

# The Charitable Deduction: A View from the Other Side of the Cliff

Joseph Rosenberg  
Urban-Brookings Tax Policy Center

February 28, 2013

Urban Institute  
Washington, DC



# Charitable Deduction: Overview

## Charitable Income Tax Deduction:

- Annual revenue cost to federal government ( $\sim$ \$40b/yr)

**Charitable Deduction Tax Expenditure, 2012 - 2017**  
(billions of current dollars)

2012	2013	2014	2015	2016	2017
36.2	39.0	43.6	45.1	47.1	49.4

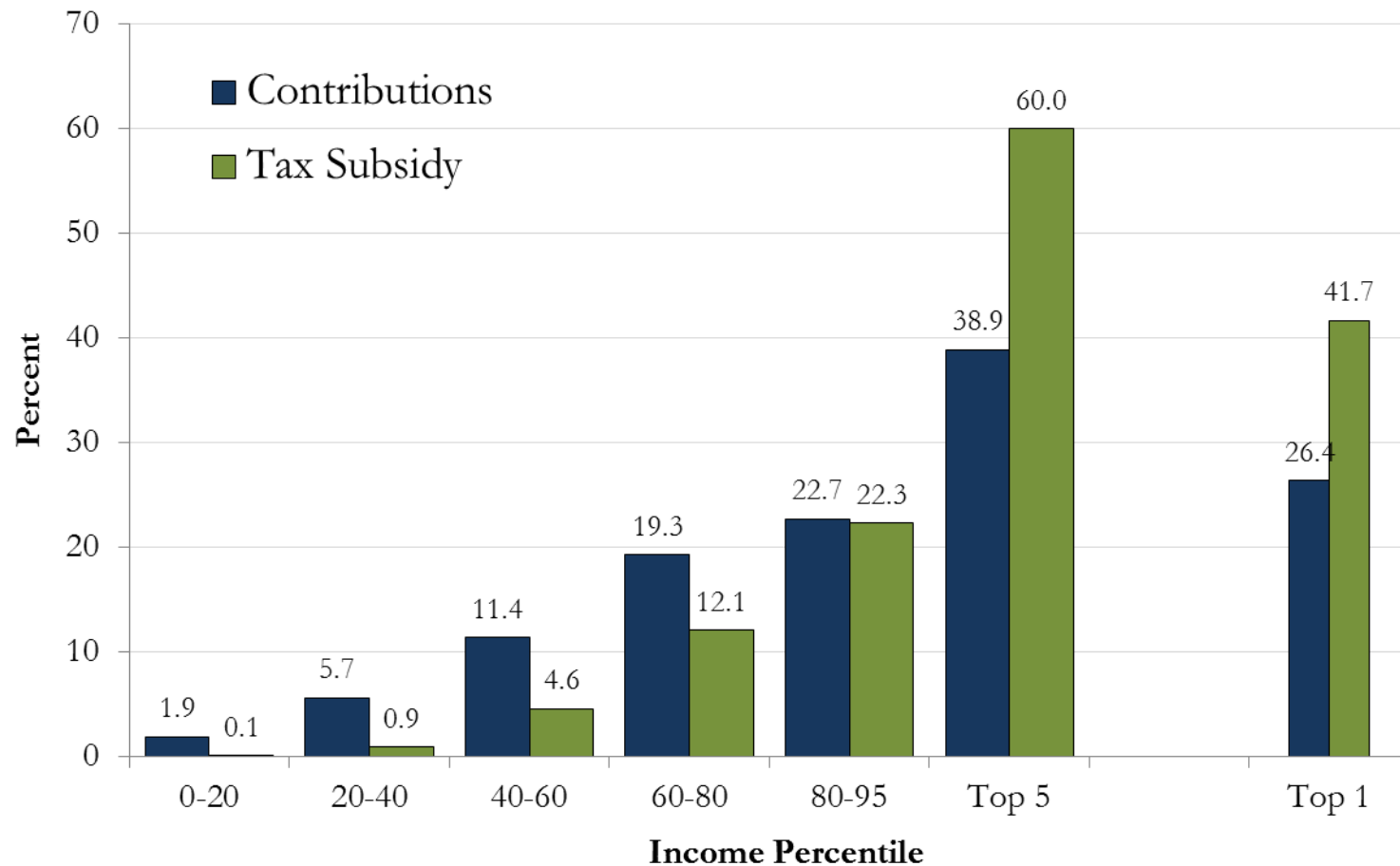
Source: Joint Committee on Taxation (JCS-1-13)

- Itemized deduction ( $\sim$ 30% of taxpayers)
- “Upside-down” subsidy: tax benefit increases with marginal tax rate



# Charitable Deduction: Distribution by Income

## Shares of Contributions and Tax Subsidies by Income Group, 2013



# Composition of Itemized Deductions

## Composition of Itemized Deductions by AGI, 2010

Adjusted Gross Income	Number of Itemized Returns (thousands)	Total Itemized Deductions (\$ billion)	Share of Total Itemized Deductions			
			Taxes Paid	Interest Paid	Charitable Contributions	Other
Under \$50K	13,392	211	22.9	35.4	9.5	32.2
\$50K under \$100K	17,258	337	31.2	40.0	11.8	16.9
\$100K under \$200K	11,874	329	39.1	38.6	12.5	9.8
\$200K under \$500K	3,317	164	45.9	32.2	14.1	7.7
\$500K under \$1M	528	54	51.1	22.3	17.5	9.0
\$1M under \$5M	246	61	53.7	13.1	21.9	11.4
\$5M or more	28	60	44.5	9.0	38.3	8.2
Total	46,645	1,217	36.6	34.1	14.0	15.3

Source: IRS, Statistics of Income. "Individual Income Tax Returns," Table 2.1.



# A Prelude to a Cliff: Tax Expenditure Limits

## “Sequestering” tax expenditures:

- Across-the-board reductions in itemized deductions and other tax expenditures
  - Obama’s 28 percent limit
  - Romney’s \$17K (or \$25K or \$50K) cap
  - Feldstein’s 2% income limit
- Appealing for political reasons, appears simple, avoids singling out individual preferences
- Significant revenue potential and can be distributed quite progressively



## TE Limits & the Charitable Deduction

- Not a “loophole”
- Reducing subsidy at the margin is the wrong policy if the goal of the deduction is to encourage giving
  - Design matters: Some proposals would effectively eliminate the marginal incentive for large donors
- Can “protect” charitable deduction (e.g., “Buffett rule”, Feldstein 2.0), but:
  - Undermines one of the stated advantages of the broad limits
  - Potential for significant indirect effects if changes are made to other itemized deductions



# A Prelude to a Cliff: Tax Expenditure Limits (cont.)

## Deductible Charitable Contributions by Cash Income Level, 2013

Cash Income	Deductible Charitable Contributions (\$ millions)	Charitable Contribution Deduction in Excess of:			
		\$50,000		\$50,000 Less All Other Itemized Deductions	
		Amount (\$ millions)	Percent of Contributions	Amount (\$ millions)	Percent of Contributions
Less than 10	0	0	0.0	0	0.0
10-20	452	0	0.0	0	0.1
20-30	1,322	0	0.0	4	0.3
30-40	3,031	0	0.0	7	0.2
40-50	4,616	0	0.0	9	0.2
50-75	17,911	1	0.0	165	0.9
75-100	19,487	0	0.0	337	1.7
100-200	51,141	103	0.2	2,313	4.5
200-500	28,062	1,577	5.6	9,178	32.7
500-1,000	10,701	2,679	25.0	8,493	79.4
More than 1,000	43,691	34,801	79.7	43,052	98.5
All	180,414	39,162	21.7	63,558	35.2
<b>Addendum<sup>4</sup></b>					
AGI above \$250K	67,391	38,565	57.2	57,024	84.6
AGI above \$500K	51,084	36,602	71.7	49,036	96.0
AGI above \$1m	41,320	33,678	81.5	40,843	98.8

Source: Urban-Brookings Tax Policy Center Microsimulation Model (version 0412-7).



# American Taxpayer Relief Act of 2012 (cont.)

Overall, ATRA increased tax incentives for charitable giving (relative to prior tax rules)

- Higher marginal tax rate (35% → 39.6%)
  - Lowers after-tax price of giving (7% decrease) for taxpayers in the top tax bracket.
- Pease (overall limit on itemized deductions)
  - In general, no effect on marginal giving incentives. Since Pease liability is based on AGI, it operates as an income surtax on itemizers.
  - Very few taxpayers up against 80% limit (TPC: 44,000 taxpayers)
  - However, creates differential b/t rate at which income is taxed and rate at which contributions are deducted.

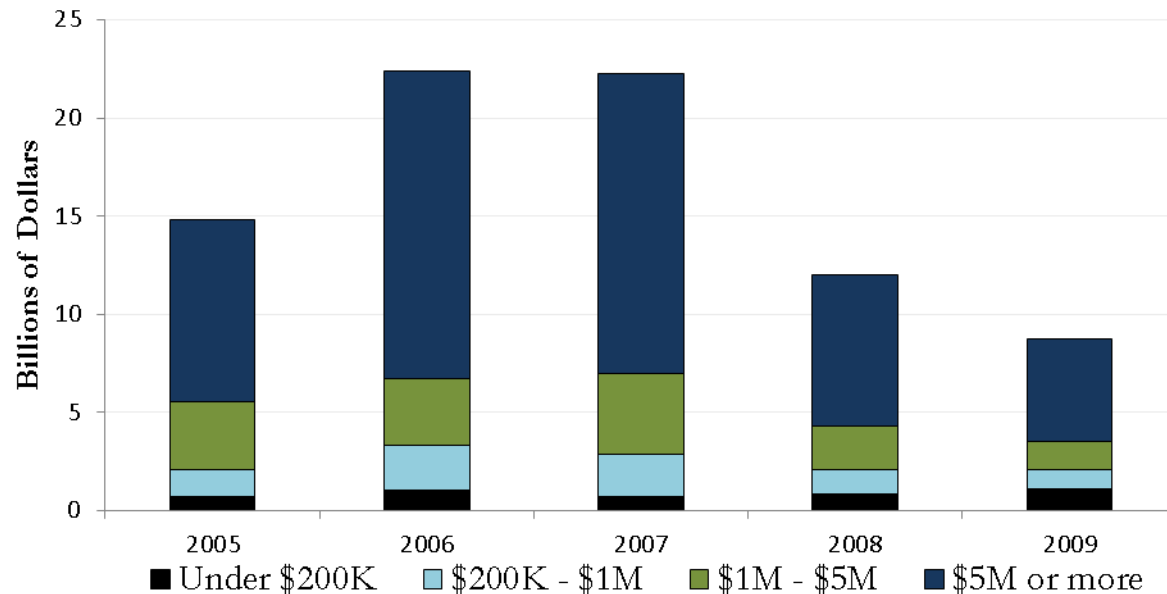




# American Taxpayer Relief Act of 2012 (cont.)

- Higher capital gains tax rate increases subsidy for donations of appreciated property (i.e., stocks)

Donations of Corporate Stock & Other Investments, Amount Deducted in Excess of Donor Cost, 2005-2009



Source: IRS, Statistics of Income.



# Fiscal Cliff: What did we learn?

- Broad tax expenditure limits will resurface
  - Future revenue increases are now more likely to occur through base broadening than via marginal rates
- Better path forward is to pursue targeted incremental reforms
- Suggestions for the charitable deduction
  - Expand to all taxpayers (i.e., move “between-the-line”)
  - Impose floor (e.g., 1% of AGI)
  - Subsidy rate? I will boldly punt to the next panel.

