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PODER Philanthropy Forum: Rethinking the Power of Giving

Keynote Speech

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Ladies and gentlemen,

Thank you very much. It is a great honor to be invited to the PODER Philanthropy Forum in Miami, and to the PODER-BCG Business Awards, which are given to the most outstanding people in business and regional leadership. Congratulations to the winners.

The topic that *PODER Magazine* and the Interamerican Development Bank chose for this forum is of crucial importance: philanthropy in the American continent, which in the XXI Century has been growing significantly with the emergence of new donors and new technologies which are bringing borders closer and are

showing that the challenges of poverty and inequality in our societies still remain daunting. At the same time, it becomes necessary to amend the law adequately to be able to reap the benefits and face the challenges of a growing philanthropy with global reach.

Philanthropy, a Greek word that means “love to mankind”, is today associated in general with voluntary donations of an individual or a group with the objective of promoting the common good and a better quality of life. Because of this, individuals and civil society organizations dedicated to philanthropy usually have a great potential to serve as collective agents of the social and political development of a country. As a reference we can look at the case of the United States, where philanthropic work is not only as old as the country itself, but also it is widely extended among the entire population —and not just among high-income individuals, as one may think. Philanthropic work in the United States thus reflects two of its core values: generosity and liberty, which come from the freedom of expression and freedom of association. Since the times of Andrew Carnegie, philanthropic work in this country puts across the commitment of the richest people to look for the circulation of

wealth and to better the quality of life of the less fortunate. As a result of this participative society, the largest philanthropic foundations of the world are today in the United States, some of them with programs and resources so big —like the Bill and Melinda Gates Foundation— that are able to compete with International Financial Organizations such as the International Development Association of the World Bank Group (IDA). In this respect, an important characteristic of US entrepreneurs is the request of the measurement of the impact of donations in order to estimate the returns of this “social investment”.

In contrast, the impact of the non-profit sector in Mexico and Latin America has been limited due to several historic reasons, in particular income inequality: an analysis done by Merrill Lynch detected in 2006 that the number high net-worth individuals in Latin America outpaced the global average, and that the wealthy saw their net-worth increase by over 20%. Latin America, according to the World Bank, remains the most unequal region in the world with big pockets of poverty despite the positive rates of growth observed in the last years.

In this framework, the policies and actions of governments in Latin America to fight poverty and promote human development could be significantly aided philanthropic work of the private sector. However, a Johns Hopkins University study estimates that the average of philanthropy donations in the region is almost five times smaller than the contributions in the United States and the United Kingdom. This fact does not only evidence how the region lags in philanthropic work, but also how important a forum like this is, as it gathers individuals who are convinced that “social investment” may constitute an effective way to promote human development in our societies and who believe that the private sector can and should contribute by sharing responsibilities with the government to allocate available resources in a strategic and progressive way.

From this perspective, it is worth to ask what would be the best policy that governments in Latin America should follow with respect to philanthropy and civil society. It could be said as an answer that it is very important for governments to privilege the freedoms of association and expression, that they enhance the legal and fiscal framework to increase the non-profit sector and its work, and that they promote partnerships between this sector, the private sector

and the government itself, as the impact of the three together is certainly larger than any of them alone.

After this brief overview of philanthropy in the United States and Latin America, I will center my comments on the current regulations in Mexico with respect to fiscal matters related to donations from individuals and corporations, as well as available incentives for this activity and their importance in a wider macro- framework.

In Mexico, philanthropic activity is carried out mainly through foundations or non-profit civil society organizations, among which we can distinguish three groups: non-profit organizations authorized by the Ministry of Finance (or *donatarias autorizadas*, as there is no equivalent legal translation), non-profit organizations, and informal civil society organizations (which, for some reason, have not formalized their legal status by joining the Public Registry).

The legal framework of the first two is comprised by the *Mexican Constitution* (Article 9, freedom of association), the *Civil Codes* of the States of the Federation (which stipulate the legal forms of associations available), the *General Law for Social Development*

(which elaborates on the mandates, activities and functions of these organizations), the *Law for Social Assistance* (through which private assistance organizations were given public interest status) and the *Law for the Promotion of Activities of Civil Society Organizations* (by which their mercantile character was modified in order to consider their activities as public interest).

Turning now to the fiscal framework, and given their particular characteristics, civil society organizations dedicated to philanthropic work are subject to a very specific regime: non-profit organizations (*personas morales con fines no lucrativos*, as again there is no straightforward legal translation) as established in the Title III of the *Income Tax Law (ISR)*, which exempts them from the payment of this tax. According to the Articles 93, 95, 96 and 97 of this law, these organizations can be classified in two groups: non-profit organizations; and non-profit organizations authorized by the Ministry of Finance to receive deductible donations (or *donatarias autorizadas*, as mentioned before).

Both types of organizations share the advantages of being exempted from income tax. The *donatarias autorizadas*, in addition,

have the prerogative of being able to issue tax-deductible receipts for the donations they receive (Articles 31 and 176 of the *Income Tax Law*), which puts them in a privileged situation in the fiscal system in exchange for greater surveillance and control from Mexico's Internal Revenue Service (SAT).

To qualify as a *donataria autorizada*, non-profit organizations must comply with some requisites by law, among which the most important are that a substantial portion of their income comes from either donations or federal, state or municipal funds; that they do not participate in political campaigns; that they fulfill their mission and do not distribute earnings among partners; that they provide the public with transparent information with respect to the sources and uses of donations; and that they surrender their whole patrimony to another *donataria autorizada* when terminated. Moreover, they must provide the Local Tax Authority with their application for authorization together with a copy of their statutes, their tax registration number (RFC), and a letter of accreditation of their philanthropic work. In addition, they must fulfill certain obligations with the Ministry of Finance such as reports, an annual statement and a fiscal certification.

It must be stated here that the *Single-Rate Business Tax Law* (the *IETU Law*) —one of the products of Mexico’s Fiscal Reform— approved in October 2007 was designed in a modern way according to best international practices in order to keep the *donatarias autorizadas* with the same exemptions and deductions that they have under the *Income Tax Law*. Specifically, Article 4 of the *IETU Law* stipulates that the *donatarias autorizadas* are exempt from this new tax, while Article 5 allows the deduction of donations that do not exceed 7% of either the fiscal earnings of organizations or the cumulative income of individuals in the previous fiscal exercise.

From the analysis of the legal and fiscal framework in which the non-profit civil society organizations work, it becomes evident that the category of *donataria autorizada* is the one that offers the largest benefits and fiscal incentives and, thus, has the greatest potential to become an engine of philanthropy in Mexico. One of the main tasks of the Ministry of Finance and Mexico’s Internal Revenue Service is precisely to support the works of these types of organizations and to make it easier for them to obtain the category of *donatarias*

autorizadas, fulfill the requisites and comply with the obligations of such a regime.

Finally, and returning to the context of globalization and philanthropy that I mentioned at the beginning, we must consider the cross-border dimensions of philanthropy in our region. In particular, the *US-Mexico Double Taxation Treaty*, which entered into force in 1994, had the purpose of facilitating the activities of philanthropic institutions on both sides of the border by authorizing Mexican non-profit organizations to receive tax-deductible donations. To do this, the Treaty established an equivalence between the organizations classified under Article 70-B of Mexico's *Income Tax Law* and Articles 509(a)(1) and (2) of the US *Revenue Code* to allow them to be included in *Publication 78* of the US Internal Revenue Service (which contains the official list of equivalent non-profit organizations). This article was updated and re-numbered in 2002 as Artículo 97 of Mexico's *Income Tax Law* and, even though being equivalent to the previous versions, in practice only very few Mexican non-profit organizations and their foreign donors are making use of the benefits under the Treaty.

Although the framework described above shows that Mexico has the legal and fiscal tools to promote philanthropic work of civil society organizations, the statistics demonstrate that there is still a lot to do if we want to compare ourselves with more advanced economies in this field: according to the *Centro Mexicano para la Filantropía* (CEMEFI), there are around 20,000 social organizations in the whole country (not all of them with formal legal status); however less than 6 thousand are authorized by the Government to receive tax-deductible donations. Of them, less than 300 are foundations that donate.

Nevertheless, Mexicans have a lot of solidarity: when an earthquake, hurricane or any natural disaster occurs, their answer is always generous and straightforward. In contrast, in terms of support to civil society organizations, Mexico ranks last in the global ranking as it only donates .04% of its GDP, according the data from the Johns Hopkins University. Michael Layton, professor at ITAM, explains these numbers by the existence of a culture of low trust and civic participation which forces Mexican generosity to deliver through informal rather than by institutional channels.

¿Why is it that, despite having legal and fiscal frameworks that promote philanthropy, civil society organizations do not make use of them? Perhaps there is still a lot of work to do to simplify the law and administrative processes that the civil society faces while keeping the objectives of revenue and transparency that the authority requires. Moreover, there are probably some discrepancies between the visions of the authority and the representatives of civil society with respect to the legal and fiscal issues applicable to the sector, and this can have a strong influence the mood of negotiations.

In this respect, it is worth to mention that the Federal Government assumed the compromise of promoting philanthropy in the country, and therefore has created a consultative group comprised by leaders of civil society organizations, Mexico's Internal Revenue Service, the office of the Minister of Finance and prominent members of the academia in the field. Together, they maintain an open dialogue to reach agreements by consensus in order to enhance the operating framework of philanthropic organizations in Mexico. In fact, one of the products of the works of this group is the "Transparency Webpage for Non-Profit Organizations" of Mexico's Internal Revenue Service (*Portal de Transparencia del SAT para*

Donatarias Autorizadas), which seeks to contribute to the generation of trust in the sector among the general population and the Congress.

Moreover, this consultative group met last week in Washington DC to analyze common problems of civil society organizations on both sides of the border, and reached agreements which can help to solve the question of why US and Mexican donor organizations are not making use of the benefits of the Double Taxation Treaty, without modifying this instrument or any other US or Mexican internal law. In this workshop, officers of Mexico's Internal Revenue Service and the Office of the Minister of Finance met with US foundations and their legal advisers, as well as with their counterparts of the US Internal Revenue Service to learn about best international practices in the field.

There is still a lot to do, however I am convinced that the government, the civil society and the private sector are pursuing decisive steps for the advancement of philanthropy in Mexico. I would therefore like to finalize by quoting Ariel Fiszbein, a researcher at the World Bank who states that

“a new pattern of responsibility for poverty reduction beyond the public sphere is emerging today. Nevertheless, given limited resources available, the ability to face this challenge depends on partnering with other sectors more”.

In this sense, philanthropic organizations are essential today as neither the government nor the private sector can address the poverty and income inequality problems alone. At the same time, it would be useful to strengthen the social bases of the organizations in order to transform their members from passive recipients of philanthropic work into participative citizens with rights and obligations looking for social change. Since these kind of responsibilities have been traditionally delegated to the State, its capacity to address them depends today in leaving aside what Octavio Paz called the “philanthropic monster” —the paternalistic and all-inclusive State— and partnering more with other social sectors, in particular the private sector.

Thank you.

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