

Effects of Limiting Charitable Deductions on Nonprofit Finances

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Talking Points

- Why elasticity matters: the Treasury Efficiency standard
- Effects on nonprofits
 - Patterns of giving by income
 - Changes in after-tax cost of giving among different income groups
 - Importance of contributions to nonprofit organizations
- Effects of some proposals
 - 28% cap on rate for itemized deductions
 - Allowing charitable deductions in excess of 1% of AGI
 - Limiting all itemized deductions to 2% of AGI
 - Including charitable deduction
 - Exempting charitable deduction

Why Elasticity Matters: Treasury Efficiency

- Magnitude of the elasticity matters from a purely welfare-economic standpoint (Saez, Bakija).
- Practical aspect
 - If the elasticity is 1.0 (absolute value) or more, then revenue foregone by allowing contributions to be deducted is “matched” by commensurate increase in contributions to nonprofits
 - If the elasticity is less than 1.0 (absolute value), then allowing contributions to be deducted may increase contributions, but by less than the fiscal cost of the tax incentive.
 - Relevance for tax policy: The higher the elasticity, the larger the potential impact of limiting the charitable deduction will be for charities as well as for donors

The Composition of Giving

- Conditional on the value of the elasticity of giving, two factors will affect the impact of proposals to scale back the deduction within the nonprofit sector
 - The composition of giving by different income groups
 - The relative importance of individual contributions as a source of revenue for nonprofit organizations.

Composition of Giving

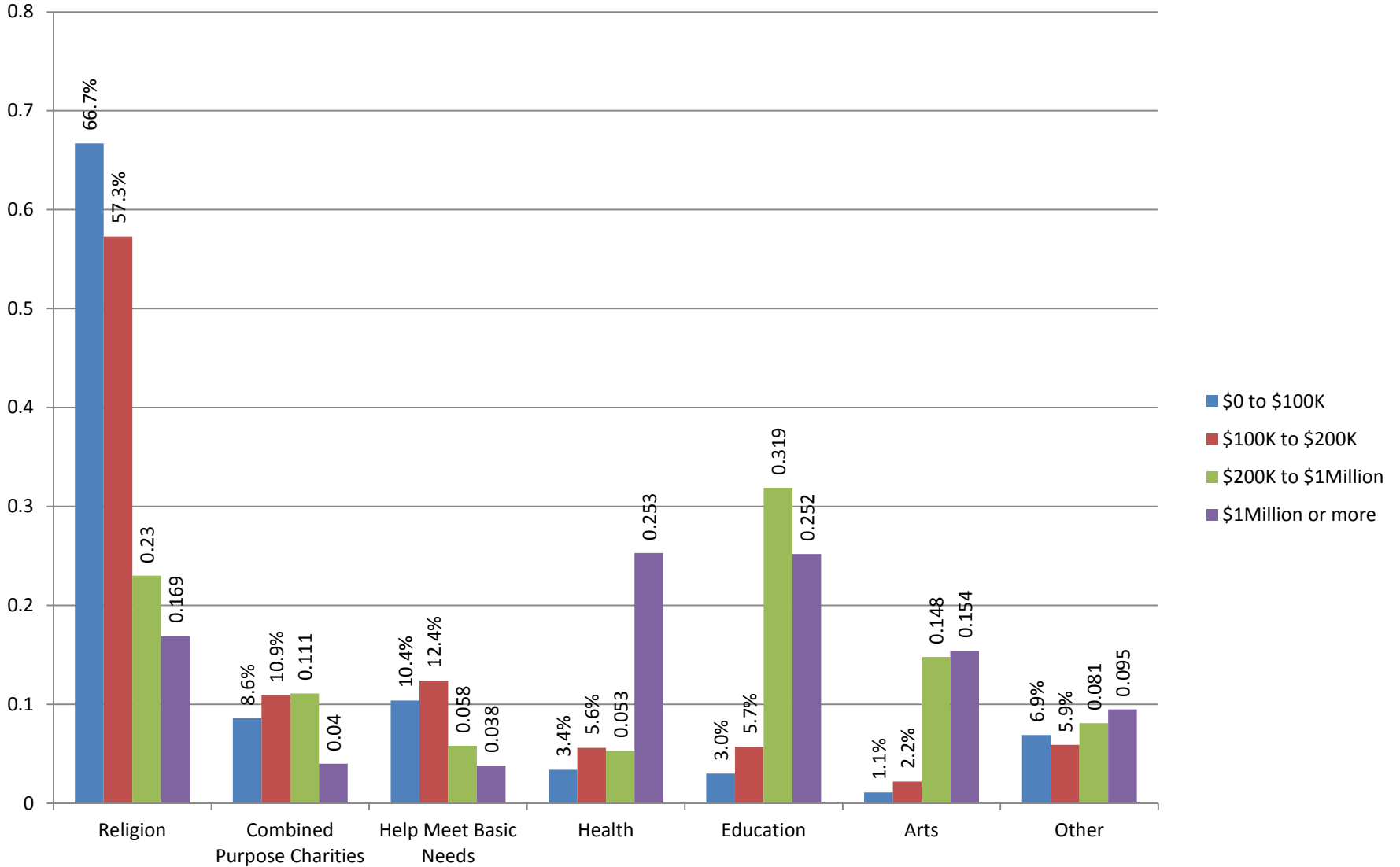
- Proposal to impose a 28% deduction cap increases the after-tax cost of giving proportionately more for higher income givers than for lower income givers.
- Implication: charities relatively favored by higher income givers (health, education, arts) would also be expected to experience relatively larger declines in individual contributions.

Charitable Deduction Reform Option: Limit Tax Benefit to 28%

Income Percentile	Tax Subsidy					Percent Change in Individual Giving	
	Baseline	Low Response		High Response		Low Response	High Response
	Amount (\$ millions)	Change (\$ millions)	Percent Change	Change (\$ millions)	Percent Change		
Lowest Quintile	18	0	0.0	0	0.0	0.0	0.0
Second Quintile	379	0	0.0	0	0.0	0.0	0.0
Middle Quintile	1,895	-1	0.0	-1	0.0	0.0	0.0
Fourth Quintile	5,079	-2	0.0	-2	0.0	0.0	0.0
Top Quintile	34,960	-5,895	-16.9	-6,859	-19.6	-3.5	-6.7
All	42,331	-5,898	-13.9	-6,862	-16.2	-2.2	-4.1
Addendum							
80-90	5,218	-1	0.0	-1	0.0	0.0	0.0
90-95	4,625	-5	-0.1	-5	-0.1	0.0	0.0
95-99	8,090	-552	-6.8	-634	-7.8	-1.1	-2.2
Top 1 Percent	17,027	-5,337	-31.3	-6,219	-36.5	-7.7	-14.7

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0412-8). Changes are estimated relative to a post-ATRA baseline.

Giving Patterns by Income Group



Relative Importance of Contributions as a Source of Nonprofit Revenue

- Effect of reduction in individual contributions on the finances of nonprofit organizations depends on the relative importance of contributions as a source of revenue for nonprofits
- Often stated that contributions are “not a major source” of nonprofit sector finances
 - For the sector as a whole, the ratio of total contributions to total revenue is on the order of 12%
- Aggregate statistic masks wide range of variation in reliance on contributions within the sector.

Relative Importance of Contributions as a Source of Nonprofit Sector Finance

- Data from the Digitized Data base of nonprofit organizations maintained by National Center on Charitable Statistics can be used to gauge at least “rough orders of magnitude” of the importance of contributions to individual nonprofits
- Data allow one to calculate the ratio of contributions to nonprofit revenue for each of some 200 thousand nonprofit organizations in the NCCS data base
 - Average of individual ratios is on the order of 25% of total revenue
 - Varies:
 - By type of nonprofit activity
 - Hospitals (average of 2.0% of revenue)
 - Higher Education (average of 14% of total revenue)
 - Human Services (average of 21% of total revenue)
 - Community improvement (average of 33% of total revenue)
 - By Size (next slide)

Relative Importance of Contributions By Size of Nonprofit

		Share of Total Contributions (%)	Contributions as a % of Total Revenue			% Change in Revenue from a 10% Drop in Contributions		
Size (Total Revenue)	Number		Mean	Lower Quartile	Upper Quartile	mean	Lower Quartile	Upper Quartile
< \$25K	14,746	0.1	17.3	7.0	25.7	1.7	0.7	2.6
\$25K to \$100K	72,069	2.0	28.9	9.1	41.2	2.9	0.9	4.1
\$100K to \$500K	67,784	8.0	28.7	0.6	43.8	2.9	0.1	4.4
\$500K to \$1M	22,839	7.4	23.3	4.6	25.8	2.3	0.5	2.6
\$1M to \$10M	22,741	33.3	22.1	0.1	43.4	2.2	0.0	4.3
> \$10M	7,466	49.1	4.5	0.7	14.0	0.4	0.7	1.4

Implications for Nonprofits

- For many nonprofits, impact of some proposals perhaps “manageable” if painful.
 - 28% deduction cap
 - Deduction floor
 - Cap on total itemized deductions, excluding charitable
- Impact of other proposals more significant.
 - Cap on all itemized deductions (including charitable)
- But even in case where total effects are modest
 - also depends on role of contributions at the margin
 - Impact on some nonprofits of reduction in revenue sources from government grants, contracts etc.

Charitable Deduction Reform Option: Impose 1% AGI Floor

Income Percentile	Tax Subsidy					Percent Change in Individual Giving	
	Baseline	Low Response		High Response		Low Response	High Response
	Amount (\$ millions)	Change (\$ millions)	Percent Change	Change (\$ millions)	Percent Change		
Lowest Quintile	18	-2	-9.4	-2	-9.4	0.0	0.0
Second Quintile	379	-74	-19.7	-75	-19.7	-0.1	-0.1
Middle Quintile	1,895	-478	-25.2	-481	-25.4	-0.2	-0.4
Fourth Quintile	5,079	-1,473	-29.0	-1,488	-29.3	-0.5	-1.0
Top Quintile	34,960	-7,924	-22.7	-8,150	-23.3	-1.1	-2.0
All	42,331	-9,952	-23.5	-10,196	-24.1	-0.8	-1.5
Addendum							
80-90	5,218	-1,684	-32.3	-1,710	-32.8	-0.9	-1.7
90-95	4,625	-1,427	-30.9	-1,451	-31.4	-1.0	-1.7
95-99	8,090	-2,655	-32.8	-2,711	-33.5	-1.4	-2.4
Top 1 Percent	17,027	-2,158	-12.7	-2,278	-13.4	-1.2	-2.0

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0412-8). Changes are estimated relative to a post-ATRA baseline.

**Charitable Deduction Reform Option: Limit Benefit of all Itemized
Deductions Other than the Charitable Deduction to 2% of AGI**

Income Percentile	Tax Subsidy					Percent Change in Individual Giving	
	Baseline	Low Response		High Response		Low Response	High Response
	Amount (\$ millions)	Change (\$ millions)	Percent Change	Change (\$ millions)	Percent Change		
Lowest Quintile	18	-6	-35.7	-6	-35.7	-0.1	-0.1
Second Quintile	379	-149	-39.4	-150	-39.7	-0.8	-1.3
Middle Quintile	1,895	-626	-33.0	-639	-33.7	-1.6	-2.6
Fourth Quintile	5,079	-1,095	-21.6	-1,127	-22.2	-1.5	-2.3
Top Quintile	34,960	-2,432	-7.0	-2,692	-7.7	-1.8	-2.7
All	42,331	-4,308	-10.2	-4,614	-10.9	-1.6	-2.5
Addendum							
80-90	5,218	-1,107	-21.2	-1,164	-22.3	-2.2	-3.6
90-95	4,625	-522	-11.3	-543	-11.7	-1.4	-1.9
95-99	8,090	-2,099	-25.9	-2,240	-27.7	-3.8	-6.0
Top 1 Percent	17,027	1,296	7.6	1,255	7.4	-0.8	-1.0

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0412-8). Changes are estimated relative to a post-ATRA baseline.

Charitable Deduction Reform Option: Limit Benefit of all Itemized Deductions to 2% of AGI

Income Percentile	Tax Subsidy					Percent Change in Individual Giving	
	Baseline	Low Response		High Response		Low Response	High Response
	Amount (\$ millions)	Change (\$ millions)	Percent Change	Change (\$ millions)	Percent Change		
Lowest Quintile	18	-9	-51.0	-9	-51.1	-0.2	-0.4
Second Quintile	379	-291	-76.9	-293	-77.3	-1.7	-3.3
Middle Quintile	1,895	-1,624	-85.7	-1,636	-86.3	-4.5	-8.6
Fourth Quintile	5,079	-4,458	-87.8	-4,500	-88.6	-7.0	-13.3
Top Quintile	34,960	-29,088	-83.2	-29,944	-85.7	-14.4	-26.1
All	42,331	-35,471	-83.8	-36,382	-85.9	-10.8	-19.8
Addendum							
80-90	5,218	-4,347	-83.3	-4,432	-84.9	-10.0	-18.8
90-95	4,625	-4,083	-88.3	-4,146	-89.7	-12.0	-22.3
95-99	8,090	-7,049	-87.1	-7,204	-89.1	-15.3	-28.0
Top 1 Percent	17,027	-13,610	-79.9	-14,162	-83.2	-16.9	-30.4

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0412-8). Changes are estimated relative to a post-ATRA baseline.