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September 21, 2005

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Exemption and Civil
Society***

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Cite as William C. Duncan, *The Charitable Exemption and Civil Society*, 2005 Sutherland J. L. & Pub. Pol'y L25, at <http://www.sjlpp.org/documents/duncan92105.pdf>

The Charitable Exemption and Civil Society

by William C. Duncan

Recent efforts to reform Utah tax policy have resulted in a renewed interest in the charitable exemption for state income tax. Some proponents of a flat-tax favor removing all tax exemptions and argue that the resulting lower tax rate will allow individuals to give more generously than they might otherwise. Charities tend to favor retaining the exemption as a way of ensuring continued contributions.

The Sutherland Institute has urged on two public occasions before the Tax Reform Task Force that the charitable deduction be maintained.

Tax policy can have many motivations ranging from redistribution of income to promoting home ownership. It is altogether appropriate that a state tax policy further the values of its citizens. Supporters of retaining the exemption point out that it can have the effect of encouraging charitable donations and their attendant benefits (certainly an appropriate value in a state like Utah with a heritage and practice of service and philanthropy).

There may be, however, an additional public policy consideration in the debate over a charitable exemption that has been little discussed. It is the message the exemption sends about the proper and respective roles of government and civil society.

The argument is that retaining a charitable exemption is one way that the government can signal its recognition of its own limitation and restrain its interference with civil society and the work that families and communities do best.

It has long been recognized that there is an inherent tension between state power and the influence of mediating institutions—those non-governmental entities that shape individual behavior and transmit values that allow for society to function with some measure of peace and fairness. It is a mark of a liberal (as opposed to authoritarian) state that it recognizes that the work of value transmission is to be done by such institutions as the family, churches and other voluntary associations. It is not only philosophically sound for the state to sharply limit its interference with these institutions, it is a practical necessity in a republic such as ours which requires conscientious citizens but which also recognizes its inability to compel such conscientiousness.

Additionally, in the absence of vibrant mediating institutions, governmental institutions must provide not only the shaping of citizenry but also the provision of basic needs. The state's effort in this regard may be ineffective (or counterproductive), advance different values than those embraced by the citizens it aims to assist, or even unjust.

However, unlike the state (which can ensure support through punitive laws), these social institutions must rely on voluntary contributions to advance their work. These contributions take the form of time commitments, in-kind donations and monetary support (among other things). Families and individuals

must make decisions about such contributions in the context of other demands on their time and resources.

Making these kinds of contributions exempt from taxation not only makes the decision to give easier for people, but it also signals an appropriate humility about what government can and ought to do. It can be seen as a recognition that civil society is the best forum for the provision of basic needs including those like moral direction and spiritual guidance that the state cannot fill. It is the state's way of saying that it will keep its hands off the money that is the lubricant for the functioning of mediating institutions.

Of course, if the government becomes unnecessarily restrictive in designating organizations as tax-exempt, makes the designations on political grounds or refuses to grant exemptions to certain groups, such as churches (as some radical politicians have suggested), the public policy argument for the charitable exemption discussed here would be inapplicable. The current system in the United States is appropriately deferential to charities, however, and thus the policy is sound.

None of this is to suggest that the current tax system is ideal but the appropriately limited view of government's role reflected in this public policy argument for the charitable exemption could be extended to more areas of the tax code with significant benefits to that system.

The model of state deference to civil society reflected in the charitable institution is valuable and ought to be preserved.