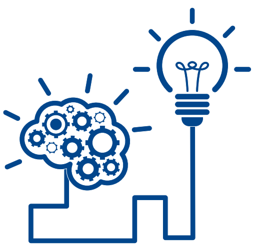
Our research suggests that increasing awareness of tax benefits, reducing the tax price of giving and changing the timing of when tax deductions on charitable donations are claimed, can affect how many people donate and how much each person gives.

How could Australian policy adapt to these findings? To begin with, improving awareness of tax incentives for donations could strengthen charitable behaviour. Additionally, allowing donations made up until the deadline for lodging a tax return to be claimed against a previous tax year would allow donors to make the most of the lowered price of giving through our tax system and allow them to be strategic in their donation decisions. The tax code already builds in flexibility that allow donors to delay claiming a donation for up to five years. Adapting this policy could potentially better support Australians and increase their generosity.[ix]

TAX PRICE OF GIVING

The out-of-pocket cost to the donor after the tax treatment of a donation. For example, Mary earns $60,000 and donates $1,000 to her favourite DGR charity one year. Being money-savvy, she saves the receipt and claims her donation when filing her tax claim. Mary's income falls into the bracket charged 32.5% tax, which is also applied to her donation. The tax-price of Mary's $1,000 donation is therefore only $675 out of her pocket, the government covers the rest.

HOW TO INCENTIVISE GIVING AND PROVIDE FURTHER SUPPORT TO COMMUNITIES IN CRISIS



Increase awareness of tax incentives

Adjust the time for claiming tax deductions on charitable donations

Reduce the tax price of donating

Further Information

Further reading:

Ross Hickey & Bradley Minaker & A. Abigail Payne, 2019. “The Sensitivity of Charitable Giving to the Timing and Salience of Tax Credits,” National Tax Journal, National Tax Association; National Tax Journal, vol. 72(1), pages 79-110, March 2019

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* Gross Domestic Product of a country. It is the total dollar value of all final goods and services produced in a country over a certain period of time and usually speaks to the health of the national economy. For this reason, we can compare financial growth for a given industry, in this instance charities, as a share of the GDP to reflect the growth relative to the overall economic activity of the country. GDP can be expressed in US dollars or, commonly, as a percentage compared to the previous time period.

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iv. Australian Taxation Office, “Individual Income Tax for Prior Years,” accessed February 5, 2019, https://www.ato.gov.au/Rates/Individual-income-tax-for-prior-years/?default.

v. David Knowles, “Snapshot of Australian Giving” (Australian Council for International Development, October 2018), https://acfid.asn.au/sites/site.acfid/files/resource_document/koda-capital_snapshot-of-australian-giving-2018.pdf.

vi. “2010 Haiti Earthquake: Facts, FAQs, and How to Help,” World Vision (blog), June 20, 2018, https://www.worldvision.org/disaster-relief-news-stories/2010-haiti-earthquake-facts.

vii. C Rangel, “Haiti Assistance Income Tax Incentive Act,” Pub. L. No. H.R.4462 (2010), https://www.congress.gov/bill/111th-congress/house-bill/4462/all-info.

viii. Authors’ own calculations using figures from “GDP Growth (Annual %) | Data,” accessed March 21, 2019, https://data.worldbank.org/indicator/NY.GDP.MKTP.KD.ZG?end=2017&locations=AU&start=2004.

ix. Myles McGregor-Lowndes and Marie Crittall, “An Examination of Tax Deductible Donations Made by Individual Australian Taxpayers in 2015-2016,” Working Paper (Brisbane, Queensland: The Australian Centre for Philanthropy and Nonprofit Studies Queensland University of Technology, June 2018), https://eprints.qut.edu.au/119001/7/119001.pdf.

This Research Insight represents the opinions of the author(s) and is not intended to represent the views of Melbourne Institute. Whilst reasonable efforts have been made to ensure accuracy, the author is responsible for any remaining errors and omissions.