A New Take on Tithing

By Claude Rosenberg & Tim Stone

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Too often, individuals make decisions about how much money to donate to charitable causes on an ad hoc basis. As a result, many people give less money than they can actually afford.

If the affluent contributed as much to nonprofits as the authors believe they can, charitable giving in the United States would increase by $100 billion a year – enough to solve many of the world’s most pressing problems.
MALNUTRITION, ILLITERACY, DISEASE – the problems of the world often seem insurmountable. But we see grounds for hope. According to our calculations, individual charitable donations in the United States alone could increase more than $25 billion a year if affluent households donated as high a proportion of their assets to charity as do the middle class and those below. This 17 percent “generosity gap” is our low-end estimate of how much additional money could be donated.

If affluent donors gave as much as we think they could afford, based on our conservative donation benchmarks, charitable giving in the U.S. would rise by about $100 billion per year.

To put those numbers in perspective, consider a recent analysis of how much money it would take to solve some of the world’s most pressing problems. According to the Borgen Project, annual expenditures of $19 billion between now and 2015 could eliminate global starvation and malnutrition. Another $12
billion per year over that same time period could provide education for every child on earth. And an additional $15 billion each year could provide universal access to clean water and sanitation.1 In other words, three of the world’s most pressing problems could be solved in less than a decade if our nation’s affluent stepped up to the plate. And there would still be another $46 billion left over to tackle other causes.

How do we know this? The NewTithing Group, our San Francisco-based philanthropic research organization, has been studying this issue since its founding in 1998. We have used our knowledge of asset management and financial planning to come up with formulas for determining how much people can comfortably donate given their income, expenses, assets, and future needs. We have also closely examined IRS data on the incomes, assets, and giving levels of various groups of U.S. citizens over the years to understand how much people actually donate. By combining these studies, we are able to project with some certainty the gap between how much people presently donate and how much they could donate.

If hundreds of thousands of Americans possess a huge untapped potential to help secure our collective future, then why do the “have” not give more to worthy charities? Anecdotal evidence from fundraisers suggests that many donors give in a piecemeal fashion, discovering their total donations only after preparing their tax declarations. Such a haphazard approach may depress major gifts because without a financial reference point, households often lack the financial perspective to donate sums commensurate to their wealth.

For example, even for the few donors who already budget for charity, the only generally accepted giving formula, tithing, calls for donations equaling up to 10 percent of income. But this guideline ignores the bulk of Americans’ wherewithal — investment assets. According to the IRS, in 2003, nearly 2 million income tax filers with adjusted gross incomes of $200,000 to $500,000 owned average investment assets of $1.2 million, not including their personal homes and retirement pensions. Even with these substantial assets, this group donated an average of just $8,230 per household to charity.

If these affluent households had systematically examined their financial plans and investments, and anticipated the tax savings they would gain from charitable gifts, would they still have concluded that the maximum they could comfortably afford to donate to charity amounted to less than 1 percent of their assets (which is the actual amount of money they did give)? We believe the answer is no. That’s why we have developed the approach that we call “new-tithing,” along with a sophisticated formula to help people understand how much money they can actually afford to give to charity.

Give Now
One of the principles that underlie our approach is the belief that donating money to charity now yields more substantial rewards for donors and society than donating money later. According to “Rosenberg’s Rule,” a donation now will likely solve more than that same donation later because “societal ills generally increase at an exponentially greater rate than does return on capital.” This rule was named after co-author Claude Rosenberg, founder and chairman of the NewTithing Group and author of the 1994 book, Wealthy and Wise: How You and America Can Get the Most Out of Your Giving. Before founding NewTithing, Rosenberg was founder and chairman of RCM Capital Management, an institutional money-management firm that is now a unit of the Allianz Group AG.

We devised Rosenberg’s Rule in reaction to Warren Buffett, who, up until his dramatic announcement in June that he would begin distributing his immense wealth, had planned to postpone the bulk of his charitable giving until after his death. Buffett reasoned that by postponing his giving, he could use his wealth to generate superior investment returns, which would benefit society more in the long term.

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Warren Buffett (right), the world’s second wealthiest person, announced in June that he would donate $31 billion to the Bill & Melinda Gates Foundation. (Bill Gates is at left.) Buffett’s unprecedented gift reversed his earlier plan to hold on to his wealth until he died and then donate it to charity.
We disagree. Rosenberg’s Rule is buttressed by a McKinsey & Company report that concludes, “The time value of money shows that delaying investments in the social sector exacts an enormous [societal] cost.” The McKinsey study confirms our own observation that if ignored, societal ills may cascade through families, potentially disadvantaging siblings, parents, future generations, and the community at large. We can’t determine whether Buffet’s rate of investment return has, or ever will, exceed the expansion rate of the world’s societal ills. However, we are delighted that he has changed his mind, and hope that his decision to give most of his wealth to charity over the next few years sets an example for affluent households.

How Much People Give

One impediment to new-tithing, and thus to increased giving by affluent households, is the flawed way that many donors, financial advisers, and researchers gauge charitable-giving capacity. The mantra of philanthropic giving and research is to measure gifts relative to income, not assets. This approach incorrectly suggests that the superrich donate more than the middle class and below. (See p. 29 for definitions of social classes.)

When one measures charitable gifts against investment assets, a different picture emerges. By this measure the upper middle class and the middle rich, whom we call the affluent, donate half as much to charity as do the middle class and below (see chart, right).

To better understand the giving patterns of the affluent, and how much money they are capable of giving, we broke this group down by age. Using the latest available IRS data (tax year 2003), we found:

- If 189,000 affluent (upper middle class and middle rich) filers age 35 and younger had donated to charity the same proportion of their assets as did their less-affluent peers, they would have donated an additional $2.6 billion, or 19 percent more than they actually gave.
new-tithing – v., n. new-tithing – l. affordable donation to charity based charitable gifts, projected expenses, assets (after debt, not counting per

• If 1.1 million affluent filers age 36 to 50 had donated to charity the same proportion of their assets as did their less-affluent peers, they would have donated an additional $12 billion, or 25 percent more than they actually gave.5

• If 876,000 affluent filers age 51 to 64 had donated to charity the same proportion of their assets as did their less-affluent peers, they would have donated an additional $10.5 billion, or 22 percent more than they actually gave.6

Added together, the affluent could have donated an additional $25 billion, an increase of 17 percent in the total amount of actual giving in 2003. As big a number as this is, the true “generosity gap” exceeds these estimates because:

• The philanthropic capacity of the affluent is understated because the findings do not account for charitable deductions, a factor which disproportionately reduces the cost of donations by the affluent.

• The actual generosity of the middle class and below is understated because IRS data do not capture non-itemized charitable contributions, which would likely reveal higher donations by these more modest groups.

• Estimates of investment assets are understated because they do not count pensions, personal homes, farm real estate, and over $300 billion in (illegally) undeclared income, generated from hundreds of billions of dollars in unidentified assets.7

Why People Don’t Give More

If charitable giving can not only help the underprivileged, but also safeguard humanity, why do the affluent donate a lower proportion of their considerable asset wealth to charity than do their middle-class peers? There are a number of factors that cause donors to think illogically and give less than they can comfortably afford, all stemming from their lack of a systematic method for determining how much to donate.

The myopia of eyeballing. When donors eyeball, they probably lowball. Many donors react to charitable solicitations in a piecemeal manner. If donors eyeball how much they give without actually knowing how much they can afford to give, they may feel the need to lowball the amount to protect themselves. This approach can cause donors to err on the side of caution, significantly underestimating their giving power. Failing to decide on an annual giving level at the beginning of each year may further depress donations because making several decisions over time may make the same total donation “feel” more costly.

The failure to anticipate tax savings. Many donors evaluate the face value of a contemplated gift without anticipating the charitable tax deduction that lowers its out-of-pocket cost. For example, if a person with an adjusted gross income of $120,000 donates $1,000 to a nonprofit, it actually costs them about $700, not $1,000. That’s because the $1,000 donation generates about $300 in tax savings. Tax savings can be even greater when people donate a long-term appreciated asset instead of cash, allowing them to avoid capital gains taxes.

The herd mentality. Most people want to give at or below the perceived average level of giving, which appears reasonable by virtue of consensus, even if the logic behind it is faulty. “What’s the average major gift?” a donor might ask a development officer. Since the majority of donors tend to have less money than the affluent, the less-affluent multitudes tend to depress the average giving level, even of major gifts. This in turn can discourage those with more wealth from giving at a higher level commensurate to their financial wherewithal.

The problem with old tithing. When people tithe, they typically base the amount they give on their income alone, not on their income and investment assets. If the bulk of a donor’s wealth resides in investments, tithing even 10 percent of their income may fall short of their actual giving capacity. It’s important to note that although we ask people to factor income and investments into their charitable choices, for those with moderate incomes new-tithing is often more conservative than old tithing because it takes into account their living expenses and need to save for future costs like tuition, healthcare, and retirement.
The deceit of inflation. Many donors give away a fixed amount of money each year, without adjusting it upward for inflation. The effect of doing this is that the amount of their giving actually declines every year. What many donors forget is that given long-term rates of return, the value of their investment assets are probably rising well ahead of inflation.

The more money syndrome. The drive to amass ever more wealth can become an irrational reflex that detracts from charitable-giving decisions. Some donors may have trouble adjusting their giving upward even when their wealth is rising. The desire for more money comes from many sources. Not only do many Americans want to “keep up with the Joneses,” virtually the entire financial industry is paid to grow its clients’ wealth according to risk/reward ratios. Few financial advisers at even the most sophisticated levels suggest to a client the personal and societal advantages of reducing their net worth, even to those who have more than enough money to live on, retire on, and pass on to their heirs.

The fear of death. The thought of parting with money may trigger in some people an association with death, which may cause some donors to avoid spending down assets for any purpose, including charity. Social workers note that some elderly adults choose to reduce their lifestyle rather than spend down their assets and acknowledge the proximity of death. Since most people can’t time their own demise, few people can predict their lifetime living expenses. However, donors reluctant to draw on assets to donate to charity—even when their assets dwarf all conceivable lifetime living expenses and financial plans—may want to reexamine their giving strategy.

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<th>Salary and Non-Investment Income</th>
<th>Start-of-Year Investment Assets</th>
<th>Actual Gift</th>
<th>Suggested Gift</th>
<th>Potential for Increased Giving</th>
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The desire to leave enough to heirs. Some donors say that they can’t give as much to charity as they would like because they want to leave their heirs as much as possible. Yet leaving large amounts of money can sometimes impede their heirs’ personal drive, self-esteem, and career. It often makes more sense to leave one’s heirs a generous yet moderate amount of money. Warren Buffett devised an instructive rule of thumb in the mid-1980s, observing that “a very rich person should leave his son’s increased donations of $4,500 would cost them only $2,800 after accounting for tax deductions.

Determining How Much to Give
To help donors more wisely decide their giving levels, NewTithing Group has developed the PrudentPal Charitable Giving Planner, an online tool available at www.newtithing.org. This tool encourages users to explore their emotional reaction to various high-, medium-, and low-donation levels. By monitoring their gut reactions to donation levels and financial scenarios, users can employ a “Goldilocks method” to find just the right giving level.

PrudentPal’s scenarios are based on donors’ investment assets, charitable deductions, and living expenses, as well as on conservative long-term rates of return. Accounting for these factors, our giving benchmarks aim to preserve donors’ assets ahead of inflation after charitable gifts. According to these benchmarks, average households earning over $200,000 in adjusted gross income can comfortably afford to more than double, or even quadruple, their annual donations (see “The Generosity of Rich and Poor,” p. 27).

One Couple’s Giving Plans
To demonstrate how the new-tithing approach actually works, we invented a fictional couple – Susan and John Goodhue of Wilmette, Ill., an affluent suburb north of Chicago. The Goodhues have a combined salary of $230,000, $500,000 in investment assets, and a $450,000 pension, to which they annually contribute $168,000, including $24,552 that they save toward college tuition for their two children, and another $18,400 that they deposit into their retirement pension. Their employer adds 5 percent of income.

Only when filing their tax return do the Goodhues discover that they donated a total of $4,500 to charity – $2,500 in religious dues and Sunday school fees; $1,000 to the public school attended by their two children, ages 9 and 12; and $500 each to their college alma maters. But something doesn’t feel right. They’d like to do more for their local community and for the world their descendants will inherit. They also want to serve as stronger civic role models for their children. John wants to give to a local nonprofit organization that helps underprivileged adults go to college. Susan wants to support an organization that helps convert farmland to corn for the production of cleaner-burning alternative fuels. What’s the maximum they can comfortably afford to give without sacrificing their lifestyle and financial plan?

To try on various donations for size, the two log on to www.newtithing.org and click “PrudentPal.” After entering their assets and salary, they first check the suggested giving level, which comes to $4,800 – about $300 more than what they donated the previous year. Given conservative long-term rates of return, PrudentPal estimates that after living expenses and charitable donations, the couple’s year-end investment assets (not counting their home, possessions, or pension) will total $329,000.

The couple then run a quick approximation to see what would happen if they donated half as much to charity as they did the previous year, or $2,250. This scenario would force them to skip contributions to either their children’s public school and their college alma maters, or to their religious congregation. This donation level seems too small.

They run a second scenario, this time doubling their previous year’s contributions to $9,000. This would allow them to continue their gifts of the previous year, and also to donate an additional $2,250 each to help at-risk youth go to college and farms develop better fuels. According to PrudentPal, the couple’s increased donations of $4,500 would cost them only $2,800 after accounting for tax deductions.

Suggested Giving Benchmarks
NewTithing Group’s giving benchmarks call for donating a specific proportion of assets after accounting for anticipated tax savings. In other words, for households in the maximum tax bracket, donating 1.5 percent of asset wealth to charity does not really cost the donors 1.5 percent of their investment assets. After factoring in tax deductions, donors’ out-of-pocket costs come to just 1 percent of assets. Using this “tax-leveraged” logic, the benchmarks suggest making annual gifts by viewing the cost to donors net of tax savings, for net donations ranging from 0.6 percent of assets for households with investment assets of $500,000 or less, to 3 percent of assets for households with over $20 million. For example, the benchmark suggests that households with investment assets of $500,000 make annual donations of 1 percent of assets, or $5,000, with a net cost of just 0.6 percent of assets, or $3,000.
Social Classes

In this article we refer to “the middle class and below,” “the upper middle class,” “the middle rich,” and “the superrich.” Although such terms are open to debate, the following definitions distinguish the least affluent, the middling, the comfortably well-off, and the very affluent.

**The middle class and below** earn household incomes under $200,000 and hold average investment assets ranging from $45,000 to $335,000.

**The upper middle class** earn household incomes of $200,000 to under $1 million and hold average assets of $1.2 million to $3.1 million.

**The middle rich** earn household incomes of $1 million to under $10 million and hold average investment assets of $5.7 million to $32.1 million.

**The superrich** earn household incomes of $10 million or more and hold average investment assets of $125.1 million.

*Investment assets do not include personal homes, possessions, or pensions.*

A third option offers to show how tax savings would allow them to donate *more* than their contemplated $9,000 donation. Clicking this option reveals that for $9,000 in out-of-pocket costs they can make $14,500 worth of donations. In other words, $14,500 in donations minus $5,500 in tax savings produces a net out-of-pocket cost of only $9,000.

They decide that the last scenario feels just right. The resulting $14,500 worth of gifts (a $10,000 increase in gifts over the previous year) will allow the couple not only to continue their previous donations, but also to add $3,500 to help the at-risk kids’ college program, $3,500 to the renewable-energy initiative, $1,000 to a teacher-training program at their children’s school, and an additional $1,000 to each of their college alma maters.

Not only are the Goodhues able to give more money to causes that they believe in, they are also able to do so without agonizing over these decisions on a piecemeal basis throughout the year. They don’t experience any gnawing doubt about how much to give, nor any uncertainty about saying “no” when confronted with other solicitations. Instead, they can watch the progress of their gifts, show their children the programs that they support, and feel positive about their contributions.

Transforming the World

New-tithing helps transform philanthropy from a reactive obligation to a proactive passion, one that helps ensure freedom and security for everyone, everywhere, for generations to come. It will also help create substantial amounts of new money for nonprofits of all types. Much of that money will end up going where charitable donations from the affluent often go – to religious organizations, universities, and prestigious arts organizations. But some of that new money will also go toward solving critical social problems like poverty, malnutrition, and illiteracy.

Can we really afford not to address these pressing issues? If the have-nots don’t step in to help the have-nots, ownership of capital may become increasingly tenuous. In many developing countries, the gap between rich and poor has caused a draconian taxation on wealth, expropriation of private industry, or the threat of crime so prevalent that owners of capital live with armed guards. Gated communities in America already suggest that wealth disparities can impact personal freedom even in our stable capitalist democracy. And given the state of the world, the security of our capital is the least of our problems. In the past, we smiled tolerantly at those who hoped to “save the world.” Now, many more people need to share that goal.

1 See the Borgen Project (www.borgenproject.org). The Borgen Project estimates that annual expenditures of $40 billion to $60 billion would meet the eight U.N. Millennium Development Goals for eliminating world poverty and would ensure environmental sustainability by 2015.

2 Jansen, P.J. & Katz, D.M. “For Nonprofits, Time is Money,” The McKinsey Quarterly 2002, no. 1. One of the report’s many examples that support Rosenberg’s Rule: “When asked to choose between receiving a donation now or in 12 months’ time, the managers of nonprofit organizations whom we interviewed indicated that to accept a delay, they would need an implied interest rate as high as 50 percent because they could use those additional resources today to address pressing social needs.”

3 As of June 2006, the value of Warren Buffett’s planned charitable gifts to the Bill & Melinda Gates Foundation and foundations run by members of his family total $37 billion, according to Fortune. This equals 85 percent of the wealth of the world’s second-wealthiest individual.

4 Based on the latest available IRS data (tax year 2003), for income tax filers aged 35 and younger, the middle class and below were three times as generous as the upper middle class and the middle rich. The former donated 1.87 percent of asset wealth to charity versus 0.54 percent by their wealthier counterparts.

5 For income tax filers aged 36 to 50, the middle class and below were twice as generous as the upper middle class and the middle rich. The former donated 1.52 percent of asset wealth to charity versus 0.74 percent by their wealthier counterparts.

6 For income tax filers aged 51 to 64, the middle class and below were nearly twice as generous as the upper middle class and the middle rich. The former donated 1.22 percent of asset wealth to charity versus 0.72 percent by their wealthier counterparts.

7 The IRS estimates the annual “tax gap” at $312 billion to $353 billion in undeclared income.

8 Warren Buffett, quoted in “Should You Leave It All to the Children?” Fortune (Sept. 29, 1968).

9 Users can alter PrudentPal’s returns, which are initially defaulted at 9.29 percent total return for common stocks, 5 percent interest income for taxable bonds, 4.9 percent interest income for tax-exempt bonds, and a total return of 17.3 percent for other private investments (investment real estate, stakes in private businesses, professional partnerships, collectibles, etc.).