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IN FOCUS

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The Charitable Deduction for Individuals

The charitable deduction is a long-standing feature of the individual income tax. It is also one of the largest individual income tax provisions in terms of annual forgone revenue, an estimated $52.4 billion in FY2020. Before changes implemented by P.L. 115-97 (commonly referred to as the Tax Cuts and Jobs Act or TCJA), the tax expenditure for charitable contributions was larger, an estimated $57.0 billion for FY2017. This In Focus provides background information on the individual charitable deduction.

The Deduction

Under current law, taxpayers who itemize their deductions can—subject to certain limitations—deduct charitable donations to qualifying organizations. Qualifying organizations are generally "public charities" or "private foundations" with tax-exempt status under Internal Revenue Code (IRC) Section 501(c)(3); federal, state, or local governments; and other less common types of qualifying organizations.

Tax-deductible donations to qualifying organizations can be in the form of cash or property. Property held for more than one year is often referred to as *long-term capital gain property*. Property held for less than a year is often referred to as *short-term capital gain property*. Depending on (1) the type of property donated and (2) the type of qualifying organization that receives the donation, there are limitations on the total dollar amount that can be deducted by the taxpayer in a given tax year. The limitations are defined as a percentage of the taxpayer's adjusted gross income, or AGI (computed without regard to net operating loss carrybacks), as noted in **Table 1**. If the amount deducted exceeds the taxpayer's AGI limitation, the excess can be carried forward and deducted on future years' tax returns for up to five years.

For noncash donations, there are rules on how to value the property. Depending on the type of property and the recipient organization, the property is generally valued at its basis (i.e., what the taxpayer originally paid for the property with adjustments) or its fair market value (how much the taxpayer would receive in an open market for the property at the time it is donated), as noted in **Table 1**.

Selected Legislative Background

The charitable deduction was first enacted to offset the potential negative effects of increased income taxes on charitable giving as part of the War Income Tax Revenue Act of 1917 (P.L. 65-50). The overall amount that could be deducted was limited to 15% of net taxable income to prevent taxpayers from eliminating tax liability by claiming the deduction. The deduction has been changed dozens of times since enactment. Key legislative changes relevant to this In Focus are highlighted next.

Table 1. Limitations on Charitable Contributions

Type of Donation	Recipient	Valuation Rules for Property	Limit (% of AGI)
Cash or short-term gain capital property	Public charity; private operating foundation; federal, state, local government	Basis of the property	50% 60% (cash) 100% (cash; 2020 & 2021)
	Private nonoperating foundation; other	Basis of the property	30%
Long-term capital gain property	Public charity; private operating foundation; federal, state, local government	Fair market value	30%
	Private nonoperating foundation; other	Basis of the property	20%

Source: Internal Revenue Code (IRC) Section 170.

Note: These are general rules, and there are numerous exceptions. AGI limits for cash contributions are temporarily 100% in 2020 and 2021, and 60% through 2025. For more information, see CRS Report R45922, *Tax Issues Relating to Charitable Contributions and Organizations*.

Over time, Congress has modified the maximum amount that can be deducted in a given year by changing the income limitation. In 1952, as part of P.L. 82-465, Congress raised the limitation to 20% of AGI. In 1954, Congress increased the maximum deduction limit to 30% of AGI (P.L. 83-591) for donations to certain public charities. The Tax Reform Act of 1969 (P.L. 91-172) raised the deduction limit to 50% of AGI for donations to public charities and allowed deductions for contributions to private operating foundations. The 1969 act also imposed a 30% limit for contributions of appreciated property and imposed other restrictions on contributions of long-term capital gain property. The Deficit Reduction Act of 1984 (P.L. 98-369) raised the limitation on the deduction for donations of cash or short-term capital gain property to private nonoperating foundations from 20% to 30% of AGI.

There were exceptions to these limits for particularly large gifts. The Revenue Act of 1924 (P.L. 68-176) specified that if a taxpayer made contributions exceeding 90% of net income in the tax year and each of the past 10 years, a full deduction was allowed. A phaseout of the unlimited deduction was included in the Tax Reform Act of 1969.

In the early 1980s, temporary changes provided a charitable deduction to nonitemizers. The Economic Recovery Act of 1981 (P.L. 97-34) allowed taxpayers who took the standard deduction to also claim a deduction for charitable giving. This temporary provision went into effect in 1982, and was allowed to expire as scheduled at the end of 1986.

The TCJA (P.L. 115-97) temporarily increased the AGI limit for cash donations made to public charities to 60%. This change went into effect in 2018, and is set to expire December 31, 2025.

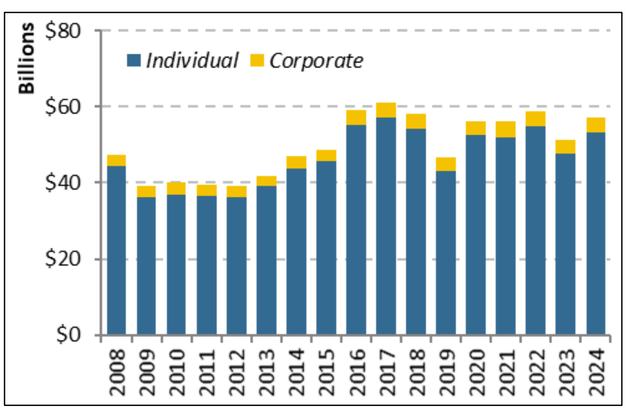
The CARES Act (P.L. 116-136) temporarily eliminated the 60% AGI limitation for cash gifts to charities for tax year 2020 (effectively raising the limitation to 100%). The law also created a temporary $300 above-the-line deduction for nonitemizers. The Taxpayer Certainty and Disaster Tax Relief Act of 2020 (Division EE of P.L. 116-260) provided a deduction of up to $300 ($600 in the case of a joint return) for charitable contributions made by nonitemizers in 2021, and extended the suspension of the 60% AGI limit for cash gifts.

Cost

The charitable deduction is estimated to result in $48.0 billion in forgone revenue in FY2020, $52.4 billion from the individual income tax and $3.7 billion from the corporate income tax (**Figure 1**). During the past decade, tax expenditures associated with the charitable deduction have fluctuated, as a result of both policy changes and fluctuations in charitable giving.

Tax expenditures associated with the charitable deduction were expected to be lower following the TCJA. The TCJA approximately doubled the standard deduction and limited or repealed other itemized deductions. As a result, fewer taxpayers are expected to claim itemized tax deductions generally, including the deduction for charitable contributions. Further, lower marginal tax rates also reduce the tax expenditure associated with the deduction for charitable contributions. Both of these factors mean reduced tax incentives for giving following the TCJA. Potentially offsetting this effect is the nonitemizer deduction for 2020 and 2021 and the higher AGI limits for cash gifts in those same years.

Figure 1. Charitable Deduction Tax Expenditures, FY2008-FY2024

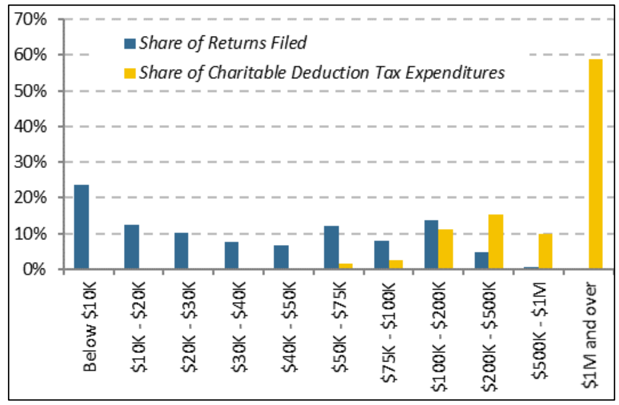


Source: Joint Committee on Taxation.

Distribution of Benefits

Tax expenditures for charitable deductions largely benefit higher-income taxpayers. Higher-income taxpayers tend to (1) be more likely to itemize their deductions; (2) have a greater ability to give; and (3) derive a larger tax benefit from each dollar given because they generally face higher marginal tax rates. An estimated 84% of tax expenditures for charitable giving in FY2022 will be claimed by taxpayers in the $200,000-and-above income class (**Figure 2**). Overall, an estimated 6% of returns fall into this class. In contrast, an estimated 5% of the charitable deduction tax expenditures are associated with tax returns filed in income classes of $100,000 or less (which account for 81% of tax returns filed). Charitable deduction tax expenditures have become even more concentrated in the highest income category following the changes made in TCJA.

Figure 2. Distribution of Returns Filed and Itemized Charitable Deduction Tax Expenditures, by Income Class, 2022



Source: Joint Committee on Taxation.

Generally, taxpayers must itemize deductions to claim a deduction for charitable donations (there was a temporary nonitemizer deduction in 2020 and 2021). In 2017, 32% of tax filers itemized deductions. An estimated 10% of taxpayers will itemize deductions in 2022.

Policy Options and Considerations

There tends to be agreement that the tax code should support charitable giving. TCJA retained the charitable deduction; broadly, however, the higher standard deduction, limits on other itemized deductions, and lower marginal tax rates reduced charitable giving incentives. Further, the marginal incentive for charitable giving tends to be strongest at the top of the income distribution.

There are various policy options related to charitable giving incentives. For example, the temporary deduction for nonitemizers could be extended and modified. This would increase the incentive to give for many lower-and middle-income tax filers. Alternatively, a floor could be imposed, restricting deductions for charitable giving to giving above some threshold. There would be no marginal incentive to give small amounts, but there would be a tax incentive to give larger amounts. The deduction could also be converted to a credit, equalizing the subsidy for giving by individuals in different tax brackets. Another way to equalize the value of the deduction for taxpayers in different tax brackets is to cap (or make fixed) the rate of the deduction. Other changes to the deduction might include modified AGI limits or changes related to valuation of noncash gifts.

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