2008

Tax Reform and Charitable Giving

Seth H. Giertz
University of Nebraska-Lincoln, sgiertz2@unl.edu

National Tax Association 2007 100th Annual Conference Proceedings, (2008).

TAX REFORM AND CHARITABLE GIVING*

Seth H. Giertz, Congressional Budget Office

INTRODUCTION

OF THE $240.7 BILLION DONATED TO U.S. charities in 2003, 75 percent was from individuals.[1] Of that total, $145.7 billion was taken as itemized deductions on federal income tax returns. In addition, non-itemizers and non-filers contributed $33.0 billion – contributions that received no special tax treatment.[2] Under current law, only taxpayers who itemize may deduct from Adjusted Gross Income (AGI) their charitable donations in determining taxable income. In recent years, a number of different proposals have been put forth that would alter the tax treatment of giving by individuals. Some plans would extend a variant of the charitable deduction to non-itemizers (see CBO, 2002, 2007). Other plans — some components of fundamental tax reform — would make changes such as imposing floors (or minimum levels of giving) that must be met before deductions are permitted or replacing the deduction with a nonrefundable tax credit.

The proposed changes are often motivated by equity or efficiency concerns. Some argue that the current system is inequitable because it favors high-income filers over other income groups who give. In terms of efficiency, tax incentives for giving could be restructured so as to yield the same or more donations, while costing the government less in foregone tax revenue.

RECENT PATTERNS OF CHARITABLE GIVING

This paper uses Statistics of Income (SOI) data for 2003 in conjunction with data from the Panel Study of Income Dynamics (PSID) to examine patterns of giving across the income distribution. Estimates are reported for giving and broken down by filing status (i.e., itemizers versus non-itemizers) and income group. Also examined are the recipients of those donations (i.e., the types of organizations receiving the donations) and at what rates people in different income groups give to those different types of organizations. Additionally, the cost to the federal government from allowing charitable deductions is estimated along with the degree to which different income groups benefit from the deduction. All of those measures represent the baseline for the succeeding section, which analyzes the effect of possible tax changes on each of those measures.

Donations by Individuals

According to *Giving USA*, U.S. charities received $240.7 billion in donations (2.2 percent of gross domestic product) in 2003. Of that, I estimate that $179.6 billion (1.6 percent of GDP), or nearly 75 percent, was donated by individuals. The other 25 percent was donated by foundations, corporations, and estates (bequests). From the mid 1960s to the mid 1990s, individual giving rose steadily, even after accounting for inflation. From the mid 1990s to 2000, individual giving increased sharply, by over 50 percent in just five years. That growth was likely closely tied to the stock market, which has historically been a good predictor of giving. With the stock markets decline, individual giving fell by 4 percent in 2001 and stagnated through 2003 before increasing by over 10 percent from 2003 to 2005.

Of the estimated $179.6 billion in individual donations for 2003, $145.7 billion was donated by itemizers; $31.8 billion was donated by non-itemizing filers and $2 billion came from non-filers.[3] Of all itemizers, 88 percent reported charitable donations; that number was 52 percent for non-itemizing filers. Giving is skewed towards those with the highest incomes. The 24 percent of itemizers with reported AGI exceeding $100,000 were responsible for 54 percent of all itemizer giving. As a share of income, giving is relatively stable for most of the income distribution, at about 2.5 percent of AGI. For those reporting more than $5 million in AGI, giving rates are often 4 percent or higher.[4]

Cost to the Government from Charitable Deductions

The cost to the government of the charitable deduction, as measured by foregone tax revenues, is referred to as a tax expenditure. The size of the tax expenditure is not self-evident from the total

*I would like to thank Tom Woodward, Ed Harris and David Weiner for helpful comment and assistance with the data. Any views expressed are those of the author and should not be interpreted as those of the Congressional Budget Office.

dollars donated or deducted because the tax rate that would have applied to the income had it not been donated varies greatly across individuals – and the marginal rate can even vary for the same individual, depending on how much he donates. Tax expenditures can be calculated using effective tax rates in conjunction with the amount donated.[5] The effective tax rates are the tax rates that the income would have faced had it not been donated. Effective tax rates are often different from the statutory rates for a variety of reasons, including phaseouts and phaseins and the alternative minimum tax. Federal effective tax rates for returns in the SOI are imputed using CBO's tax calculator. Overall effective tax rates would also include state and local taxes. However, those are omitted here because the focus is on the cost to the federal government.

Charitable deductions are one of the tax codes largest tax expenditures – although substantially smaller than tax expenditures for health care, housing, and retirement savings. I estimate that for 2003, federal tax expenditures associated with the charitable deduction totaled $29.8 billion. That tax expenditure is attributable solely to itemizers since donations by non-itemizers were not deducted and thus subject to tax. Tax expenditures are even more concentrated among high-income filers than are donations. For example, those itemizers reporting more than $100,000 in AGI received 70 percent, or $20.8 billion, of total tax expenditures for charitable contributions.

Recipients of Donations

It is not clear from tax return data the degree to which different types of organizations benefited from individual donations.[6] However, the Center on Philanthropy Panel Study (COPPS) module of the PSID does ask respondents questions on the amount of donations and the types of organizations that receive their donations. Like the SOI, the PSID is a stratified random sample of U.S. residents. The PSID is a much smaller sample and includes especially few respondents from the very top of the income distribution. According to the PSID, in 2002, 63.4 percent of the value of individual donations were made to religious organizations; 4.8 percent of the value of donations were to education; 10.3 percent to the needy; and, 4.2 percent to health, see Table 1.[7] While many think of charity as primarily benefiting the poor, the Center on Philanthropy estimates at least 69 percent of total giving is not directed to the poor.[8]

Table 1
Charitable Donations by Income Group and Recipient Category for 2003

2002		*Average*		*"Percentage (Giving/ Income)"*	*Average Giving*		*Percentage*							*Percentage Itemizers*	*Percentage of All Giving*
	Obs	*Income*	*Giving*		*Itemizers*	*Non-Itemizers*	*Religion*	*Education*	*Needy*	*Health*	*Youth*	*Culture*	*Community & Environ.*		
Less than $0	8,623	-440	385	—	1,143	192	66.3	4.6	8.1	7.0	0.8	0.9	1.1	20.3	2.2
$0 to $10k	20,395	3,280	737	22.5	1,955	440	72.5	1.1	9.7	3.4	0.8	0.8	2.7	19.6	9.9
$10k to $20k	12,319	15,204	522	3.4	1,594	249	74.3	2.1	7.0	2.6	2.1	1.5	1.0	20.3	4.3
$20k to $30k	13,028	25,315	661	2.6	1,654	328	62.3	7.2	8.5	2.6	2.4	1.9	1.6	25.1	5.7
$30k to $40k	11,414	34,868	697	2.0	949	586	54.4	2.5	13.9	5.0	2.9	0.8	2.0	30.7	5.3
$40k to $50k	9,788	45,053	1,168	2.6	1,849	609	72.3	2.2	8.9	3.5	1.4	1.0	1.3	45.0	7.6
$50k to $75k	17,150	61,866	1,501	2.4	2,009	678	71.7	3.2	9.1	3.2	1.2	1.0	0.9	61.8	17.0
$75k to $100k	10,559	86,559	2,110	2.4	2,550	997	68.6	3.6	11.8	2.2	2.3	0.7	1.5	71.7	14.7
$100k to $200k	12,695	131,550	2,546	1.9	2,701	1,714	54.4	6.1	12.1	6.0	1.5	2.5	2.1	84.3	21.4
$200k or more	2,789	368,886	6,456	1.8	6,963	2,903	48.3	12.2	8.8	6.7	1.9	1.2	1.2	87.5	11.9
total	118,761	51,306	1,273	2.5	2,310	499	63.4	4.8	10.2	4.2	1.7	1.3	1.6	42.7	100.0

Source: Author's calculations based on PSID data.

OPTIONS FOR REFORM

How tax incentives for giving are structured can have a major impact on the costs to the federal government, the level of charitable giving, and which (or how many) taxpayers benefit. Three important decisions are made in crafting each of the policy alternatives examined here. Decisions are made as to whether the tax benefit should: (1) take the form of a deduction or a credit; (2) include non-itemizers, or be restricted to itemizers; (3) include a floor (minimum level of donations) below which contributions are not subsidized.

Six Plans for Reform

Six different plans for reform are examined (see Table 2). The first reform would make the charitable deduction above-the-line (i.e., available to both itemizers and non-itemizers). The second and third options would turn the charitable deduction into a nonrefundable tax credit. In one case, the option would include a dollar floor. In the other case, there would be no floor. The fourth case would only allow deductions for itemizers donating more than a $500 floor if single (and $1,000 for joint returns). The fifth and sixth cases would impose a floor equal to 1 percent of AGI. In one case, donations exceeding 1 percent of AGI could be deducted only for itemizers. In the other case, all filers could deduct donations exceeding 1 percent of AGI.

The first plan would *make charitable deductions above-the-line*; thus, the same rules that now apply to itemizers would be extended to non-itemizers – allowing non-itemizers to subtract from AGI all of their charitable contributions (subject to the same restrictions as itemizers), in addition to the standard deduction. Under this scenario, taxpayers can be expected to respond in several ways. Because, non-itemizers would be treated more favorably than under current law while the tax treatment of itemizers would not change, some itemizers would be expected to switch to non-itemizers. Put another way, since the tax treatment of charitable contributions would now be identical for itemizers and non-itemizers, charitable giving would no longer play a role in deciding whether to itemize. Thus, itemizers whose itemized deductions minus charitable deductions are less than the standard deduction would benefit from switching to non-itemizers. Those switching would not be expected to alter their giving, however, since their after-tax price of giving does not change.[9] The only group whose giving might be expected to respond is non-itemizers with positive tax liabilities, since their after-tax price of giving would fall. For that group, the price per dollar of giving would fall (from $1) by the size of their marginal tax rate.[10]

The second and third plans would *replace the current deduction with an above-the-line nonrefundable tax credit*. The tax credit would equal 25 percent of allowable donations. Two variations of this plan are analyzed. One would not impose a floor on allowable contributions, while the other would only credit contributions exceeding $500 for singles ($1,000 for joint returns). Here, taxpayers can be expected to respond in several ways. Again, charitable giving will not influence the decision to itemize because any tax savings from charitable giving are the same independent of that decision. Thus, current itemizers whose allowable itemized deductions minus charitable deductions are

Table 2

Policy Alternatives	*Non-itemizers Eligible*	*Floor for Eligible Donations*	*Credit or Deduction*	*Donations*[a]	*Cost*[a]
Current Law	No	No	Deduction	$177.5b	$29.8b
1	Yes	No	Deduction	≈	↑
2	Yes	No	Credit	↑	↑
3	Yes	$500/$1000	Credit	↑	↑
4	No	$500/$1000	Deduction	≈	↓
5	No	0.01×AGI	Deduction	≈	↓
6	Yes	0.01×AGI	Deduction	≈	↓

[a] The column reflects estimates assuming moderate behavioral responses. For the six plans, estimates reflect changes from current law. ≈ implies a change of less than one-half of 1 percent. ↑ or ↓ implies an increase or decrease of more than 5 percent – with respect to cost, estimated changes are all in excess of 15 percent.

Source: Congressional Budget Office

less than the standard deduction would no longer choose to itemize.

With no floor, the after-tax price of donating would rise for itemizers facing marginal tax rates greater than 25 percent. For itemizers facing marginal tax rates of less than 25 percent, the after-tax price would fall. Donating non-itemizers (with tax liabilities) would all face more favorable tax treatment under this plan. The net effect on giving depends on whether the increased giving by those whose after-tax price of giving falls exceeds the decrease in giving by those for whom the after-tax price rises. With the dollar floor, the after-tax price for the next dollar of giving would fall only for itemizers giving more than the floor who also face marginal tax rates of less than 25 percent and for non-itemizers giving more than the floor.

The fourth plan would *only allow deductions by itemizers that exceed a fixed dollar floor* of $500 for individuals and $1,000 for joint filers. That change should not affect non-itemizers, since the charitable deduction would not be extended to them. The benefits to itemizers would be less generous than under current law; thus, some itemizers would switch to non-itemizers.[11] Under this scenario, no filer would have an increased incentive to donate; however, many filers after-tax price on the last dollar of giving would remain unchanged. That would be true for all non-itemizers and for those who remain itemizers and donate more than $500 if single ($1,000 if filing jointly).

The fifth and sixth plans would *allow deductions only for total contributions exceeding 1 percent of AGI*. Two variations of this plan are analyzed. One would extend the deduction to all tax filers, while the other would continue to restrict deductions to itemizers.

Plan 5, allowing deductions for giving that exceeds 1 percent of AGI only for itemizers, would have similar implications as plan 4. To wit, the change would not affect non-itemizers and would make benefits to itemizers less generous than current law. Thus, some itemizers would switch to non-itemizers.[12] In contrast to plan 4, the floor for this alternative would be proportional to AGI and thus would be larger (than the fixed dollar floor) for very high-income filers. That could result in more filers switching to non-itemizer status and may also do more to lessen costs.

Allowing deductions for giving by both itemizers and non-itemizers that exceed 1 percent of AGI, as in plan 6, would reduce the benefits from itemizing in absolute terms and relative to not itemizing. The tax treatment of individual giving in that plan is very similar to that favored by the 2005 President's Advisory Panel on Federal Tax Reform. As with the other above-the-line scenarios, charitable giving would no longer play a role in the decision to itemize – since the tax benefits from giving are independent of that decision. Itemizers whose itemized deductions minus charitable deductions are now less than the standard deduction would no longer choose to itemize. Those itemizers giving less than 1 percent of AGI would have an incentive to give less because their after-tax price of giving would rise. For itemizers giving more than 1 percent of AGI, the after-tax price of giving another dollar would remain unchanged, although the average after-tax price of giving would rise. For non-itemizers giving less than 1 percent of AGI, the after-tax price of giving would remain unchanged. For itemizers giving more than 1 percent, the after-tax price would fall, providing an incentive for those people to increase their giving.

Findings

An important caveat is in order to remind the reader that the measures of tax expenditures used in this analysis, while they superficially resemble revenue estimates, are not the same thing. Revenue estimates for specific legislation are the responsibility of the Joint Committee on Taxation. The analyses here are purposely stylized to ignore many of the specific features that would be critical to an official revenue estimate. The purpose of this analysis is to focus on the salient characteristics of the broad approaches to changing the tax treatment of charitable contributions.

From the analysis emerge several stylized facts (see Table 3). First, allowing above-the-line deductions greatly increases the number of taxpayers who benefit from the tax incentive, but has little effect on donations and greatly increases costs to the government. Second, moving from a deduction to a 25 percent nonrefundable credit does the most of the six alternatives to increase donations, but that policy would also substantially increase costs.[13] Third, imposing floors, below which contributions are not subsidized, considerably lowers costs, while only nominally affecting contributions.

Overall donations across the six plans are very close to (2003) donations under current law (see Figure 1). The 25 percent credit used for plans 2 and 3 raises donations by roughly 6.5 percent.

Table 3

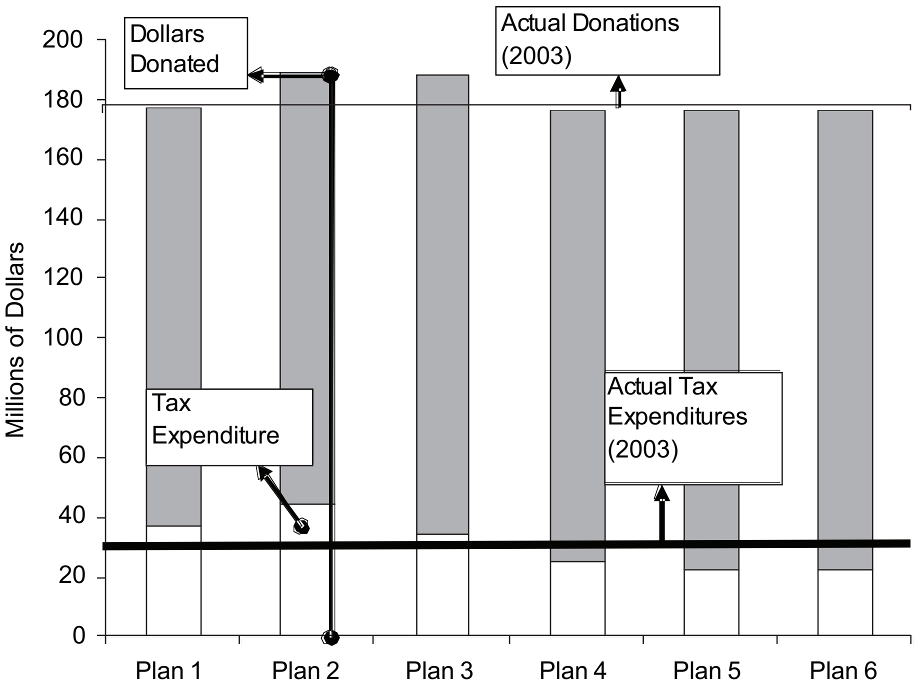
Proposals Under Various Elasticity Assumptions

		All Filers			Itemizers			Non-Itemizers			
	Elasticity	Dollars Donated	Tax Expenditure	Beneficiaries	Returns	Dollars Donated	Tax Expenditure	Dollars Donated	Tax Expenditure	Tax Expenditure Per Dollar Donated	% change in costs
		177.5	29.8	35.2	38.6	145.7	29.8	31.8	0.0	$0.17	
Estimated changes relative to the 2003 "baseline."											
Proposal 1: Above-the-Line											
	0	0.0	7.17	35.6	-5.4	-33.4	-4.3	33.4	11.5	$0.21	24.0
	-0.5	0.1	7.18		0.0	-33.4	-4.3	33.5	11.5	$0.21	24.1
	-1.5	0.2	7.22		0.0	-33.4	-4.3	33.6	11.5	$0.21	24.2
Proposals 2 and 3: Above-the-Line Credit											
No Floor	0	0.0	12.4	37.9	-5.4	-33.4	-2.8	33.4	15.2	$0.24	41.7
	-0.5	12.1	15.2		-5.4	-32.6	-2.6	44.7	17.8	$0.24	51.0
	-1.5	36.4	20.7		-5.4	-31.0	-2.4	67.4	23.1	$0.24	69.5
Dollar Floor	0	0.0	2.5	2.6	-5.4	-33.4	-8.0	33.4	10.6	$0.18	8.5
	-0.5	11.3	5.2		-5.4	-32.7	-7.9	44.1	13.1	$0.19	17.3
	-1.5	34.0	10.4		-5.4	-31.5	-7.7	65.4	18.1	$0.19	34.8
Proposal 4: Below-the-Line Deduction with Dollar Floor											
	0	0.0	-4.6	-11.7	-2.2	-3.5	-4.6	3.5	0.0	$0.14	-15.3
	-0.5	-0.3			0.0	-3.6	-4.6	3.2	0.0	$0.14	-15.3
	-1.5	-0.9			0.0	-3.8	-4.6	2.8	0.0	$0.14	-15.3
Proposals 5 and 6: Deduction with Percent Floor											
Below-the-Line	0	0.0	-6.9	-10.5	-1.5	-2.6	-6.9	2.6	0.0	$0.13	-23.2
	-0.5	-0.7			0.0	-3.1	-6.9	2.6	0.0	$0.13	-23.2
	-1.5	-2.0			0.0	-4.0	-6.9	2.0	0.0	$0.13	-23.2
Above-the-Line	0	0.0	-6.8	-9.4	-5.4	-33.4	-11.0	33.4	4.2	$0.13	-22.8
	-0.5	-0.4			-5.4	-33.9	-11.0	33.4	4.2	$0.17	-22.8
	-1.5	-1.2			-5.4	-34.8	-11.0	33.6	4.2	$0.17	-22.8

Dollars values are in billions, unless otherwise indicated.
The total number of returns is 129,013,310.
Decreases in the number of itemized returns are exactly offset by increases in the number of non-itemized returns.

Source: Author's calculations based on SOI data.

Figure 1: **Total Donations and Tax Expenditures Across Plans**



Source: Author's calculations.

Total donations from the other plans all change by less than one-half of 1 percent. Changes to tax expenditures are much larger and have a much greater variance. Changes to tax expenditures range from an increase of more than one-half for the 25 percent above-the-line credit (plan 2) to an almost one-quarter drop when imposing a 1 percent of AGI floor (plans 5 and 6).

Another way of evaluating the different plans is to compare how much each plan changes the tax expenditure per dollar of donation. This subsidy rate measure has the virtue of incorporating both costs (foregone tax revenue) and benefits (donations), instead of examining the two separately.[14] Here, the subsidy rate is defined as the average cost in foregone tax revenue per dollar of donations; or, in other words, the ratio of tax expenditures (or foregone tax revenue) to total donations. Based on that measure, plans that impose contribution floors are clearly the most cost-effective, while those that impose no floors and award benefits to both itemizers and non-itemizers are the least cost-effective, see Table 3. While change in the subsidy rate differs greatly across plans, from an increase of $0.07 to a decrease of $0.04, within each plan the elasticity assumptions have almost no affect on the measure.

In general, extending the deduction to non-itemizers increases the number of tax filers benefiting from charitable incentives, but is costly and has little effect on donations. For example, making the current deduction above-the line, and imposing no other changes, increases the number of beneficiaries by 35.2 million, but raises costs to the government by $7.2 billion (or more than 24 percent) and under the most optimistic scenario increases donations by just 0.1 of 1 percent. While costly, the benefits of extending the charitable deduction to non-itemizers tend to benefit middle-income groups. Of the $7.2 billion drop in revenues, 73 percent would go to taxpayers with AGI less than $75,000, while 5 percent would go to those with

AGI greater than $200,000, see Table 4. In terms of the subsidy rate, this plan would raise the average cost per dollar of donations by $0.04 (or 19 percent), from $0.17 to $0.21 per dollar donated. Plans 2, 3, and 6 also include an above-the-line benefit, but those plans also contain other features, which affect the overall results.

It would be possible to reduce the cost of this plan by reducing the size of the standard deduction. Since the latter was intended to encompass some level of charitable giving, pairing a reduction in the standard deduction with an above-the-line benefit could be construed as a reasonable trade-off.

Like plan 1, plans 2 and 3 make no distinction between itemizers and non-itemizers, treating charitable contributions by both groups identically. However, those two plans are different from plan 1 in that they do not offer a deduction but rather a 25 percent credit. The credit considerably increases costs, but results in much more giving.[15] Under plan 2, which imposes no floor, the above-the-line credit would increase costs to the government by between $12.4 billion and $20.7 billion, or between 42 and 70 percent. Changes to giving are highly dependent on the elasticity assumptions, and range from $0 to $36.4 billion. Plan 3 imposes a $500 floor for singles ($1,000 for joint filers), which substantially lowers the cost increase from the above-the-line credit, while maintaining most of the increased donations. Both plans 2 and 3 have higher subsidy rates, as measured by the average revenue cost per dollar donated, than both plan 1 and current law. Plan 2 would raise the average cost per dollar of donations to $0.24, or 41 percent greater than under current law. Because of the dollar floor, plan 3 is much is less costly per dollar of contributions, raising the average cost per dollar donated by 12 percent, or by $0.02 compared to current law.

Under plans 2 and 3, those with AGI less than $75,000 considerably increase their contributions because the 25 percent flat-rate credit is often more generous for them than the current deduction. For those in the top three income tax brackets, the situation is reversed. Those filers would respond by reducing their donations somewhat. The effective subsidy going to those high income filers would fall as well (see Table 5).

For plans 4, 5, and 6, imposing a dollar or percent of AGI floor on the deductibility of donations would lower the annual cost to the government by

Table 4

Allow Non-Itemizers to Deduct Charitable Contributions

Estimated changes compared to the 2003 "baseline" and assuming moderate behavioral responses.

	Plan 1					
	All Filers			*Non-Itemizers*		
Increase in:	*Beneficiaries*	*Dollars Donated*	*Tax Expenditure*	*Returns*	*Dollars Donated*	*Tax Expenditure*
Total	35.6	75.2	7,184	5.4	33,466	11,494
Less than $0	0.0	0.0	0	0.0	0	0
$0 to $10,000	1.0	0.0	66	0.1	259	66
$10,000 to $20,000	7.8	0.5	619	0.4	1,329	654
$20,000 to $30,000	8.5	2.9	1,109	0.6	2,284	1,217
$30,000 to $40,000	6.2	7.6	1,083	0.7	2,564	1,247
$40,000 to $50,000	4.0	10.3	959	0.7	2,943	1,220
$50,000 to $75,000	5.5	19.4	1,438	1.4	7,245	2,142
$75,000 to $100,000	1.7	14.6	901	0.8	4,471	1,503
$100,000 to $200,000	0.7	19.8	625	0.5	4,574	1,452
$200,000 to $500,000	0.1	0	161	0.1	1,692	537
$500,000 to $1,000,000	0	0	58	0.02	881	275
$1,000,000 to $5,000,000	0	0	74	0.01	1,420	391
$5,000,000 to $10,000,000	0	0	16	0.001	541	132
$10,000,000 or more	0	0	74	0.001	3,264	657

Numbers are in millions.

Increases in the number of non-itemizers are exactly offset by decreases in the number of itemizers.

Source: Author's calculations based on SOI data.

Table 5

Replace the Charitable Deduction with an Above-the-Line Nonrefundable Credit

Estimated changes compared to the 2003 "baseline" and assuming moderate behavioral responses.
Above-the-Line Non-Refundable Credit: 25% Rate

	Plan 2: No Floor					*Plan 3: Floor: 500/1000*				
	All Filers			*Non-Itemizers*		*All Filers*			*Non-Itemizers*	
Increase in:	*Beneficiaries*	*Dollars Donated*	*Tax Expenditure*	*Returns*	*Dollars Donated*	*Beneficiaries*	*Dollars Donated*	*Tax Expenditure*	*Returns*	*Dollars Donated*
Total	37.94	12,129	15,204	5.35	44,715	2.63	11,318	5,153	5.35	44,062
Less than $0	0.01	75	2	0.00	75	0.00	71	1	0.00	71
$0 to $10,000	1.14	903	257	0.12	1,109	0.57	832	183	0.12	1,041
$10,000 to $20,000	8.67	2,020	1,847	0.41	3,168	2.44	1,892	1,128	0.41	3,046
$20,000 to $30,000	9.20	2,398	2,812	0.59	4,381	2.37	2,261	1,742	0.59	4,252
$30,000 to $40,000	6.58	2,182	2,813	0.66	4,414	1.36	2,079	1,690	0.66	4,324
$40,000 to $50,000	4.13	1,639	2,322	0.68	4,275	0.44	1,558	1,285	0.68	4,210
$50,000 to $75,000	5.63	2,591	4,267	1.42	9,171	-1.21	2,432	2,035	1.42	9,052
$75,000 to $100,000	1.70	1,244	2,151	0.79	5,271	-1.67	1,172	583	0.79	5,234
$100,000 to $200,000	0.74	385	613	0.54	4,987	-1.49	338	-1,082	0.54	4,970
$200,000 to $500,000	0.11	-557	-904	0.09	1,698	-0.18	-564	-1,320	0.09	1,695
$500,000 to $1,000,000	0.02	-263	-405	0.02	863	-0.01	-264	-481	0.02	863
$1,000,000 to $5,000,000	0.02	-331	-469	0.01	1,405	0.00	-332	-505	0.01	1,404
$5,000,000 to $10,000,000	0.00	-85	-114	0.00	542	0.00	-85	-116	0.00	542
$10,000,000 or more	0.00	-71	12	0.00	3,357	0.00	-71	10	0.00	3,357

Numbers are in millions.
Increases in the number of non-itemizers are exactly offset by decreases in the number of itemizers.

Source: Author's calculations based on SOI data.

between $4.6 billion and $6.9 billion (or between 15 and 23 percent) while reducing donations by no more than $682,000 (or 0.4 percent), see Table 3, Table 6 and Table 7.[16] Under the most extreme assumption, that giving is very responsive to tax incentives, giving would fall by between $939,000 and $2.034 billion (or between 0.5 to 1.1 percent). In terms of tax expenditure per dollar donated, plans 4, 5, and 6 are clearly the lowest. Those plans would lower the cost per dollar donated by 18 to 24 percent, or by $0.03 to $0.04 compared to current law. Most of the cost savings would come from those with AGI greater than $75,000. For plan 4, 68 percent of the gain in revenue would come from those with AGI above $75,000. For plans 5 and 6, that number would be 84 percent.

Some policy alternatives include a combination of characteristics that separately may have opposing effects. For example, plans 3 and 6 would both extend benefits to non-itemizers, while also imposing a floor on charitable deductions. As noted earlier, extending benefits to non-itemizers should considerably increase costs while imposing a floor should help to contain costs. For plan 3, the net effect is considerably higher costs, suggesting that the cost increases from making the benefit above-the-line dominate the savings from the dollar floor. That is not to say that the dollar floor is unimportant. When compared to plan 2, which is exactly the same as plan 3, except that it does not impose a floor, costs are nearly three times higher. (Also, note that plans 2 and 3 include a credit rather than a deduction, which factors into the results.) For plan 6, cost savings from a 1 percent AGI floor dominate the increased cost from extending the deduction to non-itemizers. Here costs are much lower than under current law. A 1 percent of AGI floor excludes more deductions from higher-income taxpayers than does a dollar floor. At the same time it includes more contributions of lower-income taxpayers. But, the revenue raising effects on higher-income taxpayers is much larger than the revenue losing effects on lower-income taxpayers. Additionally, restricting that plan to itemizers (plan 5) has little additional effect on costs. That is primarily because a 1 percent of AGI floor is high enough to exclude most non-itemizers.

Table 6

Impose a Dollar Floor Above Which Contributions by Itemizers Are Deductible

Estimated changes compared to the 2003 "baseline" and assuming moderate behavioral responses.

	Plan 4: Floor of $500 for singles and $1000 for joint filers				
	All Filers			*Non-Itemizers*	
Increase in:	*Beneficiaries*	*Dollars Donated*	*Tax Expenditure*	*Returns*	*Dollars Donated*
Total	-11.7	-316	-4,557	2.2	3,246
Less than $0	0.0	0	0	0.0	0
$0 to $10,000	0.0	0	0	0.1	85
$10,000 to $20,000	-0.3	-7	-20	0.2	304
$20,000 to $30,000	-0.7	-14	-87	0.2	310
$30,000 to $40,000	-1.3	-30	-189	0.3	465
$40,000 to $50,000	-1.4	-37	-290	0.3	426
$50,000 to $75,000	-3.4	-83	-865	0.6	924
$75,000 to $100,000	-2.5	-71	-963	0.3	423
$100,000 to $200,000	-1.9	-55	-1,516	0.1	222
$200,000 to $500,000	-0.2	-15	-496	0.02	56
$500,000 to $1,000,000	-0.02	-2	-88	0.004	15
$1,000,000 to $5,000,000	-0.01	-2	-39	0.002	15
$5,000,000 to $10,000,000	0	0	-2	0.0001	1
$10,000,000 or more	0	0	-1	0	0

Numbers are in millions.
Tax expenditures for non-itemizers are 0 because they are not deductible.
Increases in the number of non-itemizers are exactly offset by decreases in the number of itemizers.

Source: Author's calculations based on SOI data.

Table 7

Impose a 1 Percent AGI Floor Above Which Contributions Are Deductible

Estimated changes compared to the 2003 "baseline" and assuming moderate behavioral responses.

	Plan 5: Below-the-Line					*Plan 6: Above-the-Line*				
	All Filers			*Non-Itemizers*		*All Filers*			*Non-Itemizers*	
Increase in:	*Beneficiaries*	*Dollars Donated*	*Tax Expenditure*	*Returns*	*Dollars Donated*	*Beneficiaries*	*Dollars Donated*	*Tax Expenditure*	*Returns*	*Dollars Donated*
Total	-10.5	-682	6,908	1.5	2,577	-9.4	-411	-6,804	5.4	33,446
Less than $0	0.0	0	0	0.0	0	0.0	0	0	0	0
$0 to $10,000	0.0	-0.1	0	0.03	28	0.2	0	16	0.1	259
$10,000 to $20,000	-0.1	-2	-7	0.1	103	0.0	0.5	3	0.4	1,329
$20,000 to $30,000	-0.3	-5	-44	0.1	143	-0.2	3	-38	0.6	2,284
$30,000 to $40,000	-0.8	-13	-120	0.2	230	-0.7	7	-118	0.7	2,564
$40,000 to $50,000	-0.9	-19	-213	0.2	247	-0.8	8	-209	0.7	2,942
$50,000 to $75,000	-2.7	-59	-756	0.4	624	-2.5	2	-741	1.4	7,243
$75,000 to $100,000	-2.3	-65	-961	0.3	375	-2.2	-14	-947	0.8	4,469
$100,000 to $200,000	-2.6	-143	-2,073	0.2	339	-2.5	-87	-2,050	0.5	4,570
$200,000 to $500,000	-0.7	-143	-1,315	0.04	114	-0.7	-125	-1,310	0.1	1,689
$500,000 to $1,000,000	-0.1	-81	-508	0.01	70	-0.1	-71	-505	0.02	878
$1,000,000 to $5,000,000	-0.1	-101	-547	0.01	144	-0.1	-90	-544	0.01	1,417
$5,000,000 to $10,000,000	-0.01	-21	-124	0.002	54	-0.01	-19	-124	0.001	541
$10,000,000 or more	-0.003	-29	-239	0.001	107	-0.003	-26	-237	0.001	3,263

Numbers are in millions.

Increases in the number of non-itemizers are exactly offset by decreases in the number of itemizers.

Source: Author's calculations based on SOI data.

CONCLUSION

This paper uses Statistics of Income (SOI) data for 2003 in conjunction with data from the Panel Study of Income Dynamics (PSID) to examine patterns of giving across the income distribution. The paper evaluates six plans for reforming the tax treatment of charitable giving, including an option similar to the one favored by the President's Tax Reform Panel and options that share some features with the President's fiscal year 2004 and fiscal year 2005 budget proposals.

I find that the structure of tax incentives for giving can have a major impact on costs to the federal government, the level of charitable giving and which (or how many) taxpayers benefit from the preference.

Imposing floors substantially improves the cost effectiveness of tax preferences for charitable giving. Floors substantially reduce the tax with minimum effects on contributions relative to similar proposals without floors. For the floors considered here, the subsidy rate is reduced to $0.03 to $0.04 per dollar of contribution, depending on other characteristics of the preference.

In general, *extending the deduction to non-itemizers is by itself costly and has little effect on donations*. For example, making the current deduction above-the line, and imposing no other changes, increases the number of beneficiaries by 35.6 million and raises tax expenditures by $7.2 billion (or more than 24 percent), but under the most optimistic scenario increases donations by just 0.1 of 1 percent. In terms of efficiency, this plan would raise the average cost per dollar of donations by 19 percent, from $0.17 to $0.21 per dollar donated.

Replacing the deduction for charitable giving with a 25 percent above-the-line tax credit greatly increases costs, but could result in substantially more giving. The credit would increase annual tax expenditures for giving by between $5.1 billion and $15.2 billion, or between 17 and 51 percent. Changes to giving are highly dependent on the assumptions about taxpayer responsiveness, and range from $0 to $36.4 billion. The costs can be substantially altered by combining the credit with a floor. Adding a $500 floor to the plan for singles ($1,000 for joint filers) substantially lowers the cost increase from the credit, while maintaining most of the increased donations. Without the floor, the credit is much less efficient than current law, raising the average cost per dollar donated by $0.07 (or 41 percent). With the floor, the average cost per dollar donated rises by $0.02 compared to current law.

Notes

1 See page 8 of *Giving USA 2004*.

2 Throughout this paper, charitable contributions are defined as in *Title 26, Subtitle A, Chapter 1, Subchapter B, Part VI, Section 170, Subsection c* of the *U.S. Code*.

3 Estimates for itemizers are based on numbers reported on income tax returns. Estimates for non-itemizers are based on imputations based on data from the Survey of Consumer Expenditures and the Survey of Consumer Finances. The imputation procedure was calibrated so that the total for non-itemizers roughly equals the number reported by *Giving USA*.

4 For itemizers, giving as a share of income is U-shaped. The giving rate is larger at both tails and smallest in the middle of the distribution.

5 Effective marginal tax rates measure the share of an additional dollar of income that is paid to the government. Effective tax rates take into account the many complexities and interactions between different parts of the tax code and thus are often different from statutory tax rates. CBO's tax model is used to impute effective tax rates applicable for deductions. Tax expenditures are calculated assuming that filers would have made no behavioral responses in the event that contributions were not deductible, although filers are assumed to switch from itemizers to non-itemizers if the standard deduction is larger than the filers remaining itemized deductions.

6 For non-itemizers, donations are not reported. For itemizers, the recipient organization is sometimes reported, but many organizations serve multiple functions.

7 According to *Giving USA*, 35.9 percent of *all giving* was to religious organizations for 2003. While all giving is roughly one-third larger than individual giving, that number seems inconsistent with the PSID estimate. For 2000, the PSID-based estimate for individual giving to religion was 56.7 percent.

8 See Sandburg (2007).

9 That assumes that income effects are small and ignores the fact that a small percentage of taxpayers move into a lower marginal tax bracket because of the change.

10 For most of those taxpayers, the average and marginal price per dollar of giving will be the same. However, deducting charitable donations could move some taxpayers to a lower tax bracket, in which case the marginal cost of giving would be greater than the average cost.

[11] Those itemizers for whom itemized deductions minus the lesser of their charitable contributions or $500 (for individuals) are less than the standard deduction would no longer choose to itemize.

[12] Those itemizers for whom itemized deductions minus the lesser of their charitable contributions or 2 percent of their AGI are less than the standard deduction would no longer choose to itemize.

[13] Costs are measured in terms of (foregone) tax revenue to the government. Those costs are referred to as tax expenditures and are discussed in more detail in the previous section.

[14] The term "subsidy rate" is identical with the term "treasury efficiency" in the literature. That former term is eschewed here to avoid confusion with economic efficiency – a very different concept.

[15] That assumes a modest elasticity. Assuming a larger elasticity results in an even greater increase in donations. At the other extreme, assuming an elasticity of zero, would imply no change in donations (under any of the plans), since that assumption implies that donations are not influenced by tax incentives.

[16] Plan 3 also includes a dollar floor, but yields somewhat different results due to other features of the plan that are discussed shortly.

References

Congressional Budget Office.

Effects of Allowing Nonitemizers to Deduct Charitable Contributions. Washington, D.C., December 2002.

Budget Options. Washington, D.C., February 2007.

Center on Philanthropy at Indiana University. *Giving USA 2004: The Annual Report on Philanthropy for Year 2003*. Indiana University-Purdue University, Indianapolis, 2004.

Federal Reserve Board. Survey of Consumer Finances. Washington, D.C. http://www.federalreserve.gov/PUBS/oss/oss2/scfindex.html

Institute for Social Research. Panel Study of Income Dynamics. University of Michigan, Ann Arbor, MI. http://psidonline.isr.umich.edu/

Sandberg, Sheryl. The Charity Gap. *Wall Street Journal*, April 4, 2007, A15.

The President's Advisory Panel on Federal Tax Reform. *Simple, Fair, and Pro-Growth: Proposal to Fix America's Tax System*. Washington, D.C., 2005.

U.S. Department of Treasury. Internal Revenue Service. Statistics of Income. Washington, D.C., 2003. http://www.irs.gov/taxstats/article/0,,id=120303,00.html

U.S. Department of Labor. Bureau of Labor Statistics. Consumer Expenditures Survey. Washington, D.C.

United States Internal Revenue Code. Title 26, Subtitle A, Chapter 1, Subchapter B, Part VI, Section 170, Subsection c. Washington, D.C. http://www.access.gpo.gov/uscode/title26/title26.html