

# Analysis on the Situation of Charities in China

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## ABSTRACT

Charities play an important role in society. However, charities in China experienced the corruption of credibility in 2011 and needed to be improved in different aspects including the Charity Law and the regulation inside charities. This paper summarizes the status of the Charity Law and charities in China by pointing out the existing problems with secondhand data and gives some potential solutions by comparing the cases and solutions used by other countries including Canada, the United Kingdom, and the United States. To be more specific, the deficiencies of charities are studied from the aspects of credibility and tax incentives, and the solutions are given concerning the policies of some other countries. The solutions include a clearer rule for the information disclosure and a more accessible tax deduction application process. Finally, the author draws the conclusion that these solutions should be taken into practice based on the status of the economy and society in China so that the efficiency of charities will be improved significantly. The paper points out some directions for charities and the Charity Law to be improved and the potential topics for future studies.

**Keywords:** Charities, China, Credibility, Tax incentives.

## 1. INTRODUCTION

Charities play an important role in society, especially when the country faces big natural disasters. However, charities' progress directions are not clear enough in China, and the law about tax incentives and administration for charities still needs to be improved. After the Chinese Red Cross Scandal in 2011, the credibility of the charities was corrupted, which seriously influenced the donations. According to the data provided by Yaosong Liu, Min Zhang, Tingting Ye, and Yue Zhang [1], the total social donations divided by GDP in China drops from about 0.47% in 2010 to about 0.17% in 2011. Then from 2011 to 2016, the data increases to less than 0.20% at a very low speed. Nevertheless, there are limited studies about the status of charity organizations now and how charities should be developed in the next step [2].

Among the relative research done, scholars including Qing Xu provide some pieces of advice to improve the supervision of charities and the Charity Law using the data provided by FTI [2]. Providing the advice, the scholars admit that research about charities now is limited [2]. Additionally, Brian Kastner argues that the tax

deduction is not really taken into practice well since the process is not clear to most charities and donors [3], which further decreases the social donations.

This paper analyzes the status of charities in China, argues some problems about them with data, and points out the potential solutions by comparing the status of the charities in China and some western countries. Then some solutions are provided based on the existing studies. The paper aims to provide solutions to the problems of credibility corruption and tax deduction policies and to evoke more thoughts for future scholars.

## 2. STATUS OF CHARITIES IN CHINA

### 2.1 Information Disclosure

The charities' credibility is corrupted after the Chinese Red Cross corruption scandal in 2011, but there are limited solutions provided to fix the problem and efficiently help with the improvement of reestablishing the credibility [2]. According to Qing Xu's study, the corruption of credibility of charities is not only caused by the scandal but also caused by the problems in the Charity Law in 2016

[2]. In the Charity Law, financial reporting standards are not explained clearly, and the supervisory to the charities are far from completion. The law requires charities to disclose information, but there are no specific requirements on how to disclose and what information is required to be disclosed [2]. The results of these flaws in the Charity Law are justified by the testing results provided by Chinese Foundation Centers in 2021 April. According to the testing results of 2478 different charities, the average score of the basic information completion test is 45 out of 100, and there are 14.6% of those charities even have no basic information published [4]. Fundraising record information is much more completed than the use of charity funds records, whose test scores are respectively 61 and 47 [4]. In this comparison, it is clear that the information on the use of charity funds is more needed to be collected and published, which is important to make charities more credible and efficient. Additionally, in China the government takes control of many charities, however, some government officers who are responsible for the supervision of the charities are not reliable. This is shown in many examples, such as the cases of Shufu Li and Pengnian You discussed by Qing Xu [2]. The charities with strong political ties are more convenient to pass and even skip the supervision, which leads to the corruption of credibility [2].

## **2.2 Effects on the Companies as Donators**

Moreover, the loss of credibility of the charities influences not only the donations but also the companies who give the donations for better reputations, which makes the improvement of the credibility more necessary and urgent. In some companies, stakeholders use donations to improve their reputation and gain better resources and opportunities [1]. The credibility loss of charities pushes away public trust, and strongly diminishes donations from the public [1]. The corporations then choose to decrease the donations to the charities to prevent the negative influence on their corporations, which results in the further ineffectiveness of charities in society [1]. Besides, the corporations who continue to give donations to those charities have to bear the negative influences on themselves and lose better resources and business, thus negatively influence not only the society but also the economics of the cities [1]. Based on Yaosong Liu, Min Zhang, Tingting Ye, and Yue Zhang's studies, private-owned companies suffer more from this credibility corruption [1].

## **2.3 Application for Tax Deductions**

Talking about tax deductions, based on the Charity Law in 2016, in China, the tax deduction for the donates is up to 30%, which is lower compared to some other countries such as 60% in the United States. But the lower level of tax deduction is not the main problem about the tax deduction. One of the reasons is that tax deduction should be determined based on the country's economic development, and it is not necessary to follow up with other countries in this aspect without a comprehensive consideration of our own country. It can be told that in the future when the economy of China is developed into a certain high level, the tax deduction will be much higher. The main problem with tax cuts is that many charitable organizations do not know how to apply for tax cuts, which leads to this policy not being implemented well [3]. Tax is exempt for subsidies and donations of NGOs. In practice, the formal NGOs who are eligible for the tax deduction do not know about the tax law enough to apply them. 60% of the donators who take the advantage of tax incentives are corporations because it is hard for individuals to know enough about tax law and imply them [3]. Only a small number of charities apply for tax exemption successfully in practice while most charities cannot imply them well. Moreover, the tax law is only applied to legal NGOs, while those informal NGOs who cannot and do not register as charities have no tax incentives [3]. This is because of the problem in the tax incentives: the process to apply a tax-exempt is not clear enough on the law.

Similar conclusions are drawn by YanJie Li, the assistant researcher in the Institute of Law in the Chinese Academy of Social Sciences, Doctor of Law, and postdoctoral fellow in social security. In his analysis of tax incentives on charities in China, the practice of tax incentives needs to be improved and completed since the law now has many gaps in the different processes of different tax incentive applications, and the tax laws are too general without more specific categories and hierarchical regulations [5]. In addition to the gaps in tax incentives application, according to YanJie Li, the total tax is actually so heavy that some donations are reduced for millions after the donators pay different kinds of taxes [5].

## **2.4 Different Tax Deduction Policies**

Additionally, more academic studies are needed to learn about how to set the tax policy to maximize their positive effects on donations, simultaneously, to minimize the negative effects on tax revenue. There are many ways to imply the tax deduction, for instance, nonrefundable tax credits with different upper limits. Which policies are practical in China and suitable for Chinese charities, donors, as well as government tax revenue, and which policy is best for both donations and tax revenue should be identified for future development.

## **3. ACTIONS OF OTHER COUNTRIES REGARDING THESE PROBLEMS**

### **3.1 Comparison to Canadian Charities and the UK Charity Law**

By evaluating different types of Canadian charities, Canadian Feed the Children becomes the A-level charity in all of the international-type charities with its excellent accountability and transparency [6]. Canadian Feed the Children is a Canadian charity that aims to gain donations for the children in poverty in developing countries and help the communities with sustainable development [7]. It is a typical charity with a clear website used to not only receive donations but also publish its financial report in a fixed period, which guarantees its transparency and credibility. Clicking into the website of Canadian Feed the Children, there is a distinctive section called "ANNUAL REPORTS & FINANCIAL STATEMENTS", in which people can download its annual reports, financial statements, and public tax return on the CRA website. Under this clear section, there are websites portals for more annual reports and financial statements categorized based on different periods from 2013 to 2016 [7]. In addition to the financial reports, there are many other parts, including the determination of the organization's mission and their planning of goals.

A similar website regulation method is used by many large charities in China such as the Red Cross Society of China and China Women's Development Foundation, however, it is needed for small charities to learn to use the website regulation and gain transparency in the information needed. Take ShuiDiChou as an instance, the company ShuiDiChou is famous for raising money for people who are sick and need help. On its website, it is

clear to see the list of dishonest fundraisers and the personal serious illness help information publicity system, however, there are no clear financial statements available for donors to check [8]. When it comes to its credibility, it suffers from credibility corruption since people are susceptible to its quality. In the studies done by Xiao Wang and Rong Guo [9], the ShuiDiChou company was complained of fraud by people. The transparency of ShuiDiChou is far from enough, and there were fraud events published before. For instance, a girl with an eye tumour in Zhoukou Taikang County received donations from the public. In fact, her mother did not take her to the hospital until volunteers were going to her home to ask about her disease. The event was ended with the disappearance of the girl and her mum [9]. Until today, people still use it to donate money without getting access to its financial statements or any other detailed financial information.

Additionally, although the annual financial reports are accessible on the website, the Spring Bud Project of China Children Teenagers Fund, which aims to help girls with their education, was disclosed as defraud. The money claimed to be spent on girls' education was partly spent for boys including some boys who are older than 19 years old. Of the 1267 high school students they helped, 453 of them are males, which was different from their claim that their donations are for girls' education [10]. This detailed information such as aid-receiving students' background information was not accessible until the Spring Bud Project was reported as defrauding, and was provided by the aid-receiving schools instead of the China Children Teenagers Fund [10]. This incident of integrity and corruption ended with the promise of the China Children's Fund. They claimed that all donations will be used for girls' education in the future [10].

When it comes to the Charity Law, a comparison to the Charity Law of the UK is shown. In the UK Charity Law, there is a clear list of different types of charities to check the process by which they report their information, such as annual reports [11]. In the law published on the website, these related links are provided inside the sentences to contain more detailed instructions. By contrast, in the Charity Law [12] shown in the Chinese Government Website, there are no such links provided inside the sentences, and people have to scroll down slowly to catch the information they need. Moreover, the Charity Commission of the UK also gives examples for the charities to consider and helps them report the required information

correctly [11]. In this case, the whole process of making the information accessible for the public and the supervisors is clear and easy to be put into practice, which will definitely improve the credibility of the charities and reestablish the efficiency of the charities in society.

### **3.2 Comparison to the United States**

Taking the United States as an example, some scholars compare the effects on tax revenue and donations of different tax policies implied by the American government and study which one is the best to increase donations and decrease the loss of tax revenue. According to the study results by Indiana University Lilly Family School of Philanthropy [13], seven different types of tax deduction policies and their effects on donations are compared. Among the policies, nonrefundable 25 percent tax credit brings 37 billion dollars on donations while having a loss of tax revenue of 33 billion dollars, which is the most costly policy for the government. Non-itemizer charitable deduction brings 26 billion dollars on donations while causing a loss of 22 billion on tax revenue. The best policy is the non-itemizer deduction with a modified 1 percent floor, which brings up 7 billion on donations more than the amount of the losing tax revenue. By contrast, the non-itemizer deduction with a 4000/ 8000 dollars cap has the worst effect on donations, bringing fewer additional donations than the loss in tax revenue. However, when people consider the policy to bring equity for lower-income donors and high-income donors, a non-refundable 25 percent tax credit should be the best policy. Similar studies are needed for China to pick up the best policy because the suitable policies should be different in different cultural backgrounds.

## **4. SOLUTIONS PROVIDED**

### **4.1 Credibility**

According to the reasons for the credibility corruption and its potential consequences, there are some possible ways to improve the transparency of the charities. First, the government should decrease the political ties of the charities to make the supervision more strict and fair, preventing the phenomenon that charities with weak political ties have more strict supervision while others have less strict supervision. According to Dr. Lu Dezhi, the founder of the Human Charity Foundation, it is better to have a third party take the responsibility

for the supervision of the charities [14]. Then the government takes the responsibility of random inspection to both the charities and the third party, managing a rewards and punishment system for them. Second, there should be an efficient online system for the charities to post the information on time, and the systems should be free to access for the public. What kind of information is needed to be published should be categorized and regulated by the government on the Charity Law. Based on the data provided by CFC, 90.2% of public foundations have financial information accessible to the public, while 79.6% of private foundations have the information accessible [4]. Only 36.9% of public foundations publish their financial information automatically, and 30.1% of private foundations do the same [4]. This status will be improved if the charities have an efficient online system to help with collecting and managing their related data, and the government has a third party to help with supervision and implementation for the information publishing of the charities. Finally, the Charity Law should be more completed about what information is required to be included when the charities publish the information and how the supervision would be conducted in detail. On the website for publishing the law, links between lines and keywords can be added so that the charities can check the rules and follow them more easily. When the officers try to complete the law, the cases of other countries can be considered.

### **4.2 Tax Policies**

To solve the problem that tax incentives are not completely implied by charities, some strategies can be considered. First, there should be government officers regulated to teach charities and donors about how to imply tax incentives in a fixed time, and there should also be government officers who are responsible to answer questions any time when charities and donors have problems about their specific circumstances of application for tax deductions. In the law published online, the process of applying for tax deductions should be more completed and specified. The information and systems used to submit the application if needed should be accessible for all charities and donors. In addition, the informal NGOs should be classified more carefully so that there will be more NGOs are eligible for tax deductions. In addition to these improvements needed about the application, which tax policies are feasible and effective for China needs more studies. Different policies which lead to a tax deduction as

the result should be considered, and the best one should be applied in China after consideration based on the conditions and cultures in China. For example, non-refundable tax credits with some specific upper limits to retain groups of donators are a common policy to deduct tax for the donators. The upper limits for lower-income donators and higher-income donators should be set according to their different average income levels in China to bring the equity. And if the tax credits are a good way to give the tax incentives is also considerable, which should involve the economic development and the tax revenue of China.

## 5. CONCLUSION

According to the analysis above, the credibility of charities and tax incentives policies have different problems that obstacle to the development of charities since the credibility corruption in 2011, and there are potential solutions available to solve them. First, with the comparison to Canada and the United Kingdom, careful regulation of the Charity Law is needed for charities in China to rule the information they should disclose, which will efficiently improve the transparency of charities and improve the credibility of charities from the public. Second, the process of applying for the tax deductions needs to be improved. The process is not clear and accessible to the donators and charities, which leads to the inefficient practical use of tax deductions. And some public rights NGOs should be clarified more clearly with a specific law for them. Now they are not eligible for the tax deductions since they cannot register as legal charities, which further leads to a decrease in donations to people who need help. Besides, different policies of tax deductions should be studied, and the best one should be picked based on the conditions of China.

With the analysis in this paper, many thoughts of the status of charities in China and the Charity Law are provided, and the directions for Chinese charities to develop are pointed out. The areas discussed in this paper need more studies to learn deeper and test the feasibility of the solutions provided. Referring to the examples of other countries is a way to make improvements for Chinese charities, but it is also important to get a closer look at the status of Chinese charities and get the application of the solutions into practice to solve the problems.

## AUTHORS' CONTRIBUTIONS

This paper is independently completed by Wenlin Du.

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