Mitigating the Effects of an Economic Downturn on Charitable Contributions: Facing the Problem and Contemplating Solutions

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MITIGATING THE EFFECTS OF AN ECONOMIC DOWNTURN ON CHARITABLE CONTRIBUTIONS:
FACING THE PROBLEM AND CONTEMPLATING SOLUTIONS

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Charitable giving has been a foundation of American society almost since the nation began, but the issue of how such giving should be treated for tax purposes has been the subject of frequent debate. Scholars have proposed various theories explaining why the positive effects of this deduction on both donors and donees outweigh the negative impact on government coffers of this tax expenditure, although many still criticize certain features of the deduction in its current form. However, one area of this research that has been neglected is how the charitable sector is affected by changes to the economy at large. Contributions to charitable organizations tend to decline during an economic downturn, and such a decline may be catastrophic for those organizations that simultaneously experience an increase in demand for their services during such times. The government should try to stimulate charitable giving during economic downturns because doing so will further the goals of the charitable deduction and address some of the concerns raised by critics of the deduction. The most effective means of stimulating giving would be to temporarily convert the deduction to a credit during those periods when the economy falls into a recession and to provide a tax credit to for-profit corporations that send their employees to work for charitable organizations.
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INTRODUCTION

For almost one hundred years, the federal government has encouraged charitable giving by allowing taxpayers to deduct donations made to certain charitable organizations.\(^1\) Since that time, various changes have been made to the deduction, including changes in the amount taxpayers may deduct, which organizations may receive deductible contributions, and who is eligible to take the deduction.\(^2\) Currently, taxpayers who itemize their

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\(^1\) War Income Tax Revenue Act of 1917, ch. 63, 1201(2), reprinted in J.S. Seidman, Seidman’s Legislative History of Federal Income Tax Laws, 1938-1861, at 944 (1938). Vada Waters Lindsey, *The Charitable Contribution Deduction: A Historical Review and a Look to the Future*, 81 Neb. L. Rev. 1056, 1061-62 (2003). Originally, the deduction was intended to sustain previous levels of charitable giving in the face of the recently implemented income tax. Commission on Private Philanthropy and Public Needs, *Giving in America* 18 (1975) [hereinafter Giving in America]. Additionally, it was believed that income used for charitable purposes did not enrich the giver and therefore did not deserve to be taxed. *Id.*

\(^2\) See, e.g., War Income Tax Revenue Act of 1917, ch. 63, § 1201(2) (1917) (implementing the charitable deduction and setting a cap of 15% of net income); Act of July 7, 1952, Pub. L. No. 82-456 (1952) (raising the cap on the deduction from 15% to 20%); U.S.C.C.A.N. 4017 (1954) (raising the cap to 30% for contributions made to certain organizations); Pub. L. No. 87-8345 (1962) (extending the deduction to colleges and universities); Revenue Act of 1964, Pub. L. No. 88-272 (1964) (extending the deduction to include any organization that receives a substantial part of their support from the general
deductions on their tax returns may deduct contributions made to certain charitable organizations that have registered with the Internal Revenue Service (the “Service”). The amount a taxpayer may deduct is generally limited to 50% of that taxpayer’s adjusted gross income, although in some cases the deduction is limited to 20% or 30% of adjusted gross income. Although taxpayers may not deduct the value of the services they provide when they volunteer with a charitable organization, they may be able to

3 I.R.C. § 170 (2010). Taxpayers may not deduct contributions made to specific individuals, contributions to nonqualified organizations, contributions from which the taxpayer receives financial or economic benefits, or contributions of partial interests in property. Id. Taxpayers who contribute property to such organizations may generally deduct the fair market value of such property at the time of the contribution. Id. Many state income tax laws allow for a similar deduction. Charles T. Clotfelter, FEDERAL TAX POLICY AND CHARITABLE GIVING 12 (1985).

4 Id.
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deduct some of the costs incurred in providing those services.\(^5\)

Scholars have debated the benefits and drawbacks of the deduction since its inception, and both proponents and critics have focused largely on the effect the deduction has both on taxpayers’ incentives to give to charitable organizations and on those organizations’ ability to sustain themselves through donations. While some examine the effect that the deduction has on donors,\(^6\) others look at the impact the deduction has on either the organizations themselves\(^7\) or donors’ ability to direct government funds to particular organizations.\(^8\) However, little attention has been paid to the effect that an economic downturn has on the incentives provided to donors and, consequently, on the charitable sector.

In this Article, I attempt to address those deficiencies by looking at how different types of organizations are affected by an economic downturn and

\(^5\) Treas. Reg. § 1.170A-1(g) (2010).


how charitable giving can be stimulated during such times. Unsurprisingly, charitable contributions tend to decline during a recession. In some cases, donors may anticipate the effects that a stagnant economy will have on charitable organizations and try to mitigate these effects on their own; for example, contributions to some types of organizations, such as homeless shelters and food banks, actually increase when the economy declines. However, other organizations, like museums and other arts organizations, may suffer as a result of this reallocation of charitable donations, and some may be forced to shut their doors altogether.

I argue that encouraging charitable giving by both individuals and organizations during an economic downturn is not only an effective means of addressing these issues but is also consistent with the goals of the charitable deduction. While scholars have proposed several changes to the charitable deduction in an attempt to either equalize treatment among donors or to stimulate giving in general, some of these proposed changes would be inconsistent with the larger goals of the deduction, difficult to implement or of limited practical use.

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Part I of this article examines the policies underlying the charitable deduction and discusses the arguments made by proponents and critics of the deduction. Part II examines the effect that an economic downturn has on charitable organizations. Part III revisits theories about the charitable deduction in light of the impact that changes to the economy have on charitable organizations and considers the question of whether proposed changes to the deduction should target specific organizations. Part IV looks more closely at various proposals aimed at both individual and corporate donors. Finally, Part V examines some possible criticisms of these proposals. Ultimately, this Article concludes that the best way to aid the charitable sector during an economic downturn is by converting the deduction to a credit and providing employers with a tax credit for paying their employees to work for charitable organizations.

I. TAX POLICY REGARDING THE CHARITABLE DEDUCTION

When examining the charitable deduction, we must keep in mind that all tax deductions, including the deduction for charitable contributions, are tax expenditures and therefore have an impact on the federal budget.\textsuperscript{10} As a

\textsuperscript{10} STANLEY S. SURREY & PAUL R. McDaniel, TAX EXPENDITURES (1985). Furthermore, as Benshalom points out, “taxpayers that receive benefits from charitable
result, those who support the deduction must demonstrate that its benefits outweigh the consequent reduction in tax revenue. Additionally, relief assign the revenue costs to other taxpayers. The Treasury Department needs to tax other taxpayers at a higher effective tax rate to recoup these reserves.” Ilan Benshalom, *The Dual Subsidy Theory of Charitable Deductions*, 84 Ind. L.J. 1047, 1073 (2009). However, McDaniel suggests in a subsequent article that discussion of the charitable deduction as an expenditure is misguided, since the true expenditure is “the nontaxation of the beneficiaries, again, either directly, or through a surrogate tax on the charitable organizations. Paul R. McDaniel, *The Charitable Contributions Deduction (Revisted)*, 59 SMU L. Rev. 773, 783 (2006). In his view, the individual benefits that motivate such contributes, such as altruism or increases in status or power, constitute “psychic income” that should be deductible unless “the value of the gift is not likely to be included in income on the donee’s side of the transaction or administrative concerns justify such an approach.” *Id.* at 778.

11 For example, Paul McDaniel argues that, were the deduction to be repealed, the unsubsidized portion of donors’ contributions would remain unchanged, even though the total amount received by charitable organizations would undoubtedly go down. Paul R. McDaniel, *Federal Matching Grants for Charitable Contributions: A Substitute for the Income Tax Deduction*, 27 Tax L. Rev. 377, 378 (1972). In other words, because a taxpayer in the 70% tax bracket who makes a $100 donation generally does so with the knowledge that he or she will receive $70 of that $100 back, he or she will continue to make a $30 contribution in the absence of a deduction. *Id.* at 380. While this argument makes logical sense, it ignores the psychological impact that receiving a tax deduction may have on a taxpayer’s desire to make a charitable donation. Nonetheless, McDaniel’s point
proponents of the charitable deduction must explain why assistance to charities should take the form of a tax expenditure rather than direct government spending, especially since reliance on tax expenditures is well taken that the debate is less about the extent to which we wish to stimulate taxpayer donations through the deduction as it is about the extent to which we wish to subsidize those donations with government funds. *Id.* at 381 (“charitable institutions are not concerned solely with maintenance of the level of out of pocket private giving, but with ensuring that federal funds will continue to be available at the level provided through the deduction mechanism”). Although some proponents of tax expenditures argue that such expenditures are more effective than government spending at encouraging private decisionmaking, others dispute this claim. *See* SURREY & MCDANIEL, *supra* note 10, at 99-100 (“[t]he government [] may decide to use a tax expenditure to foster the illusion that the private sector is making the spending decisions”). Surrey and McDaniel suggest that the lower visibility of tax expenditures may lead them to be favored by politicians who want to provide funds to certain sectors of the economy while still being viewed as fiscally conservative. As an example of this, they cite the debate surrounding the deduction for expense account entertainment deductions, noting that politicians supporting the deduction argued that it would benefit luxury restaurants, even though these same politicians would have found it politically disastrous to voice support for a direct spending program supporting such restaurants. They also suggest that the length and complexity of tax expenditure provisions encourage legislators to pass them with little analysis or debate. *Id.* at 104-05.
greatly decrease[] the ability of the Government to maintain control over the management of its priorities [and] run counter to the whole thrust of our concerns with the ordering of national priorities and with the wise allocation of our resources, which we have come to see as limited and therefore in need of careful management.  

Some proponents of the deduction argue that charitable contributions are fundamentally different from other expenses and therefore should not be subject to tax, while others argue that charitable contributions provide some societal benefit that makes them worthy of a deduction. Still others argue

12 Stanley S. Surrey, Tax Incentives as a Device for Implementing Government Policy: A Comparison with Direct Government Expenditures, 83 HARV. L. REV. 705, 731 (1970). Surrey points out that tax expenditures present some additional disadvantages when compared with government spending. For example, because tax legislation goes through the House Ways and Means Committee and the Senate Finance Committee, rather than through the committee charged with examining the substantive issue involved, tax expenditures are essentially vetted by legislators with little relevant knowledge regarding the goals and policies underlying the expenditures. Furthermore, “the tax incentive program considered by the tax committees would be isolated from the regular flow of legislation and activity in the field involved, and this isolation would make coordination and the consideration of priorities difficult.” Id.
that the charitable deduction provides a mechanism through which taxpayers can choose which charitable organizations will receive subsidized support from the government.

These various justifications that have been given for the charitable deduction can be broadly grouped into three categories: expenditure theory, subsidy theory, and choice theory.

A. EXPENDITURE THEORY

According to expenditure theorists, any discussion of the charitable deduction should focus not on whether charitable organizations should be subsidized but instead on whether charitable donors should be taxed for their contributions. William Andrews, the leading proponent of expenditure theory, rejects the idea that tax deductions should be used to implement social policy, arguing instead that they should be used only when necessary to ensure that the distribution of government funds is consistent with the distribution of tax burdens. In other words, the role of personal deductions should be to distinguish “real” income and expenses from accumulation and expenses that we should not and do not wish to tax.

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13 Andrews, supra note 6, at 311.

14 Id. at 330.
According to Andrews, deductions are justifiable when they do not fall into the category of “divisible, private goods and services whose consumption by one household precludes enjoyment by others” and are rather “collective goods whose enjoyment is nonpreclusive or the nonmaterial satisfactions that arise from making contributions.”

Andrews argues that charitable contributions should be deductible because the goods and services they provide do not benefit the donor directly; rather, the direct benefit goes to others, while the donor receives only nonmaterial satisfaction. He notes that almost all charitable organizations produce collective goods or services and that, as a result, the value of these goods and services should not be taxable to either their recipients or their donors. Furthermore, he notes that measuring the individual benefits received by donors would be not only impracticable but also undesirable.

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15 Id. at 314-15. Arguably, even “alms for the poor” produce common goods by reducing poverty and therefore indirectly reducing crime rates, homelessness, and other social ills.

16 Id. at 314.

17 Id. at 314-15.

18 Id. at 360. Andrews further argues in support of the deduction by claiming that charitable contributions differ from most ordinary gifts, which are generally non-deductible
Expenditure theory has been subjected to heavy criticism, most notably by Mark Gergen and Mark Kelman. Gergen argues that Andrews’ theory
by the donor, because such gifts tend to occur within a single household. *Id.* at 349. Charitable contributions are also distinct from non-household gifts because of the likely difference in tax rates between the donor and the likely recipient and because the organization provides a means of monitoring the redistribution of funds from donor to recipient. *Id.* at 351. He also argues that including taxable contributions as a proxy for taxing benefits would lead to an excessively high tax rate because of the fact that charitable contributions disproportionately come from a small number of high-income donors. *Id.* at 361. He notes that donors faced with the prospect of a tax on their contributions will be likely to reduce those contributions rather than other expenditures, because a reduction in contributions will not lead to a reduction in benefits to them. *Id.* Finally, he argues that charitable organizations, unlike political organizations, “are numerous enough, and sufficiently voluntary in their membership relations, so that we need not have the same fear of oppressive domination by wealthy contributors” as we do in the political arena. *Id.* at 364. In a variation on expenditure theory, Boris Bittker argues that corporate charitable contributions can be viewed as true “business expenses” because they serve as a form of advertising and that even individual contributions could be seen as business expenses if they are made at the prompting of one’s employer and are rewarded with a work-related incentive, such as extra vacation days. Boris I. Bittker, *Charitable Contributions: Tax Deductions or Matching Grants?*, 28 Tax L. Rev. 37, 57 (1973).

19 See also Benshalom, *supra* note 10, at 1055 (calling Andrews’ theory “inconsistent with fundamental tax-policy principles” and arguing that “[i]t neglects the fundamental notion that income is attributed to the taxpayer that earns it and not to the persons to whom
ultimately does little more than “repackage” subsidy theory because, even though Andrews never defines exactly which collective goods should be excluded from income, he nonetheless argues that contributions used to provide these goods should be excluded from income. Kelman, on the other hand, questions Andrews’ basic definition of a charitable donation as a nonpreclusive appropriation that does not divert resources away from the satisfaction of others’ needs. Instead, Kelman states that “[e]ven when the it is assigned”); Stanley A. Koppelman, Personal Deductions under an Ideal Income Tax, 43 Tax L. Rev. 679, 689 (1988) (criticizing Andrews’ argument as circular because “[t]he effects of a tax follow from the definition of the base”). Koppelman also argues that charitable contributions are not justifiable under expenditure theory because “[t]he expenditure of cash or property [as a charitable contribution] represents a clear personal benefit to the donor.” Id. at 707.

20 Mark P. Gergen, The Case for a Charitable Contributions Deduction, 74 Va. L. Rev. 1393, 1416 (1988). In fact, Gergen describes Andrews’ expenditure theory as merely the reverse of the subsidy argument, which sees the deduction as a way “to encourage people to do voluntarily what we would otherwise have to coerce them to do.” Id. at 1423. In particular, Gergen notes that Andrews fails to distinguish between “charitable” goods that are eligible for a subsidy and other goods that create positive externalities, like school tuition. Id. at 1424.

donor assumes no control over the donee’s spending, I would argue that his donations are likely to be appropriative” and that “[i]f the donee, the charitable conduit, or other members of the donee’s community expend any time or energy ensuring that the donor enjoys his donation, at least some of the donation ought to be included in the tax base.” For Gergen, Kelman and other critics of expenditure theory, subsidy theory may provide a more appealing rationale for the charitable deduction.

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22 Id. at 850. Kelman is particularly skeptical of the characterization of donations as “nonpreclusive” when dealing with high-income donors. Id. at 856 (“the character of gifts from high-income givers is inevitably reciprocal in a way not necessarily true for the low-income donor”). For example, he notes that gifts by the rich to educational institutions are often intended to benefit the upper class and “involve a great deal of reciprocity, at least in the form of attention and deference.” Such contributions “seriously undermine[] vertical tax equity because large amounts (and percentages) of income are at stake.” “Thus,” he notes, “real world complexity undercuts even further an already questionable defense of the charitable deduction.” Id. at 858. Others have also criticized Andrews’ “ideal income tax” as applied to the charitable deduction, including McDaniel, who argues that “[t]he notion that a charitable contribution should be deductible because it creates a common or public good is suspect” and “finds no support in the Simons definition of income. McDaniel, supra note 10, at 774.
Subsidy theorists generally agree with expenditure theorists that contributions to charitable organizations should be deductible because of the collective nature of the goods and services provided by those organizations. However, unlike expenditure theorists, who argue that the public nature of these goods makes it impractical to tax the donors who fund the organizations that provide these goods, subsidy theorists argue that taxing those goods will lead to their underfunding. Such goods are commonly referred to as public goods because “one person’s consumption of the good does not reduce its availability to others (i.e., the good is nonrival or in joint supply); and no one can be excluded from the good (i.e., the good is nonexclusive).” Generally, a good is considered public or

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23 See, e.g., Bittker, supra note 18, at 61 (arguing that contributions may be characterized as either a discharge of a moral obligation or as a reward for praiseworthy behavior; under either framework, a deduction for contributions would not need to operate “efficiently” in order to be considered worthy).

24 Gergen, supra note 20, at 1398 (“[c]harities that provide goods for which we cannot or do not wish to charge beneficiaries deserve government support because, without the subsidy, society will tend to underfund them”).

25 Id. at 1397.
nonrival if charging individual users for the benefits received would be more costly and/or burdensome than providing the good for free.\textsuperscript{26}

Because of their nonexclusive nature, public goods can be provided to people who do not pay for them; as a result, some people will inevitably refuse to pay, essentially “freeriding” on the payments of others.\textsuperscript{27} Others will give less than the true cost of the public good, in part because they may not account for its ancillary benefits.\textsuperscript{28} The charitable deduction helps alleviate this problem by spreading the cost of providing public goods among all taxpayers, including freeriders.\textsuperscript{29}

Proponents of subsidy theory argue that, “even with its flaws, [the charitable deduction] better matches expense with preference in cases of collective goods for which demand is universal but heterogeneous.”\textsuperscript{30} Private charity appears to be more responsive to differences in demand for collective goods than the government, in part because it allows smaller

\begin{quote}
\textsuperscript{26} Id. at 1397-98.
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\begin{quote}
\textsuperscript{27} Id. at 1398.
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\begin{quote}
\textsuperscript{28} Id. Gergen gives as an example a student who fails to take into account the societal benefits of her education when determining whether to go to college.
\end{quote}

\begin{quote}
\textsuperscript{29} Id. at 1403.
\end{quote}

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\textsuperscript{30} Id.
\end{quote}
groups to act collectively while avoiding the political process.\textsuperscript{31} Subsidization may be particularly attractive when the public good is highly desired by a small minority and only slightly preferred by a large majority, since, without a subsidy, “the minority may not be able to overcome its freerider problems to provide the appropriate amount of the good.”\textsuperscript{32}

In a variation on subsidy theory, Johnny Rex Buckles argues that the benefits provided by charitable organizations, like many of the benefits provided by government (and even, in some cases, by private actors) constitute types of “community income” that are not subject to tax because

\textsuperscript{31} Id. at 1399.

\textsuperscript{32} Id. However, Gergen also notes that this very phenomenon of free riding can be used to argue against the notion that a deduction is necessary solely because the goods it provides can benefit society as a whole. \textit{Id.} at 1411-12. In his words, “[e]specially in the cases of churches, schools, and other charities that primarily benefit a small group and secondarily benefit society generally, attention must be paid to the possibility that the small group has sufficient incentive to fund the good at an optimal level without a deduction for its payments.” \textit{Id.} at 1412. Moreover, while the charitable deduction alleviates the problem of free-riding, it arguably harms those who either oppose the programs that receive greater contributions as a result of the deduction or the “marginally disinterested” who support some level of charitable funding but do not receive any benefit from the additional donations that occur as a result of the deduction. \textit{Id.} at 1412.
they inure primarily to the general public rather than to individuals.\textsuperscript{33} Community income is not, and should not be, included in the tax base because its value to an individual taxpayer is not easily ascertained, because it is not consumed to the same degree by all taxpayers, and, most importantly, because such income is attributable to the community, which is not an appropriate object of taxation.\textsuperscript{34} With respect to the last point, Buckles argues that, when an individual donates to a charitable organization, he or she is acting not as a private consumer but as part of a separate, non-taxpaying unit, the community.\textsuperscript{35}

Ilan Benshalom criticizes subsidy theory on the grounds that “there is no one ‘optimal’ way to supply a set of agreed upon public goods, and [] there is no way of determining what goods are indeed undersupplied.”\textsuperscript{36} According to him, the deduction in its current state “does not necessarily promote more or better spending on charitable objectives and creates

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\textsuperscript{34} \textit{Id.} at 970-71.

\textsuperscript{35} \textit{Id.} at 980. McDaniel criticizes the community income theory for being “[nothing] more than an elaboration of the Andrews ‘common good’ concept…” McDaniel, \textit{supra} note 10, at 775.

\textsuperscript{36} Benshalom, \textit{supra} note 10, at 1051.
\end{flushleft}
serious negative externalities,” such as tax loopholes. Furthermore, he decries “the lack of a complete and coherent definition of charitable objectives” among those who espouse subsidy theory.

In part, Benshalom criticizes subsidy theory for ignoring the fact that the charitable deduction may be inefficient if it does not lead to “an increase in the overall private and public funds allocated toward charitable objectives as a result of charitable relief.” According to him,

[t]his calculation should subtract from the increase in contributions that were made only due to charitable relief the revenues lost by the government because of it, which could have been spent by the government to promote the charitable objectives. The ultimate outcome thus depends on the complicated interrelationships among the price elasticity of contributing, the marginal and effective average tax rates and the nature of charitable relief… The inverse impact of the average and marginal tax rates significantly complicates the

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37 *Id.* at 1072.

38 *Id.* at 1076.

39 *Id.* at 1059.
analysis of whether the deduction meets the standard of
treasury efficiency.\textsuperscript{40}

Benshalom describes charitable relief as “a nondemocratic [and, in
many cases, antidemocratic] way of allocating public funds because it
prefers individuals’ discretion over majority compromises.”\textsuperscript{41} Furthermore,
because the benefits of the deduction are available only to affluent
taxpayers, “[g]rounding the role of charitable relief within a democratic
regime is [] a difficult and unintuitive task.”\textsuperscript{42} Ultimately, he finds that
“none of the substance-subsidy approaches fully accounts for what ‘good’
means, and [] none of them offers a satisfying foundation for charitable
relief’s substance-subsidy justification.”\textsuperscript{43} Benshalom and other critics of
subsidy theory may prefer choice theory which argues that the deduction is
beneficial because it not only provides assistance to charities that provide
collective goods but also because it allows taxpayers to have a voice in

\textsuperscript{40} Id.

\textsuperscript{41} Id. at 1067.

\textsuperscript{42} Id.

\textsuperscript{43} Id. at 1070.
deciding which organizations will be subsidized.\textsuperscript{44}

C. CHOICE THEORY

Benshalom argues that we should consider not only the substance-subsidy role of the charitable contribution, but also what he deems its “process-subsidy” role.\textsuperscript{45} Because the typical method of allowing majoritarian preferences to drive government spending prevents some preferences from being voiced and addressed, the charitable deduction “should be understood not only as a method of determining what public goods are undersupplied, but also as a way to respond to unheard and unaddressed preferences; this may be referred to as the process-subsidy justification.”\textsuperscript{46} In his view, “[c]haritable relief can correct some of the imperfections associated with democratic decision making in a way that

\textsuperscript{44} See, e.g., Bittker, supra note 18, at 61 (arguing that the charitable deduction could be seen not just as an incentive but as a tool that could be used by taxpayers “to divert funds which would otherwise be spent as Washington determines and to allocate them to other socially approved functions”).

\textsuperscript{45} Benshalom, supra note 10, at 1077.

\textsuperscript{46} Id.
does not undermine the centrality of the majority’s decision.”\textsuperscript{47} In other words, “charitable relief-worthy transactions should promote ‘good things’—meaning a general category of public goods—through a process that reveals that some donors consider these ‘good things’ as socially undersupplied.”\textsuperscript{48}

Similarly, Saul Levmore argues that charitable contributions can be viewed as a means of “voting” on which organizations are worthy of financial support and proposes that the charitable deduction “essentially casts the government as a financing partner, with taxpayer-donors serving as intermediaries or agents who choose the providers of, or indeed the very existence of, certain services.”\textsuperscript{49} The deduction, unlike direct government funding,

\textsuperscript{47} Id.

\textsuperscript{48} Id. at 1083.

\textsuperscript{49} Saul Levmore, \textit{Taxes as Ballots}, 65 U. CHI. L. REV. 387, 388 (1998). \textit{See also} Miranda Perry Fleischer, \textit{Generous to a Fault? Fair Shares and Charitable giving}, 93 MINN. L. REV. 165, 229 (2008) (“charitable tax subsidies allow individuals whose preferences differ from [the median voter] to redirect a portion of funds otherwise flowing to the federal fisc toward their preferred visions of the public good”); McDaniel, \textit{supra} note 10, at 782 (arguing that the deduction both provides donors with a matching gift by the government and gives donors the ability to control who will receive donated funds).
may induce citizens not only to choose for themselves where
to apply personal and government funds, but also to develop
a sense of commitment to the chosen charities. Thus, they
become involved individually as volunteers in ways that they
would not if their tax money were simply allocated to the
charities by the legislature or by government bureaucrats.50

As a result, “[t]he charitable deduction scheme permits a kind of ongoing
vote.”51 While some may argue the deduction is unfair to lower-income
taxpayers who receive fewer of its benefits, Levmore counters that “the
government may need all the help it can get in monitoring and choosing
among hospitals, schools, social welfare agencies, and the like.”52

Mark Hall and John Colombo propose donative theory, another

50 Levmore, supra note 49, at 406. Levmore has been criticized for failing to explain
how the charitable deduction, an essentially nondemocratic allocation mechanism, is
consistent with the principles of democratic governance. Benshalom, supra note 10, at
1062-63.

51 Levmore, supra note 49, at 406.

52 Id.
variations on choice theory, which argues that “only those charitable organizations funded substantially by philanthropic donations deserve and should be entitled to the tax exemption.” While they focus primarily on the exemption from income tax that is available to many charitable organizations, the same standard can be, and essentially is, applied in determining whether an organization is entitled to the subsidy that results when donors are allowed to deduct donations to a tax-exempt organization. According to Hall and Colombo, “the fact that an entity can attract a substantial level of donations demonstrates its worthiness of and need for donations—hence, deservedness.” Because freeriding prevents the level of charitable donations from rising to the level needed to optimally satisfy public needs, the tax exemption (and, presumably, the charitable deduction) are needed to fill the funding gap. In sum,

although a majority of voters may resist paying the full cost of government directly providing certain goods and services,


54 Id.

55 Id. at 398.
a majority may be willing for government to ‘contribute’ to such production because, while they do not value the particular good or service enough to pay for all of it, they recognize that they would receive some marginal benefit from increased production and hence would be willing to pay for a portion of that increased production, especially if such agreement would permit a partial-cross-subsidy of their own special interest.\footnote{Mark A. Hall & John D. Colombo, The Charitable Tax Exemption 107-08 (1995).}

By selecting particular organizations from among the many available alternatives, donors “reveal those that are of special worth in the public’s estimation.”\footnote{Id.} The organization’s neediness is apparent because its “resort to solicitations evidences that its needs are not being met elsewhere.”\footnote{Id.} However, the donations themselves will not fully satisfy the organization’s needs, due in part to the fact that some donors will “free ride” on the contributions of others; as a result, an additional “shadow subsidy” is

\footnote{Id.}
needed “to take up the donative slack.” Hall and Colombo describe donative theory as “operat[ing] at the intersection of the failure of both private markets and the government.” In other words, the subsidy is necessary to counteract the apathy of individuals who are not actively opposed to the activities of charitable organizations but do not value their services enough to support a direct government subsidy for those organizations.

To the extent that the deduction is intended to promote pluralism among charitable organizations by providing donors with a choice in which organizations receive governmental support, as the choice theorists claim, McDaniel notes that such pluralism is confined mostly to that small percentage of donors who have a high enough income to benefit from the deduction. Given the fact that high income individuals generally give to different organizations than low income individuals, the pluralism argument “has a decidedly elitist cast to it.” Alice Gresham Bullock adds that, not

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59 Id.

60 Id.

61 Id.

62 McDaniel, supra note 11, at 391. See Part III, supra.

63 McDaniel, supra note 11, at 397. See also Surrey, supra note 12, at 725 (“[t]ax
only do high-income individuals tend to support “high-brow” organizations like public television, orchestras, and museums, but they are also more likely to patronize the programs offered by these organizations.  

William J. Turnier goes even further, arguing that the deduction for charitable contributions is the crass, political result of a “symbiotic relationship” between those taxpayers who claim the deduction and the charitable organizations themselves and that the justifications given for the deduction are no more than “lofty platitudes [] conjured up which serve[] as an altruistic fig leaf to cover over the self-interest of the masses and the politically powerful lobbying forces.”

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65 Personal Deductions and Tax Reform: The High Road and the Low Road, 31 VILL. L. REV. 1703, 1751 (1986). Similarly, David A. Good & Aaron Wildavsky argue the deduction is “truly uncontrollable” by Congress because “[i]t is not subject to annual or periodic congressional review and, within the tax system, there is no limit on how much a taxpayer can receive.” A Tax by any other Name: The Donor Directed Automatic Percentage Contribution Bonus, A Budget Alternative for Financing Government Support
D. CRITICISMS AND DEFENSES OF THE CHARITABLE DEDUCTION IN ITS CURRENT FORM

Some theorists, even when supporting the charitable deduction in general, find flaws in the way the deduction is currently implemented.

The charitable deduction, like all tax expenditures, provides greater benefits to those in higher tax brackets, although this effect can be mitigated or eliminated by, for example, using a credit rather than a deduction or by limiting the deduction to taxpayers below a certain income bracket. In

66 Surrey & McDaniels, supra note 10, at 103. See also Levmore, supra note 49, at 405 (“An obvious objection to the use of the charitable deduction as a social choice mechanism to determine government spending is that many citizens effectively are disenfranchised because they need not file returns or do not benefit from itemizing their deductions”). Evelyn Brody criticizes this feature of the deduction as unfair, since “the opportunity cost of virtue falls as one moves up the income scale.” Charities in Tax Reform: Threats to Subsidies Overt and Covert, 66 Tenn. L. Rev. 687, 695 (1999) (quoting Richard A. Musgrave & Peggy B. Musgrave, Public Finance in Theory and Practice 348 (4th ed. 1984)). See also Benshalom, supra note 10, at 1057 (“Because tax authorities can use means other than deductions to change behavior, deductions seem to be an inappropriate measure to achieve that end unless there is a special reason to change the
1977, the top 1.4 percent of taxpayers received 73.3% of tax expenditures resulting from the charitable deduction for education, 58.8% of tax expenditures resulting from the charitable deduction for health, and 43.2% of expenditures resulting from the deduction for all other charitable contributions. As suggested by Surrey and McDaniel, “[n]ot only are the tax expenditure provisions the primary cause of perceived tax inequity, but it also seems safe to say that they fail to achieve what most Americans would perceive to be a fair distribution of funds...” As a result, “the deduction appears to provide the greatest financial incentive to those who have the least financial need for one.” The situation is exacerbated by the particular behavioral patterns of high-bracket taxpayers”). However, Benshalom does suggest that such a reason may exist, since limiting the deduction to higher tax brackets may be an efficient way of targeting behavioral changes in taxpayers with more available income. He notes that “[s]ome may even claim that this arrangement is equitable if, as a result, rich people end up saving and consuming less for themselves and investing more in society.” Ultimately, he concludes that, “[r]egardless of its consequentialist outcomes, it is hard to see how the 170 deduction could be incorporated in a society that venerates the democratic, majority-based decision-making process.” Id. at 1068.

67 Surrey & McDaniel, supra note 10, at 71.

68 Id. at 172.

69 McDaniel, supra note 11, at 383. In response to those who argue that this “upside-down subsidy” is the natural result of our progressive tax structure, Surrey and McDaniel
fact that the vast majority of taxpayers who claim the deductions do so in amounts constituting less than the standard deduction. Consequently, “for the overwhelming majority of taxpayers the incentive is conditioned not on the act of charitable giving, but by the taxpayer’s status in life as a homeowner, installment purchaser, consumer of durable goods on which local sales taxes are levied, owner of a car, etc.”

respond as follows: “Although an individual’s tax burden under a progressive income tax will rise with income, it does not follow that government assistance should also rise with income; such a view is contrary to generally accepted notions of the terms on which government assistance should be granted.” SURREY & McDaniel, supra note 10, at 80. Similarly, they reject the argument that elimination of the charitable deduction would have the negative effect of increasing the “disposable income” of the rich in relation to the poor while reducing charitable contributions. Id. at 81. See also Surrey, supra note 12, at 719-20 (deductions “are worth more to the high income taxpayer than the low income taxpayer” and “do not benefit those who are outside the tax system because their incomes are low, they have losses, or they are exempt from tax”). But see Hochman & Rodgers (“[a]ny system in which people save taxes by giving to charity removes power from the majority and revests it in wealthy donors… [but] the poor perhaps should not complain that a deduction makes giving by the wealthy less costly if that savings prompts the wealthy to fund charities like the Red Cross or the Salvation Army which primarily benefit the poor”).

70 McDaniel, supra note 11, at 383.

71 Id. See also Brody, supra note 66, at 716 (noting that itemizers generally tend to live in areas with high state and local income taxes, another factor associated with wealth).
A related argument, raised by Charles T. Clotfelter, among others, is that even among those who itemize their deductions and therefore can take advantage of the tax incentive, the amount of benefit they receive depends on their marginal tax rate, which is greater for high-income individuals.  

In the words of Musgrave and Musgrave, “[a] philosopher-economist might observe that the opportunity cost of virtue falls as one moves up the income scale.” Because of the progressivity of marginal tax rates, those taxpayers in the highest tax brackets incur the lowest price per dollar for their charitable contributions, leading to an inefficient allocation of resources.

Bittker responds to this criticism of the “upside-down” nature of the deduction by arguing that it is the natural result of a progressive tax structure and protests that “you cannot hold up one as the authentic voice of the people, and condemn the other as a craven surrender to special privilege.”

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72 Clotfelter, supra note 3, at 672.

73 Id.

74 Id.

75 Bittker, supra note 18, at 54. See also John K. McNulty, Public Policy and Private Charity: A Tax Policy Perspective, 3 Va. Tax Rev. 229, 244 (1984) (arguing that, if philanthropy is only price sensitive in the higher income brackets, then concentrating the benefits of the deduction on those brackets may in fact be more efficient). Similarly, if we
progressivity of the tax structure by increasing either the width of the upper tax brackets or raising marginal rates, both of which would increase the tax burden on wealthier taxpayers while simultaneously granting a select group of them (i.e., charitable donors) some relief from that burden.\textsuperscript{76} Finally, he argues that, while the deduction’s role in our tax structure may work against vertical equity, the deduction itself may actually increase progressivity by encouraging wealthier taxpayers to transfer funds to those in lower tax brackets.\textsuperscript{77}

Like Bittker, John Simon argues that the inequitable effects of the charitable deduction on different tax brackets is an inevitable result of a progressive tax system:

\begin{quote}
Short of revolution or undreamt-of redistributitional legislation, affluent individuals will continue to have more
\end{quote}

\footnote{\textsuperscript{76} Bittker, supra note 18, at 55.}
\footnote{\textsuperscript{77} Id.}
discretionary income and wealth than poor individuals; they will therefore be better able to afford charitable gifts; and, accordingly, they will be in a better position to take advantage of any allowance or matching grant system…

[T]he present deduction arrangement represents only an exaggerated version of a more general power-and-privilege dilemma that will exist so long as people are allowed to take charitable gifts off their estate and income taxes…

Some critics of the charitable deduction claim that, to the extent its purpose is to incentivize contributions, it achieves that purpose inefficiently, because many of those contributions would be made even if they were not deductible. In other words, they believe that charitable giving is inelastic because it does not increase or decrease in response to changes in cost and


79 See, e.g., McDaniel, *supra* note 11, at 384 (“[t] o the extent there is an incentive effect, the deduction is an inefficient means of achieving the desired result”); Surrey, *supra* note 12, at 719-20 (charitable deduction is inefficient “because some of the tax benefits go to taxpayers for activities which they would have performed without the benefits”).
that, as a result, tax incentives to encourage giving have little effect.\textsuperscript{80} Bittker argues that the study most frequently cited in support of this claim, a doctoral dissertation by Michael K. Taussig, is both flawed and limited in scope.\textsuperscript{81} He also notes that subsequent studies have reached the opposite conclusion by discovering that charitable giving at both the individual and corporate level is quite elastic.\textsuperscript{82} Finally, he argues that “even those who profess faith in Taussig’s conclusions seem simultaneously to accept the conventional view that the deduction has a powerful incentive effect” by characterizing the deduction as a “subsidy” to charitable institutions.\textsuperscript{83} In his words, “[t]he same dollar of public money, after all, cannot be both a

\textsuperscript{80} See, e.g., Brody, supra note 66, at 715 (“[i]f the policy behind the charitable-contribution deduction is to spur donations, then tax subsidies are wasted on donations that would have been made anyway”). Brody notes that even high-income taxpayers may not be increasing their total contributions so much as shifting the timing of their contributions into those time periods when tax rates are higher. \textit{Id.} at 717. As evidence of the limited effect that the deduction has on giving, she notes that donations actually increased among most income levels when the charitable contribution deduction for non-itemizers expired, removing for many taxpayers any tax incentive to make charitable contributions. \textit{Id.} at 719.

\textsuperscript{81} Bittker, \textit{supra} note 18, at 44.

\textsuperscript{82} \textit{Id.} at 52.

\textsuperscript{83} \textit{Id.}
Gergen criticizes the charitable deduction for providing the same benefit to all charitable organizations, arguing that this ignores very important distinctions between those organizations and, in particular, the motivations behind giving. According to him, contributions made to churches may be the result of social pressure (since donations are often made public to other members), whereas donations made to public television are generally made with the expectation that the donor will receive something of value in the form of desired programming. In other words, he finds that subsidized donations are efficient in some situations and equitable in others. As a result, he finds the current form of deduction lacking in its failure to distinguish between the effects that donations to different organizations have on individual donors.85

Having considered the theoretical foundations of the charitable deduction, as well as the criticisms that have been made against the deduction in its current form, we should now consider how those charitable organizations that rely on the deduction are affected by negative changes to the economy.

84 Id.

85 Gergen, supra note 20, at 1450.
II. THE EFFECT OF AN ECONOMIC DOWNTURN ON CHARITABLE GIVING

While it is hardly surprising that charitable giving declines during recessionary years, charitable giving actually falls at a greater rate than gross domestic product (“GDP”) during an economic downturn. For example, during the most recent recession, charitable giving fell by over $11 billion between 2008 and 2009, even through GDP actually rose marginally during that time.\(^{86}\) Although charitable giving will gradually increase as the economy recovers, such giving tends to lag a year or more behind economic growth and generally takes three to five years to reach pre-recession levels.\(^ {87}\)

During an economic downturn, average income obviously decreases, which naturally would lead to a decline in charitable giving, even if

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charitable giving as a percentage of income were to remain static. However, those taxpayers who do experience a decline in income are unlikely to maintain the same level of charitable giving as a percentage of their income (i.e., a taxpayer whose income declines ten percent is likely to reduce his or her charitable contributions by more than ten percent), for the following reasons.

Unsurprisingly, “the more financially secure [an individual] feels, the more is given to charity, not just in absolute amounts but also as a percentage of income and net worth;” conversely, an increase in financial insecurity should lead to additional declines in charitable giving, for the following reasons.88 First, a decrease in income may send a taxpayer into a lower tax bracket, at which point the charitable subsidy becomes less valuable to him or her.89 Second, a decrease in income may lead a taxpayer to make changes that would affect his or her ability to itemize his or her deductions; for example, the taxpayer may end up selling his or her home


89 Yair Jason Listokin, Stabilizing the Economy through the Income Tax Code, 123 TAX NOTES 13 (2009). See also McDaniel, supra note 11, at 383 (noting that the deduction is of greater value to those in higher tax brackets).
and renting, which means he or she would no longer be able to deduct mortgage interest payments. A loss of the ability to itemize deductions would also mean a loss of the tax incentive provided by the charitable deduction.\footnote{\textit{Annual Report, supra note 87, at 23.}} Third, an individual facing a sudden and unexpected decrease in income, as a result of a job loss for example, may be forced to allocate all his or her income to necessities and may drastically reduce or eliminate discretionary expenses, including charitable donations.

Finally, even if a taxpayer’s income does not actually decline, he or she may be less willing to spend money on charitable contributions if he or she feels poorer or more insecure about his or her economic future. For example, a taxpayer who sees his or her friends, neighbors or co-workers losing their jobs may be reluctant to spend money on charitable contributions, even if he or she has not yet experienced any actual decline in income him or herself. Similarly, even if a taxpayer’s income has not actually declined, he or she may feel financially insecure, and therefore reluctant to give to charity, if the value of his or her assets, like a home or retirement fund, have declined.

Taxpayers may change not only the amount that they give but also the organizations to which they give during lean economic times, as can be seen
by the fact that not all non-profit organizations saw a decline in contributions during the most recent recession. For example, international organizations, environmental and animal-welfare organizations, health organizations and human services organizations all saw an increase in contributions in 2009. Religious and educational organizations and organizations devoted to culture, arts and humanities, on the other hand, did see a decline in contributions during that time.

The strain currently felt by charitable organizations is similar to the situation that existed in the 1970’s, in the midst of another economic downturn. At that time, the Commission on Private Philanthropy and

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91 Id. at 19. In fact, organizations dedicated to human services or public-society benefit actually show higher rates of growth during longer recessions. Giving during Recessions, supra note 9, at 7.

92 Id. This trend is also consistent with larger historical patterns, which indicate that contributions to educational organizations drop precipitously during sustained economic downturns and that contributions to organizations devoted to the arts, culture and humanities drop more than contributions to other organizations during economic slowdowns (which are smaller than recessions). Id. at 7, 14.

93 GIVING IN AMERICA, supra note 1, at 70 (1975) (“[W]hile private giving is still large in the United States by comparison with other countries, and while it has grown continuously in current dollar measurements ever since estimates of philanthropy have been compiled, it has not kept pace with the growth of the economy over the last decade,
Public Needs (the “Filer Commission”) concluded that non-profits faced particular challenges during a recession because so much of their activities involved the provision of services rather than the manufacture of products.\textsuperscript{94} The rising costs of labor left non-profits at a disadvantage in comparison to other sectors of the economy during a recession, particularly since those other sectors could take advantage of labor-saving technology and economies of scale.\textsuperscript{95} These strains continue today, when “80 percent of nonprofits have experienced significant economic stress, with more than a third indicating the stress is ‘severe’ or ‘very severe.’”\textsuperscript{96}

Moreover, many charitable organizations experience an increase in demand for their services during an economic downturn. For example, food banks in major metropolitan areas experienced an increase in demand of around 35%, and the Cleveland Food Bank reported distributing an

\textsuperscript{94} Id. at 83.

\textsuperscript{95} Id.

additional 1.5 million pounds of food in 2008 over the previous year.97 Additionally, the 2009 Annual Homeless Assessment Report to Congress stated that “almost 62,000 more family members were in shelter at some point during 2009 than had been during 2007, making up almost 40,000 families.”98 Animal shelter admissions at PAWS Chicago increased from


98 2009 Annual Homeless Assessment Report to Congress, p. 5. The report further notes that

The continued growth in sheltered family homelessness almost certainly reflects the ongoing effects of the recession. When compared to 2008, a slightly higher proportion of families came from housed situations, most commonly staying with family. The fragile economic circumstances of the relatives of struggling parents may mean that, as soon as job losses begin in an economic downturn, support networks for families at risk of homelessness fall apart. Doubled-up housing situations cannot be sustained, cash is no longer available to help others with rent payments, and families turn to homeless shelters as the only way of keeping a roof over their heads.
In light of the fact that an economic downturn appears to have a significant negative effect on charitable organizations, the question then becomes whether the government should try to mitigate that effect through changes to the charitable deduction. In order to answer this question, we must first consider whether such a change would be supported under the primary theories that support the deduction.

III. **DO CURRENT THEORIES SUPPORT THE IDEA OF INCREASING THE SUBSIDY TO CHARITABLE ORGANIZATIONS DURING A RECESSION?**

Because expenditure theory argues that contributions to charitable organizations should be deductible due to the nature of the goods and services those organizations provide, expenditure theorists would be unlikely to support any changes to the deduction that are based on the state of the economy rather than any fundamental changes to those goods and services.

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services. However, both subsidy theory and choice theory are consistent with the idea of adjusting the charitable deduction during a recession in order to stimulate charitable giving.

A. Subsidy Theory

Subsidy theorists argue that the charitable deduction is necessary to prevent the underfunding of public goods and services.\textsuperscript{100} The collective nature of these goods allows some taxpayers to enjoy them without paying for them; by providing a subsidy to all eligible organizations, the charitable deduction spreads the cost of these goods across all taxpayers, including the “freeriders.”\textsuperscript{101} As noted above, charitable giving drops during a recession; because this drop outpaces the decline in the economy as a whole, it appears that freeriding increases during a recession, since the amount people are paying for public goods declines without any accompanying decline in the demand for those goods (and, in some instances, is accompanied by an actual increase in demand, as will be discussed below).\textsuperscript{102} If the charitable

\textsuperscript{100} Gergen, supra note 20, at 1397.

\textsuperscript{101} Id.

deduction is intended to address the issue of freeriding, as the subsidy theorists argue, then an increase in the deduction is warranted when an increase in freeriding outpaces changes in the economy as a whole.

B. Choice Theory

Choice theorists argue that the charitable deduction serves not only as a subsidy to charitable organizations but also as a mechanism for providing a voice to donors who wish to express a preference regarding which organizations should receive governmental assistance.\(^{103}\) Whether the deduction is seen as a means of “voting” or as a means of allowing taxpayers to demonstrate an organization’s deservedness of a donation, choice theorists argue that it serves the goal of promoting pluralism among organizations.\(^{104}\) However, in the same way that more donors move from the category of active donors to freeriders during a recession, the number of taxpayers expressing their choice of particular charitable organizations through monetary donations also declines during a recession. If the goal of the charitable deduction is to promote pluralism among organizations by

\(^{103}\) Levmore, supra note 49, at 388; Hall and Colombo, supra note 53, at 1383-84.

\(^{104}\) Levmore, supra note 49, at 388; Hall and Colombo, supra note 53, at 1383-84.
providing taxpayers a means for expressing their preferences for which organizations should be subsidized, then the loss of taxpayers who are able to express that choice should be an issue of concern for supporters of the charitable deduction.

Having determined that changes to the charitable deduction during an economic downturn are justified under both subsidy and choice theories, the question then becomes whether modifications in the charitable deduction should be aimed at all charitable organizations or only those that experience both a decline in contributions and an increase in demand during a recession.

A. Who Should Benefit?

In 2009, 1,238,201 organizations had registered with the Service as nonprofit, charitable organizations under Section 501(c)(3) of the Internal Revenue Code (the “Code”), up from 819,008 in 2000, an increase of over 50%. The massive growth in both the number and types of tax-exempt nonprofit organizations begs the question of whether all organizations registered as tax-exempt with the Service should be entitled to favorable treatment during an economic downturn.

105 Annual Report, supra note 87, at 27.
For our purposes, charitable organizations can basically be divided into three different categories based on how an economic downturn affects their income on the one hand and their expenses on the other. The first group consists of those organizations, like food banks and animal shelters, that see an increase in both the income they receive from contributions and the demand they see for their services.106 Because such organizations help the needy, they naturally see an increase in demand during an economic decline; however, because donors are generally able to identify such organizations as ones that will need more assistance during tough economic times, they may increase their donations to such organizations, even if such efforts come at the expense of aid to other organizations.107

The second category consists of those organizations that experience increases in demand without concomitant increases in contributions because donors do not anticipate that those organizations will need more money during an economic downturn. For example, demand for the services provided by domestic violence shelters and legal service providers rose

106 See Giving during Recessions, supra note 9, at 11 (“Recent growth in giving to [human services], while very encouraging, reportedly does not do enough to help social service agencies keep up with growing needs for shelter, food support, and other types of assistance sought by people during economic crises”).

107 Id.
dramatically during the recent recession, the latter by as much as 400%. Because donors may be less aware of the increased need for the services provided by such organizations during an economic downturn, funding to such organizations either stays stagnant or decreases; as a result, they may find themselves unable to keep up with increased demand and may end up turning potential beneficiaries away.

The final category consists of those organizations that do not necessarily experience any increase in demand for their services but do experience a decline in donations during a recession, like educational organizations and organizations devoted to culture, arts and humanities. Even though such

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108 In addition to the problems brought on by decreased contributions and increased demand, charitable organizations also face increasing pressure from governmental regulators. In particular, Nina J. Crimm has found that state and local authorities increasingly challenge the tax-exempt status of non-profit organizations during economically difficult times, noting that “financially strapped state and local governments have targeted nonprofits as one means of resolving their pinched monetary and tax base dilemmas.” Why All is Not Quiet on the “Home Front” for Charitable Organizations, 29 N.M. L. Rev. 1, 29 (1999). Additional challenges may come from cuts in federal spending for social programs, as occurred under President Ronald Reagan in the 1980’s, which “reduced an important revenue source for nonprofit organizations at the same time it increased demand for many of their services.”

organizations do not necessarily experience an increase in expenses during an economic downturn, they may nonetheless see such a drop in contributions that they find themselves unable to operate under a decreased budget and be forced to either reduce their staffs or close down entirely. This outcome may be sub-optimal if donors reduced or eliminated their contributions based on the belief that the organization could continue without their contributions. Moreover, the costs of maintaining the organization through an economic downturn, e.g., through additional tax expenditures resulting from changes to the charitable deduction, may be less than the costs of disbanding the organization during a recession only to re-establish it after the economy has turned around.

In looking at these three groups of organizations, the question becomes whether the distinctions between them warrant differential treatment in terms of which organizations should receive any sort of favorable tax treatment during a recession. In other words, should the proposals discussed below target only one or two of these categories, or should they apply to all such organizations without distinction?

The idea of tax measures that distinguish between different types of charitable organizations is certainly not unprecedented. For example, the Filer Commission separated out organizations, like those dedicated to welfare rights and minority business enterprises, that strive “to empower the
powerless of American society, often non-white, non-middleclass groups that through their own resources have been able to exercise little influence on the priorities and processes of majoritarian government or of other institutional areas of our society.”\textsuperscript{110} According to the Commission, such organizations differ from “old-style charity” that aims to fill the basic needs of the underprivileged, since they are focused instead on “helping groups to organize and act so as to be able to effectively exact social and economic and political benefits or ‘rights’ from society and its institutions.”\textsuperscript{111}

Congress has also previously distinguished among various groups recognized as tax-exempt under Section 501(c)(3). For example, in 1954, they increased the maximum allowable deduction for charitable contributions from 20\% to 30\%, but limited the additional 10\% deduction to those contributions made to churches, religious orders, educational institutions, and hospitals.\textsuperscript{112} Congress specifically targeted these organizations because they perceived that these particular institutions were

\textsuperscript{110} \textit{Giving in America, supra} note 1, at 67-68.

\textsuperscript{111} \textit{Id.}

suffering from rising costs and modest returns on endowments.\textsuperscript{113} Over time Congress increased the number of organizations to which the increased deduction applied, eventually expanding it to apply to all exempt organizations “that receive a substantial part of their support from a governmental unit or from the general public.”\textsuperscript{114} Later, when Congress limited the amount of the maximum deduction for charitable contributions to 50\% of adjusted gross income, it nonetheless allowed a carryover for contributions made to churches, educational organizations, health care organizations, and private foundations.\textsuperscript{115}

Similarly, the Service has occasionally drawn distinctions among charitable purposes, usually in the wake of a disaster. For example, after the terrorist attacks on September 11, 2001, the Service agreed to treat payments made to victims or their families as being “related to the charity’s exempt purpose.”\textsuperscript{116} Similarly, after Hurricane Katrina in 2005, the

\textsuperscript{113} Id.

\textsuperscript{114} Id.

\textsuperscript{115} Id. \textit{See also} Simon, Dale & Chisolm, from Non-Profit handbook- 277.

deduction limitation for charitable contributions was temporarily lifted, presumably to encourage giving to victims of the disaster, and an additional tax exemption was given to individuals and organizations who housed those who had been displaced.117 Additionally, the mileage rate for charitable use of a vehicle for purposes of hurricane relief was increased, and, in the alternative, taxpayers were allowed to exclude from their income reimbursement for use of a vehicle for those purposes.118 Other measures included providing tax relief to those who either donated books to public schools or who donated food inventory.119 After Hurricanes Rita and Wilma, Congress instituted the GO Zone Act, which provided even broader tax incentives to those who contributed to hurricane relief efforts.120

These efforts to encourage charitable giving in the wake of national emergencies, while clearly done with the best of intentions, have

117 *Id.*

118 *Id.*

119 *Id.*

120 *Id.* Such targeted measures have not been limited to domestic disasters; after the Asian tsunami, Congress allowed contributions made for tsunami relief in January, 2005 to be deducted on the tax returns for the 2004 year. Danshera Cords, *Charitable Contributions for Disaster Relief: Rationalizing Tax Consequences and Victim Benefits*, 57 CATH. U. L. REV. 427, 448 (2008).
nonetheless created some significant problems. For example, Patrick Tolan describes difficulties in coordination between the government and charitable organizations, and among the charitable organizations themselves.\footnote{Tolan, supra note 116, at 799 (2007).} Furthermore, so long as such measures take the form of increased deductions, they are subject to the same criticisms that are often leveled at the deduction system as a whole, namely that they favor the rich over the poor.\footnote{Ellen P. Aprill & Richard L. Schmalbeck, Post-Disaster Tax Legislation: A Series of Unfortunate Events, 56 Duke L. J. 51, 88-89 (2006). See also Tolan, supra note 116, at 799 (noting that only extremely wealthy taxpayers benefit from the removal of the cap on deductions and that only taxpayers who itemize their deductions benefit from such tax relief measures).}

Tolan further notes that contributions are not always spent immediately, despite the fact that the tax measures are often intended to stimulate the local economy.\footnote{See Tolan, supra note 116, at 799 (noting as well that only taxpayers who itemize their deductions benefit from such tax relief measures).} Implementing similar measures in response to an

\begin{enumerate}
\item Tolan, supra note 116, at 799 (2007). Professor Tolan also notes that, with respect to geographically specific opportunity zones that are often created after natural disasters, “strong incentives without adequate controls could be counterproductive, harming those the legislation was intended to benefit.” Patrick Tolan, Questioning Tax Expenditures for Economic Recovery, 127 TAX NOTES 67, 69 (2010).
\item Ellen P. Aprill & Richard L. Schmalbeck, Post-Disaster Tax Legislation: A Series of Unfortunate Events, 56 Duke L. J. 51, 88-89 (2006). See also Tolan, supra note 116, at 799 (noting that only extremely wealthy taxpayers benefit from the removal of the cap on deductions and that only taxpayers who itemize their deductions benefit from such tax relief measures).
\item See Tolan, supra note 116, at 799 (noting as well that only taxpayers who itemize their deductions benefit from such tax relief measures).
\end{enumerate}
economic “disaster” presents similar concerns, since one of the main goals of fiscal policy during a recession is to stimulate spending. Yet another problem with the tax provisions implemented after Hurricanes Katrina, Rita, and Wilma was that they created artificial distinctions based on which specific disaster was involved. As Tolan notes, “it is nonsensical that mileage allowances are higher for volunteers who engaged in Hurricane Katrina relief efforts than those who responded to Hurricanes Rita or Wilma, or to any other disaster for that matter.” He further argues that direct payments to individuals affected by the disaster may have been counterproductive with respect to the local economy because they “may have served as a disincentive to laborers, whom local businesses could have put to productive use.” Another concern that may arise from targeting particular charitable organizations for tax relief is whether organizations

124 Listokin, supra note 89, at 13.

125 Tolan, supra note 116, at 799. Professor Tolan cites similar problems with respect to federally designated enterprise zones, since “similar taxpayers should be treated similarly, yet in these zones there is an indisputable advantage to taxpayers who can enjoy the many tax incentives.” Tolan, supra note 121.

126 Id. (noting as well that only taxpayers who itemize their deductions benefit from such tax relief measures).
will be equipped to handle the resulting increase in contributions.  

Other attempts to distinguish between charitable organizations have focused more specifically on poverty relief, including a proposal made in 1995 by Representatives Joseph Knollenberg of Michigan and James T. Kolbe of Arizona that would have provided a credit to taxpayers who donate to organizations that provide services to individuals whose incomes are near poverty levels.  

Implementation of similar measures during an economic downturn would be akin to targeting those organizations that see an uptick in both supply and demand during those times. Such proposals have been criticized by, among others, Bullock (who ultimately supports

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127 See, e.g., Robert A. Katz, A Pig in a Python: How the Charitable Response to September 11 Overwhelmed the Law of Disaster Relief, 36 Ind. L. Rev. 251, 331 (2003) (noting that “[t]he outpouring of charitable contributions following 9/11 not only strained the logistical abilities of many [charitable organizations], it also overwhelmed key parts of the legal regime that governs them”). Such problems may be exacerbated when the goals of the charity and involve particularly sympathetic and media-genic individuals. Gergen, supra note 20, at 1409 (noting the case of Jessica McClure, the girl rescued from a well in Texas). With few exceptions, such intense media focus on a few individual victims is less likely during an economic downturn, which tends to be more prolonged and diffuse than a natural disaster or other emergency.

128 House Bill 2225. A similar proposal was made separately by Representative Kolbe in 2001.
such measures). She describes the administrative problems associated with
determining how such organizations are actually using their funds and
argues that “many national charities that fight poverty do not limit their
services to just the needy and thus may not qualify as donees for the
credit.” 129 She further notes that such distinctions “may create a deeper
divide between the poor and the rest of the community.” 130 Lawrence B.
Lindsey further criticizes the proposals, arguing that such measures “would
lead to a multitude of other special interests lobbying Congress to enact
provisions favorable to their causes as well.” 131

Gergen, on the other hand, argues that “it is ludicrous that sports
museums, jazz festivals, and singing groups are treated as charities.” 132
Because such organizations may receive adequate support in other ways,
and because “it is implausible that gifts to these charities are altruistic in
motive,” he proposes removing such organizations altogether from the
realm of tax-exempt organizations, which he argues should be limited to

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129 Bullock, supra note 64, at 358.

130 Id.

131 Lindsey, supra note 112, at 1089.

132 Gergen, supra note 20, at 1450.
what he calls “social welfare” organizations. Similarly, Halstead and Lind propose allowing a higher deduction for contributions to organizations, like the Salvation Army and soup kitchens, “which are entirely dedicated to providing direct care to the neediest,” while retaining a lower deduction for contributions to organizations, like churches, schools, and arts organizations, which only indirectly serve the public interest.

Charles Borek argues that Congress should “[decouple] the concept of charitable exemptions and deduction from other tax favored activities” by reserving the term “charitable” for those organizations whose primary purpose is to benefit the poor. In his words, “[i]t is nonsensical that, for legislative, budgetary, and policy evaluation purposes, private funding for

133 Id.

134 Simon, Dale & Chisolm, from Non-Profit handbook 277

135 Charles A. Borek, Decoupling Tax Exemption for Charitable Organizations, 31 WM. MITCHELL L. REV. 183, 219-20 (2004). Other scholars have focused on the distinction between religious and secular organizations. For example, Hochman and Rodgers argue that giving to religious organizations should be favored because such organizations do not benefit from direct governmental support. On the other hand, Schaefer argues that religious giving should be treated less favorably because religious organizations often use funds to maintain their own internal structures and support activities aimed at their members.
the relief of poverty is lumped together with fostering amateur sports competition and the prevention of cruelty to animals, among other things.\textsuperscript{136} Narrowing the definition of charitable in this manner would allow both taxpayers and the government to better “assess the effectiveness of private aid to the poor, and determine when and if direct subsidies are advisable.”\textsuperscript{137} According to Borek, focusing on organizations aimed at serving the needy may be warranted in light of the fact that “[c]haritable giving to organizations benefiting the neediest sector of the population is relatively modest.”\textsuperscript{138}

Simon counters that any requirement that charitable organizations serve the needy would surely be met with the objection that modern-day

\textsuperscript{136} Id. Borek does, however, note that “[o]ther non-charitable enterprises, such as those principally organized for religious, educational, or health related purposes, may, and in fact do, assist the poor with economic transfers and services. It would be administratively unfeasible to distill the charitable functions from the primary endeavors of these entities” Id. at 223.

\textsuperscript{137} Id.

\textsuperscript{138} Lindsey, supra note 112, at 1086. (finding that only three of the top twenty-five recipients of charitable contributions in 1999 were dedicated to poverty relief).
charity and modern-day charitable tax law serve other important values. Weighing this objection would take us back to basics—to the search for a rationale for exemption or deductibility, or indeed to even more fundamental issues relating to the primacy of redistributonal norms in American law.\textsuperscript{139}

Clotfelter points out that, to some extent, the current tax system already discriminates among entities. In particular, high-income taxpayers receive a higher subsidy than low-income taxpayers due to their higher tax bracket.\textsuperscript{140} Consequently, the charitable organizations supported by high-income taxpayers—including higher education and cultural institutions—are in essence “favored” by the current tax system over those charitable organizations favored by low-income taxpayers—primarily religious organizations.\textsuperscript{141} Clotfelter notes that such favoritism may be justified if the former have a greater external benefit to those outside the organization, although he admits that there is currently no conclusive answer to that

\textsuperscript{139} Simon, Dale & Chisolm, from Non-Profit handbook

\textsuperscript{140} See Section I.B, \textit{supra}.

\textsuperscript{141} Clotfelter, \textit{supra} note 3, at 18.
question.\textsuperscript{142}

The public, at least, seems to have some strong ideas regarding which organizations deserve the most support during economic downturns, as demonstrated by the fact that their giving to some organizations, such as those directed at serving the poor, increases, while their giving to other organizations, such as those focused on the arts, decreases during those times. A survey conducted by \textit{Parade} magazine seems to bear this out, finding that respondents, when given a hypothetical amount of money, allocated the greatest amount to food and shelter for the needy and to research on curing disease and allocated the least amount of money to promoting world democracy and to the visual and/ or performing arts.\textsuperscript{143} Corporate donors may also shift their charitable donations in response to an economic downturn, with some refocusing their donations “towards the provision of urgent needs, such as homelessness, hunger, and job development initiatives, and away from arts and culture.”\textsuperscript{144} This “focus on

\textsuperscript{142} \textit{Id.}

\textsuperscript{143} Giving USA 2010: Giving by Individuals, The Center on Philanthropy at Indiana University, at 5, \textit{available at} http://www.givingusa2010.org.

vital needs” is similar to what occurred during the Great Depression, according to Patrick M. Rooney of the Center on Philanthropy.145 Perhaps in response to these trends, Colombo and Hall have argued that only organizations that receive a substantial level of support from the general public merit subsidization.146

Further line-drawing, if intended to stimulate giving to charities that provide basic human services, may ultimately be futile, according to a study by Michelle H. Yetman and Robert J. Yetman. They “find that donations to charities that provide basic goods and services to humans in need appear to be unresponsive to tax incentives, while donations to charities that appeal to higher human needs, animals, and the environment are very sensitive to tax incentives.”147 In other words, those charities that many people consider the “worthiest” during an economic crisis are the least likely to receive much

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145 Annual Report, supra note 87, at 27.

146 Hall & Colombo, supra note at 53, at 1385.

benefit from additional tax relief. Additionally, the administrative costs related to distinguishing among charitable organizations (and enforcing those distinctions) should be taken into consideration, since those costs may be greater than any benefit that would be derived from such distinctions.

One of the strongest arguments against favoring certain charitable organizations over others is that those organizations that are commonly perceived as less “needy” during economic downturns are likely to receive fewer donations even as they continue to need support to maintain their services. This criticism has been leveled against the measures implemented after various disasters; for example, Danshera Cords argues that “[d]onations directed to benefit the victims of a mega disaster may leave

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148 Professor Clotfelter also found differences in elasticity to various nonprofit organizations, noting that donations to religious non-profit organizations are somewhat less elastic than donations to secular ones, although he concluded that “the evidence regarding the price elasticity does not, on the whole, support the notion that religious giving is less price-sensitive than giving for other purposes.” Clotfelter, supra note 3, at 12. Although Professor Clotfelter’s study does not look specifically at charitable giving during a recession, it does suggest that charitable giving to secular non-profits, at least, might increase if the cost of such giving were to decrease due to changes in the charitable deduction. Id.

149 Id.
less aid available to victims of less well publicized and smaller disasters.\textsuperscript{150} Similarly, aiming tax relief at certain types of organizations, such as those dedicated to poverty relief, may lead to drastically fewer donations for other organizations that, while less appealing to those donors who want to feel like they are helping those in need, are nonetheless both worthy of and in need of donations. For example, arts and culture organizations tend to be particularly hard hit during economic downturns and generally face additional hurdles in raising donations.\textsuperscript{151}

\textsuperscript{150} Cords, supra note 120, at 439.

\textsuperscript{151} Giving USA 2010: Giving by Corporations, The Center on Philanthropy at Indiana University, at 3, available at http://www.givingusa2010.org (citing Bloomberg News, Berman Says Corporate Giving May Fall 5%-10% in 2009, December 23, 2009, available at http://www.clipsyndicate.com/video/playlist/10834/1226135; S. Hoye, Painting a Grim Picture, THE CHRONICLE OF PHILANTHROPY, January 15, 2009). Nonetheless, Professor Tolan finds little evidence of “donor fatigue,” i.e., of donors shortchanging other charitable causes in order to focus on disaster relief, since contributions aimed specifically at disaster relief made up only three percent of all contributions even after special measures were implemented. Tolan, supra note 116, at 799 (noting as well that only taxpayers who itemize their deductions benefit from such tax relief measures). See also Stephanie Strom, Many Dismissing ‘Donor Fatigue’ as Myth, N.Y. TIMES, April 30, 2006, at A22 (noting that over three-fourths of charitable organizations raised as much or more in 2005, the year of Hurricane Katrina, than they had in the previous year). Strom notes that “[m]ore and more leaders of nonprofit groups are dismissing donor fatigue as a myth” that is
According to Colombo and Hall, the charitable deduction is necessary to compensate for the failures of not only the private markets (due to free riding) but also the public sector (due to a lack of information about donor preferences). The question then becomes whether this dual failure strikes some organizations harder than others during an economic downturn. As noted in the previous paragraph, free riding may impact some organizations more than others in a recession. At the same time, if only those donors who continue to have funds available to donate during a recession will have their preferences heard, then perhaps we should focus on maintaining aid to all organizations.

As Hall and Colombo note in their discussion of which charitable organizations in general are worthy of tax exemption, “[i]n addition to guarding against subsidization of activities that are unworthy or that simply do not need support, an ideal concept of charity in the tax exemption arena should guard against oversubsidization (or undersubsidizing) those activities that are deserving.”152 Because donors may already allocate unsupported by any evidence. *Id.* For example, Delane Butler of the United Way suggests that disasters like Katrina can lead to increased donations to other, unrelated organizations by raising awareness of philanthropy in general. *Id.*

money to those charities that seem most relevant to an economic crisis, additional attempts to further direct donations to particular types of charities seem both unnecessary and potentially harmful to those organizations that may not be as readily able to demonstrate increased need. As a result, this article argues that the tax incentives outlined below should apply to all organizations, regardless of category.

Extending the benefits of the charitable deduction to all organizations is consistent with subsidy theory, which argues that the deduction is aimed at alleviating the effects of free-riding across all types of organizations, not just those that serve the needy. Similarly, because choice theory rests on the notion that the deduction gives donors the right to express which organizations they believe should receive governmental support, any measures that provide greater tax incentives to some organizations over others would run counter to the goals of that theory. For all these reasons, the proposals aimed below are designed to apply to all charitable organizations without differentiating among them.

Having looked at how changes to the charitable deduction during a recession are supported by both subsidy and choice theories, the question then becomes which changes will best achieve the desired end result under those theories. The following section reviews proposed changes to the deduction that have been made and examines which of these proposals
would best achieve the goals of the charitable deduction during recessionary
times, looking first at individual donors and then at organizational
donors.  

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153 One of the first issues that arises when discussing the treatment of charitable
ccontributions during an economic downturn is how to determine when an economic
downturn has reached a phase where emergency measures should be implemented. One
possibility is to implement certain measures automatically whenever the gross domestic
product dips below a certain benchmark or falls below a certain percentage; this is
essentially the approach adopted by Professor Listokin in his proposals to stimulate the
American economy. Listokin, supra note 89, at 13. Alternatively, such measures could be
implemented whenever the gross domestic product falls for more than two consecutive
quarters, consistent with the conventionally accepted definition of a recession. Subsidy
theory and donative theory both argue in part that a deduction for charitable contributions
is necessary to alleviate the problem of free-riding with respect to certain communal goods
and services. Arguably, free-riding becomes a greater problem during a recession, because
many people who would have been donors during flush times switch over to become free
riders during a recession, in part because many donors lose their jobs and hence their
sources of income. If the goal of the charitable deduction is to address this particular issue,
then perhaps special measures are most justified when unemployment numbers dip below a
certain rate, since this would presumably be correlated with many former donors becoming
free riders. Although the need for a definitive benchmark is apparent, determining an
appropriate one is beyond the scope of this Article.
MITIGATING THE EFFECTS OF AN ECONOMIC DOWNTURN ON CHARITABLE CONTRIBUTIONS

IV. PROPOSALS

A. Individual Donors

Proposals aimed at individual donors should have the greatest impact on charitable giving, since individuals gave over $227.41 billion in 2009, representing about 75% of all contributions. While some measures aimed at individuals, like lifting the cap on the current deduction for contributions, allowing volunteers to deduct the value of volunteering, and increasing the rate of the deduction, may have some impact on levels of charitable giving, I argue that the most effective way to stimulate giving by individual donors during a recession is to convert the current deduction to a tax credit that is available to all donors.

154 Annual Report, supra note 87, at 11.

155 Some measures, while initially promising, are clearly non-starters. For example, in 2001, Congress proposed allowing individuals over age fifty-five to make penalty-free withdrawals from their retirement accounts in order to make charitable contributions. Annual Report, supra note 87, at 11. The drawbacks of such a measure are clear; not only would it incentivize people to spend money intended for their retirement, it would, if implemented during an economic recession, encourage people to remove money from their accounts at a time when those accounts are likely to be at their lowest values. Another possibility may be to encourage non-cash contributions. In 2007, 23.8 million individuals reported $58.7 billion in deductions for their non-cash contributions. Id. Corporate stock
1. Lift Cap on Charitable Deduction

One administratively simple way to stimulate charitable giving would be to raise the cap on deductibility for charitable contributions, currently set at fifty percent. One proponent of lifting the cap, Boris Bittker, argues that “[f]or those who fear that we will be unable to carry on as a nation if everyone adopts the practice of giving all of his income to charities, I suggest there are greater dangers on the fiscal horizon to which they could turn their attention with profit.”

While lifting the cap on deductions may seem to be a fairly straightforward way to increase donations, particularly during an economic downturn, donations accounted for almost half of these contributions, followed by donations of clothing and land. Pearson Liddell & Janette Wilson, Individual Noncash Contributions, 2007 (2010). While adjustments to the treatment of non-cash contributions may be desirable, the focus of our inquiry should nonetheless be on the tax treatment of cash donations, since they constitute the bulk of all charitable contributions. Id.

The Obama administration is unlikely to support lifting the cap on the charitable deduction, since it recently proposed legislation that would extend the reach of the current cap.

Id. at 62.
downturn, the measure does have its critics. Tolan, in his critique of the lifting of the cap as part of the Katrina Emergency Tax Relief Act of 2005, notes that the measure “violates vertical equity, because only those with donations above the suspended limits would benefit.” As he notes, “[t]hose likely to benefit the most would have to have sufficient wealth to be able to subsist on less than fifty percent of their AGI.”

Fleischer argues that the charitable deduction represents a “bargain” between two groups of donors, the “classic majority and the new majority,” in which “[t]he classic majority will fund the new majority’s minority-preferred projects only to the extent the new majority agrees to fund the classic majority’s preferred projects, and vice versa.” Given this system, “[l]imiting an individual’s charitable deduction to half of her income implements this bargain by ensuring that the amount of governmental subsidy to her preferred minority projects will not exceed the amount of taxes she pays to fund the classic majority’s project.” If Fleischer is correct, then lifting the cap could disrupt this delicate balance.

158 Tolan, supra note 116, at 799.

159 Id.

160 Fleischer, supra note 49, at 229.

161 Id.
The greatest advantage, or disadvantage, of lifting the cap on the charitable deduction lies in the fact that it would have the largest effect on wealthy donors. One argument in favor of lifting the cap, and in doing so focusing our efforts on high-income donors, is that such a measure would stimulate giving on those donors who tend to give the most to charity. After all, while the average individual taxpayer who claimed the charitable deduction gave less than $5000 on average in 2007, households with more than $100,000 annual income gave an average of almost $9000, while households with more than $200,000 annual income gave an average of over $22,000, more than four times the average amount across all taxpayers. Moreover, targeting high-income donors may be desirable from a distributional justice perspective, since “an appealing aspect of encouraging charity from the wealthy is that it induces them to increase their support of public goods.” In other words, donations by wealthy individuals essentially act as a form of voluntary redistribution that places the burdens of giving on those who are best able to bear them.

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164 Id.
Some critics argue that focusing on the wealthy is unfair because they will then disproportionately receive the benefits of the subsidy, i.e., the pleasure of making a donation. However, David Schizer counters that this does not in fact raise any such problems, since wealthy donors essentially “pay for” this benefit as a result of the progressive tax rate schedule. David A. Good and Aaron Wildavsky, on the other hand, argue that any measure that disproportionately benefits wealthy donors erodes legitimacy in the tax system; they argue that, “[b]y allowing some individuals to substantially decrease their tax bills by means of charitable contributions, public confidence in the fairness of the tax system is diminished.”

The strongest argument against lifting the cap is that it may not have much effect and would be nothing more than a superficial remedy aimed at those who are simply looking for a feel good way to argue that they are taking some action to help charitable organizations without actually doing anything. As Nancy Knauer notes,

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165 Id.

166 Id.

167 Good & Wildavsky, supra note 65, at 2400.
MITIGATING THE EFFECTS OF AN ECONOMIC DOWNTURN ON CHARITABLE CONTRIBUTIONS

[The most widely-touted tax incentive [of the Economic Recovery Tax Act of 1981] was the increase in the ceiling limitation on the charitable contribution deduction from five percent to ten percent of the corporate taxpayer’s “contribution base.” In the end, the increase represented a case of wishful thinking because virtually no [corporate donor] sustained contributions that even approached the old five percent limit.168

Among all individuals who claimed a charitable contribution on their tax return, the average contribution was only $4708 in 2007, far below 50% of adjusted gross income for most taxpayers.169 Even taxpayers with incomes greater than $200,000 contributed an average of only $22,418 in 2007, which is less than even the 20% threshold set for donations to some organizations.170

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170 Id. Currently, the Obama administration has proposed reducing the rate at which
Retaining the cap on the charitable deduction does little to advance the goals of subsidy or choice theory, both of which rely on a large pool of donors having an incentive to participate in the charitable sector. As a result, while lifting the current 50% cap may be an administratively simple measure to implement, the measure runs counter to the goals of the charitable deduction and presents little upside in terms of increased aid to charitable organizations.

2. Allow Donors to Deduct Volunteer Services

Another way of encouraging individuals to provide assistance to charitable organizations is by allowing them to deduct time spent volunteering at such organizations. Currently, taxpayers are not allowed to deduct the value of volunteer services they provide to charitable organizations, although they may deduct some of the expenses they incur as individual donors may deduct their charitable contributions from 35 percent to 28 percent; such a proposal is estimated to decrease charitable giving by more than $7 billion a year. Giving USA 2010: Giving by Individuals, The Center on Philanthropy at Indiana University, at 5, available at http://www.givingusa2010.org (citing Martin Feldstein, A Deduction from Charity, WASHINGTON POST, March 25, 2009).
a result of volunteering.\textsuperscript{171} Although the donation of time is not deductible, while the donation of money or goods is, the effect on those taxpayers who itemize their deductions (and therefore are allowed to deduct their tangible donations) is essentially the same regardless of the form their donation takes.\textsuperscript{172} For those taxpayers who do not itemize their donations, and therefore would not be able to deduct donations of goods or services, volunteering is more advantageous from a financial standpoint.\textsuperscript{173}

The number of Americans who formally volunteered with charitable organizations rose by about one million in 2008 over the previous year, to 61.8 million, or about 26.4\% of the adult population.\textsuperscript{174} These volunteers contributed about eight billion hours of service, which had an estimated

\begin{itemize}
\item \textsuperscript{171}Treas. Reg. § 1.170A-1(g) (2010).
\item \textsuperscript{172}Clotfelter, \textit{supra} note 3, at 12.
\item \textsuperscript{173}\textit{Id.}
\end{itemize}
value of $162 billion. These numbers represent an increase of almost half a million volunteers over the previous year, and charitable organizations forecast increasing numbers of volunteers in the coming years. In comparison to charitable donations, which declined between 2007 and 2008, the rate of volunteering actually increased slightly, from 26.2% to 26.4%. The most obvious explanation for this increase is that the rise in unemployment has led many people who were previously working in paying jobs to switch to volunteering. Ideally, such commitment and contributions will continue even after the economy recovers and volunteers transition back into the workforce.

Some scholars have suggested encouraging volunteering even further through tax incentives. For example, Alice M. Thomas proposes “a charitable volunteerism deduction (or tax credit) [that] would be available to people who volunteer at least thirty-five hours in a taxable year, engaged in


176 Id.

177 Id.

178 Id.
meeting the needs of marginalized individuals and/ or communities.”

She supports the deduction as part of a “profoundly American” tradition and argues that “[a] civil society requires its citizens to engage and connect with one another.” Additionally, she notes that people who volunteer tend to be “happier, have positive self-esteem, and are less depressed and less anxious.”

Finally, Thomas suggests that a deduction for volunteer time would counteract the currently biased system, in which organizations that provide charitable services receive preferential tax treatment, while individuals who do so do not.

The effect of such measures depends in part on how taxpayers view volunteering, *i.e.*, whether they see it as “simply a competing use of time, such as leisure, work, and household production, or whether it is a form of

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180 *Id.* at 303. For example, she notes that “[p]romoting a spirit of civic participation and service has been a longstanding policy of the federal government that came together in a formal program most recently in the early 1990’s”. *Id.* At 307.

181 *Id.*

182 *Id.* at 320-21.
investment in human capital.” If the former is true, then tax incentives for volunteering are likely to have little effect, since volunteers are making their decisions wholly independently from tax considerations. However, if the latter is true, then a tax deduction may cause taxpayers to see volunteering as a more “profitable” investment in human capital than other, similar investments of time.

Similarly, the effect of a tax deduction also depends on whether taxpayers view gifts of money and gifts of time as complements or as mere substitutes. If the former is true, then a tax deduction for volunteering would once again have little effect, since volunteers would neither increase their volunteering nor reduce their monetary contributions in response to the deduction. On the other hand, if donations of time are seen as a substitute for donations of money, then the former may increase in response to a tax deduction, at least among those taxpayers who would be eligible for the deduction. Thus far, little research has been done into these questions, so the true impact of a tax deduction for volunteering remains unclear.\(^\text{184}\)

One potential advantage to encouraging volunteering through a tax

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\begin{footnotes}
\item[183] Clotfelter, supra note 3, at 21.
\item[184] Id. (finding that, among women, “contributions and volunteering are complements, implying that the charitable deduction encourages volunteering as well as donations”).
\end{footnotes}
deduction is that it may increase monetary donations as well. The Office of Research and Policy and the Corporation for National and Community Service note that “[v]olunteers were much more likely than non-volunteers to donate to a charitable cause in 2008, with 78.2 percent contributing $25 or more compared to 38.5 percent of non-volunteers.”185 While such a result may seem surprising, especially if so many volunteers are donating their time because they are unemployed, the generosity of volunteers may stem from their desire to aid an organization once they become personally involved in its success.

Some critics may argue that allowing a deduction of time would create inequities between those who give time and those who, unable to give time, give money instead. In order to understand this argument, we must understand the relationship between monetary contributions and volunteer services. Some proponents of the charitable deduction argue that individuals who contribute the money they earn through time spent on for-profit activities should not pay higher taxes than similarly situated individuals who directly contribute their time to charitable organizations.186

185 Volunteering in America, supra note 175.

186 McNulty, supra note 75, at 241 (comparing a doctor who volunteers his time to an attorney who volunteers the money he earned by spending the same amount of time on paid work).
The deduction is justified under this view because it “equalizes both the relative incentive to contribute services, cash or property and the tax treatment of taxpayers who similarly surrender economic resources only in different forms.”\textsuperscript{187} In other words, the deduction is not so much an incentive as the removal of a disincentive to contribute cash or property that neutralizes the choice between giving money on the one hand or services on the other.\textsuperscript{188}

However, donations of money and time may not be as equivalent as they initially seem. Gergen notes that volunteer services are typically estimated to be worth only about one-fifth to two-fifths the value of cash contributions, which suggests that the two types of contributions are not comparable.\textsuperscript{189} Similarly, Clotfelter observes that the argument that volunteers and monetary contributors become equal under the current system of deduction holds true only if we consider itemizing taxpayers; for non-itemizers, volunteering is more cost-effective than contributing money

\textsuperscript{187} Id.

\textsuperscript{188} Id.

\textsuperscript{189} Gergen, supra note 20, at 1420. See also Rachel M. Zahorsky, Pro Bono: Help Goes Corporate: In-House, Outside Firms Link for Pro Bono Work, 96 A.B.A.J. 35 (2010) (“some nonprofits may not have the resources, or even the physical space, to use [volunteers] effectively”).
or goods.\textsuperscript{190}

There may also be hidden financial costs associated with volunteering as well. For example, Jerald Schiff notes that “attracting and utilizing volunteers is costly to a charity.”\textsuperscript{191} An organization must expend valuable resources to solicit, train, and supervise volunteers, resources that may be put to more effective use elsewhere.\textsuperscript{192} As a result, “[o]rganizations may, and often do, turn down volunteer labor, since it is unpaid, but not free.”\textsuperscript{193}

Moreover, individuals’ motivations for volunteering appear to differ from their motivations for donating money and goods; Schiff notes that “donors view contributions of money, rather than time, as the preferred

\textsuperscript{190} Clotfelter, \textit{supra} note 3, at 677.

\textsuperscript{191} Jerald Schiff, \textit{CHARITABLE GIVING AND GOVERNMENT POLICY} 59-60 (1990). For example, Jean Baldwin Grossman & Kathryn Furano note that “benefits are not automatically bestowed when volunteers show up. No matter how well-intentioned volunteers are, unless there is an infrastructure in place to support and direct their efforts, they will remain at best ineffective or, worse, become disenchanted and withdraw, potentially damaging recipients of services in the process.” \textit{Making the Most of Volunteers}, 62 \textit{LAW \& CONTEMP. PROBL.} 199, 217 (1999). They further note that mentoring programs, for example, cost about $300 per year per volunteer. \textit{Id.}

\textsuperscript{192} Schiff, \textit{supra} note 191, at 60.

\textsuperscript{193} \textit{Id.}
means for increasing charitable output, while volunteering may be seen as a means for obtaining influence or information.”

He also observes that an individual’s level of volunteering is affected by factors, like the presence of children, which may have different effects on the level of monetary contributions. Finally, he finds that female volunteers are more likely than male volunteers to perform clerical or manual tasks, while male volunteers are more likely to serve in leadership roles. Such a finding is problematic if, as Schiff argues, volunteering in leadership roles has a positive impact on an individual’s future wages, both because it develops skills and contacts and because it serves as a “signal to future employers.”

As an alternative to allowing taxpayers to deduct time spent volunteering with charitable organizations, Nancy Staudt proposes giving a “charitable service credit” to individuals who donate their services to

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194 Id. at 96.

195 Id.

196 Id. at 102. Schiff does not provide an explanation for this phenomenon, although he suggests it may be due to either women’s inability to capitalize on their previously acquired skills when volunteering or discrimination within the charitable sector. Id.

197 Id.
charitable organizations. Staudt acknowledges that such a program would pose administrative problems, in part because of the indeterminate value of labor. She also recognizes the philosophical dilemma presented by rewarding individuals for fulfilling their social responsibilities, as well as the potential for corruption and budget overruns that would accompany what essentially amounts to publicly funded employment. Nonetheless, she argues that a charitable service credit would be beneficial because it would “work as an incentive for individuals to participate in social and political institutions and at the same time give public recognition to their labor as socially valuable.” If implemented as a small, “almost symbolic,” payment for service, the credit would increase community involvement and provide the poor with a way to fulfill their social obligations without creating an undue burden on federal revenues.


199 Id.

200 Id.

201 Id.

202 Id. Another alternative to allowing a deduction for individual volunteer service would be to pay individuals a salary who donate their time to non-profit organizations through a government agency. The Clinton Administration created the Corporation for
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While a tax deduction for volunteer time may initially appear to be inconsistent with subsidy theory, such a proposal would provide an incentive for those who may not be able to give money to charitable organizations to nonetheless provide something of value and therefore avoid free-riding. Similarly, such a measure is consistent with choice theory, since the giving of time to charitable organizations allows donors who cannot vote with money an opportunity to express their preference for certain charities by providing time and labor. Ultimately, however, a deduction of time may prove to be unworkable, even as a temporary measure during a recession. Unlike the relatively straightforward process of lifting the cap on charitable deductions described above, allowing taxpayers to deduct time spent volunteering, even if such a deduction were only instituted temporarily during a recession, would involve major changes to the Code and to the way we conceive of the charitable deduction.

National and Community Service, a charitable government corporation, as a partnership between the government and non-profit sectors to work closely with state and local authorities. Knauer, supra note 168, at 969. The Corporation, whose purpose is to allow young people to serve their communities while also earning money for education, manages three volunteer programs: AmeriCorps, Learn and Serve, and the National Senior Service Corps. Id. at 970. Given the relatively young age of this corporation, its effectiveness is not yet known, although it does provide one example of an innovative way to encourage charitable contributions of time rather than money.
3. Increase Rate of Deduction

Another way to stimulate charitable giving by individuals during an economic crisis is to increase the value of the deduction by increasing the rate at which a contribution may be deducted.\textsuperscript{203} Currently, this rate is tied to the donor’s marginal tax rate, so the deduction would have to be decoupled from the income tax rate, perhaps through the use of uniform tax credits that are tied, for example, to the business cycle.\textsuperscript{204} Listokin observes that such manipulation of tax subsidies in response to an economic downturn is hardly novel, since Congress frequently makes such adjustments during recessions.\textsuperscript{205}

Paul McDaniel’s proposal of matching grants achieves similar results by tailoring each donor’s deduction to the relative value of the contribution to that individual. Under this system, “[e]ach donor’s gift would be matched by a predetermined amount from the government, the federal share to be transmitted directly to the charitable institution of the donor’s choice.”\textsuperscript{206}

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\textsuperscript{203} Listokin, \textit{supra} note 89, at 13.
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\begin{flushright}
\textsuperscript{204} \textit{Id.}
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\textsuperscript{205} Listokin, \textit{supra} note 89, at 13.
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\textsuperscript{206} McDaniel, \textit{supra} note 11, at 378.
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However, the amount of the match would be based on the percentage of the donor’s income represented by the grant because, in McDaniel’s words,

if there is to be a reward for charitable giving, the incidence and amount of the reward should bear some rational relationship to the act of charitable giving. The reward should be the same for persons who make a similar sacrifice, however measured. This appears to call for a system which increases the reward as the individual sacrifices a greater proportion of his income to charity. 207

Bittker, however, argues that “[a] system of matching grants would be a poor substitute for the deduction, but the proposal independently faces such serious constitutional and political obstacles that it can in any event be regarded as a dead end.” 208

Increasing the deduction is consistent with subsidy theory, since it provide greater incentives for giving to taxpayers who may be otherwise

207 Id. at 394.

208 Bittker, supra note 18, at 56.
tempted to free-ride on the donations of others. Similarly, an increase is also consistent with choice theory, since it provides potential donors with additional incentives to express their choice among different organizations through their donations. While the data is unclear, an increase in the rate of deduction is likely to have the largest impact on wealthier taxpayers, (and, under the current system, would have no impact on taxpayers who do not itemize). Certainly, during a recession, many middle-income taxpayers will be unable to make charitable contributions even with the added incentive that comes from an increased deduction, especially if they are part of the many taxpayers who lose their jobs during an economic downturn. As a result, while an increase in the rate of deduction appears to have its benefits, such an increase, without more, is unlikely to have a large impact on levels of charitable giving.

4. Extend Deduction to Non-Itemizers

Currently, only taxpayers who itemize their deductions may take advantage of the charitable deduction; since about seven out of ten taxpayers take the standard deduction, the vast majority of taxpayers have no monetary incentive to contribute to tax-exempt organizations. Non-itemizing taxpayers have been allowed to deduct their charitable
contributions in the past, most recently between the years 1982 and 1986.\textsuperscript{209} Since that time, various scholars have advocated extending the deduction to non-itemizers again.\textsuperscript{210}

Making the tax benefits associated with charitable giving available to all taxpayers during a recession has the added advantage of potentially providing additional tax relief to lower-income taxpayers for contributions they may have been inclined to make anyway. Various attempts have been made to introduce legislation that would once again allow such taxpayers to deduct at least some portion of their charitable contributions, although none of these attempts have been successful.\textsuperscript{211} In 1975, the Filer Commission proposed that taxpayers taking the standard deduction should also be allowed to deduct their charitable contributions, with low-income families being able to deduct as much as twice the amount of their contributions.\textsuperscript{212}

\textsuperscript{209} Lindsey, supra note 112, at 1068.


\textsuperscript{212} GIVING IN AMERICA, supra note 1, at 20-21.
Others have proposed allowing the deduction only for those contributions that exceed one percent of the taxpayer’s income, based on the rationale that “using a fixed percentage of income as the threshold for the deduction would ensure a uniform incentive to contribute, regardless of income.”

Despite its supporters, Congress nonetheless eliminated the provision allowing non-itemizers to deduct their charitable contributions in 1985, in part because they viewed it as a “double deduction” that created administrative burdens for both the Service and for taxpayers who could otherwise avoid filing a return. Congress further noted that “[w]hile the proposal to repeal the nonitemizer deduction may have some adverse effect on the amount of charitable giving, we believe that contributions by nonitemizers, who generally have relatively low marginal rates, are not affected significantly by tax considerations.”

Extending the deduction to include non-itemizers is consistent with

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215 Id.
subsidy theory, since it extends the incentive to give to taxpayers who may be otherwise tempted to free-ride on the donations of others. Similarly, an increase is also consistent with choice theory, since it expands the base of taxpayers who have an incentive to express their choice among different organizations through their donations. However, a more effective measure may be to not only expand the donor base but also provide additional incentives to give through a tax credit.

5. Switch from Deduction to Credit

Several scholars have proposed not just increasing the rate of deduction but changing the deduction to a credit. In essence, a full tax credit for the amount of a contribution is the equivalent of a 100% tax deduction. Converting the deduction to a uniform credit that would be divorced from marginal tax rates could address the previous criticism of the charitable deduction, namely that it is of greater value to those in higher tax brackets. Moreover, at least some studies have shown that donors are more responsive to a credit than they are to a deduction or matching

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Another alternative, proposed by the Filer Commission, would be to allow donors at certain income levels to deduct some multiple of the amount of their contribution.
Recently, Saul Levmore proposed “a partial credit, or a partial credit up to some ceiling… [combined with] a greater credit or deduction for filers whose charitable contributions exceed a specified percentage of their income.” However, he notes that such a system runs the risk of organizations competing too vigorously for a donor’s funds, “greatly reduc[ing] the likelihood of either extracting information about respondents’ true preferences or encouraging individual involvement in (or monitoring of) charitable works.” Viewing donors as “voters” and contributions as “votes,” he argues that “voters might take their votes more seriously when required to pay for them,” which does not happen when the donor receives a full credit for the amount of their donation.

One of the most appealing features of a tax credit for charitable contributions is that a credit could be made available to all taxpayers. A tax credit that can be utilized by all taxpayers is likely to increase contributions

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219 *Id.* at 410-11.

220 *Id.* at 411.
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to organizations favored by lower-income taxpayers, like religious organizations, while reducing contributions to organizations favored by the wealthy, like educational institutions, hospitals and arts organizations.\textsuperscript{221} This effect may be exacerbated by the fact that organizations like schools and hospitals are more sensitive to changes in the cost of giving than religious organizations.\textsuperscript{222} For example, in one study, Martin Feldstein estimated that replacing the charitable deduction with a thirty percent tax credit would increase total giving by fifteen percent but would reduce contributions to schools and hospitals by about twenty percent.\textsuperscript{223} In a subsequent study, Feldstein and Amy Taylor found that a twenty-five percent tax credit would leave total giving relatively unchanged, but would increase giving to religious organizations by almost ten percent while

\textsuperscript{221} Good & Wildavsky, supra note 65, at 2400. \textit{See also} Daniel Halperin, \textit{A Charitable Contribution of Appreciated Property and the Realization of Built-in Gains}, 56 \textsc{Tax L. Rev.} 1, 9 (2002) (noting that a credit would likely increase support to religious organizations and arguing that “it may not make sense to support a credit, which would be disruptive and controversial, unless one also asserts that this shift in priorities is desirable”).

\textsuperscript{222} Martin Feldstein, \textit{The Income Tax and Charitable Contributions: Part II- The Impact on Religious, Educational, and Other Organizations}, 28 \textsc{Nat'l Tax J.} 209, 224 (1975).

\textsuperscript{223} \textit{Id.}
Some scholars have expressed concerns about converting the current tax deduction for charitable contributions to a credit. For example, McNulty notes that, while a tax credit “appears to be the most neutral or fair allowance if the allowance’s purpose is… to subsidize or reward socially desirable behavior… a deduction would better serve to define income and cannot definitively be viewed as less efficient than a credit nor more inappropriate as an incentive or subsidy.”^225 Bruce Chapman goes further, arguing that a deduction is preferable to a credit because it not only encourages diversity, an advantage that the charitable sector has over politics—which can only avoid political instability by offering bland consensus-building policies—but also comes closest to charging high income, high demanders the price for public goods that is closest to that which is required of them to achieve a community wide consensus. A tax credit fails sufficiently to take into account

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^225 McNulty, supra note 75, at 247.
the higher share of the taxes that high demanders must pay to
the general tax revenue to make up for the tax subsidy given
to charitable contributions. The tax deduction offsets this
higher share by the same marginal tax rate that generates the
higher tax share in the first place and, therefore, is more tax
neutral and more politically stabilizing. 226

Although attempts to permanently institute a tax credit for charitable
contributions have met with resistance, a temporary credit that is only in
place during an economic downturn may be more politically palatable and
therefore easier to implement. In addition, a credit would go furthest
towards advancing the goals of the charitable deduction under subsidy and
choice theories, since it would give equal voice to all taxpayers, including
those taxpayers who may feel the most neglected during a recession,
namely those whose incomes are too low to take advantage of the current
itemized deduction for charitable contributions.

6. Conclusion

Because individuals serve as the greatest source of funding for charitable organizations, it is almost impossible to discuss aid to the charitable sector without looking at how contributions made by individual donors are taxed. The best way to stimulate giving among these individual donors is by converting the current deduction into a credit that is available to all taxpayers. However, focusing solely on the role that individuals play in the charitable sector neglects the important contributions that organizations can also play in this field, so the next section looks at how organizational actors can aid the charitable sector during an economic downturn.

B. Organizational Donors

Corporations present a lucrative source of contributions to charitable organizations, giving a total of $14.10 billion in 2009, including $4.42 billion from corporate foundations.\textsuperscript{227} As a result, we should consider ways

\textsuperscript{227} Annual Report, supra note 87, at 11. While this amount represents only 4% of total contributions, corporate contributions, unlike individual contributions, actually rose in 2009 by 5.5% (5.9% adjusted for inflation). \textit{Id.} at 8. Much of this increase can be attributed to increased non-cash contributions from pharmaceutical companies, as well as
to stimulate charitable giving by corporations, which can be done largely through the measures already discussed above. Corporations can also take advantage of their higher profile to publicize effective non-profit organizations, “attracting greater funding and thus creating a more effective allocation of overall philanthropic spending.” Moreover, corporations can work in conjunction with non-profit organizations to make them more effective, particularly when they can use their knowledge and skills, clout and connections, and presence within the community to help non-profit organizations address social problems. We should at least consider, then, how corporate philanthropy can be encouraged during an economic downturn.

1. Provide Corporations with a Charitable Tax Credit instead of a Deduction

Corporate donations appear to be at least somewhat responsive to the price of giving, which suggests that levels of corporate giving could be expanded in the financial and healthcare industries. Id. at 3. In fact, the majority of corporations actually reduced their charitable giving in 2009. Id.

\[228\] Id. at 64.

\[229\] Id. at 65-66.
easily manipulated by changes to the current charitable deduction.\textsuperscript{230} Michael Porter and Mark Kramer note that corporations are better positioned than individuals (or even foundations) to monitor how non-profit organizations utilize their contributions and tap into those organizations’ capabilities, particularly when there is a connection between the activity of the organization and the for-profit corporation.\textsuperscript{231}

Some scholars, such as Clotfelter, extol the virtues of corporate giving, noting that “[b]ecause of corporations’ visibility in political and economic activities, corporate gifts are viewed as a barometer of business sentiment and, to some extent, as a model for individual giving.”\textsuperscript{232} Similarly, Henderson and Malani argue that corporations may actually be better than nonprofit organizations and the government at delivering philanthropy because “their ordinary profitmaking activities sometimes give corporations an edge at helping the less fortunate.”\textsuperscript{233} They also argue that corporations, “[b]y aggregating a number of different shareholders’ and consumers’

\begin{itemize}
\item \textsuperscript{230} Clotfelter, \textit{supra} note 3, at 12.
\item \textsuperscript{231} Porter & Kramer, \textit{supra} note 242, at 63.
\item \textsuperscript{232} Clotfelter, \textit{supra} note 3, at 12. (noting President Ronald Reagan’s call for increased corporate giving as a way to make up for reductions in federal support of social programs).
\item \textsuperscript{233} Henderson and Malani, \textit{supra} note 210, at 611.
\end{itemize}
donations, [] have greater leverage over charity managers” and can “use their greater size to more efficiently produce network effects in warm glow.”234 According to them, increasing philanthropy by corporations is the natural result of demand by investors, employees, and customers for more charitable activity.235

Linda Sugin, on the other hand, argues that the charitable deduction for corporations is problematic because “[t]here was never any compelling reason to subsidize corporate contributions more than contributions made by shareholders out of dividends they have received;” instead, this phenomenon is the accidental result of the dual system of taxation.236 Seeing no connection between federal policy and the bias towards corporate philanthropy, she argues “there is no reason to have a federal policy in the Code that prefers giving at the corporate level.”237 She also notes that “[c]orporate charity overwhelmingly supports projects that are related to either employees, customers, or communities in which the business

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234 Id. at 599-600.

235 Id. at 612.

236 Id.

237 Id.
According to Sugin,

there is no reason to believe that corporations are better at prioritizing different charitable purposes, determining appropriate levels of support for diverse needs, or resisting the temptation to support conventional tastes than either the government or individuals. In addition, the concentration of charitable funding from corporations inevitably leads to the exertion of power by those corporations over the charitable institutions, while the individual deduction is more likely to produce small gifts that fail to buy influence. The anthropomorphic conception of the corporation is an inadequate model for the Code because it fails to appreciate the differences between human persons and corporate

238 Linda Sugin, Encouraging Corporate Charity, 26 VA. TAX REV. 125 (2006) (citing Ian Wilhelm, Company Giving Habits Influence Workers, Consumers, Two Studies Find, THE CHRONICLE OF PHILANTHROPY (2004)). Such cynicism regarding the motivations behind corporate philanthropy is hardly new, for example, Franklin Roosevelt also opposed attempts by corporations to “purchase” goodwill and argued that charitable giving should be left to individual shareholders. Clotfelter, supra note 3, at 12.
Ultimately, she argues that “[t]he corporate deduction for charitable gifts was never completely consistent with the theory or doctrine of section 170 and changes in both the tax law’s treatment of dividends and the accepted practices of businesses suggest that the special deduction for charitable giving be replaced by the ordinary business deduction, which broadly governs ordinary and necessary business expenses.”

Sugin is not the only critic of corporate philanthropy; Faith Stevelman Kahn also opposes the current treatment of corporate charitable contributions, noting that

the absence of substantive regulation under state corporation law, in combination with the absence of a disclosure requirement under the federal securities (or other) regulations—has created the potential for abuse with respect to both shareholders’ property interests and in regard to their


240 *Id.* at 835.
interests in avoiding compelled subsidization of entity-level political expression. 241

Porter and Kramer also profess concerns about corporate philanthropy, quoting Milton Friedman’s statement that “[t]he corporation is an instrument of the stockholders who own it. If the corporation makes a contribution, it prevents the individual stockholder from himself deciding how he should dispose of his funds.” 242 With respect to cause-related marketing programs, for example, they express “genuine doubts about whether [such programs] actually work or just breed public cynicism about company motives.” 243 Similarly, with respect to corporate matching programs, they argue that

[t]he majority of corporate contribution programs are diffuse and unfocused. Most consist of numerous small cash


243 Id. at 57.
donations given to aid local civic causes or provide general operating support to universities and national charities in the hope of generating goodwill among employees, customers, and the local community.\textsuperscript{244}

Unlike Sugin, Kahn, Porter, and Kramer, Knauer sees some advantages to encouraging corporate philanthropy, noting that “[i]t takes fewer resources to secure several large contributions from corporations than smaller gifts from many individuals” and that “the federal government may have more influence over the donative patterns of corporate taxpayers.”\textsuperscript{245}

Most recently, Benshalom has argued that corporations should be denied charitable relief because “[m]anagers are not political agents of their shareholders; they obtain no better knowledge of what social goods are underprovided and they tend to come from a relatively thin privileged social class.”\textsuperscript{246} He also argues that the deduction may be improperly used to purchase political influence.\textsuperscript{247} To avoid these issues, Benshalom proposes

\begin{flushright}
\textsuperscript{244} Id.
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\textsuperscript{245} Knauer, supra note 168, at 957.
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\textsuperscript{246} Benshalom, supra note 10, at 1091.
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\textsuperscript{247} Id.
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analyzing corporate contributions using the same tools as general business expenses. Henderson and Malani seem to agree, arguing that direct contributions from corporations to non-profit organizations should only be allowed if the corporation can “explain why it should not step out of the way and let shareholders make these donations directly.”

Many of the proposed changes to the charitable deduction as applied to individual donors, including implementation of a tax credit in lieu of the current deduction, could apply to corporate as well as individual donors. In fact, such measures could have an even greater impact at the corporate than at the individual level, since “[t]he tax law has long contained a bias in favor of charitable giving by corporations compared to distributions by corporations followed by charitable giving by individual shareholders.”

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248 Id. Conversely, Professor Bittker proposed repealing section 162(b), which prevents corporate taxpayers from deducting disallowed charitable contributions as ordinary and necessary business expenses. Bittker, supra note 18, at 62.

249 Henderson and Malani, supra note 210, at 576.

250 Many of these proposals were considered, and rejected, by the Filer Commission, which found “that none of the tax alternatives… was both clearly effective enough and sufficiently in tune with the spirit and philosophy of philanthropy, so as to merit the commission’s endorsement.” GIVING IN AMERICA, supra note 1, at 54.

251 Sugin, supra note 239, at 835.
Because corporate income is taxed both when it is earned by the corporation and when it is distributed to the shareholder, a charitable contribution made by the corporation avoids an additional layer of taxation, thereby encouraging the corporation to distribute those funds directly to the charity rather than distributing them to shareholders to be contributed later.\textsuperscript{252} However, we should also consider ways in which private businesses are uniquely positioned to provide assistance to charitable organizations during an economic downturn.

While the debate continues over whether corporate contributions should be treated the same as individual contributions under the Code, there does not seem to be any reason to exempt corporations from the proposed tax credit for contributions.

2. Promote Partnerships between Private Businesses and Charitable Organizations

Any attempts to increase the involvement of for-profit corporations in the non-profit sector should acknowledge that corporate philanthropy is increasingly “used as a form of public relations or advertising, promoting a company’s image or brand through cause-related marketing or other high-

\textsuperscript{252} \textit{Id.}
The motivations behind corporate giving may differ some from those for individuals, since corporations contribute to charities not only for marketing or public relations purposes, but also as part of broader tax strategies and to demonstrate their status among other corporate entities. As noted above, these programs have occasionally been criticized for serving the needs of the corporation rather than the needs of the non-profit organization. Although corporations tend to reduce their marketing budgets during economic downturns, a tax deduction aimed specifically at cause-related marketing could provide the incentive needed to encourage such programs at a time when they are likely to otherwise be cut.

Similarly, the Code could provide greater incentives to corporations that supply “altruistic” goods, like fair trade coffee or hybrid cars. These altruistic goods provide an added advantage of being “bundled” with private

253 Porter & Kramer, supra note 242, at 57.


255 See, e.g., Porter & Kramer, supra note 242, at 58 (arguing that cause-related marketing leads to public cynicism).

256 Henderson and Malani, supra note 210, at 590.
goods so that consumers who may not have paid separately for the public benefits that derive from the public good are willing to subsidize that benefit via purchase of the bundled private good.\textsuperscript{257} In other words, a consumer who may not directly contribute to help fair trade farmers or environmental groups may nonetheless be willing to pay more for a cup of coffee or a car that indirectly benefits those groups.\textsuperscript{258} Moreover, unlike the government, private corporations can adjust the extent to which they offer these altruistic goods in response to the needs of individual consumers.\textsuperscript{259}

Henderson and Malani argue that “the government should allow consumers to deduct the charitable component of the green goods they purchase.”\textsuperscript{260} While this deduction would be taken by individual consumers rather than corporations, the deduction would presumably benefit corporations as well, since consumers would be more likely to purchase these “green” goods, which would provide more profits to the corporation. Henderson and Malani point out that implementation of such a deduction

\begin{footnotesize}
\textsuperscript{257} Id. at 594.
\textsuperscript{258} Id.
\textsuperscript{259} Id. at 596.
\textsuperscript{260} Id. at 609.
\end{footnotesize}
would require coordination with the IRS;\textsuperscript{261} moreover, the same constraints on charitable deductions in general would also limit the scope of the benefits associated with a deduction solely for green goods.\textsuperscript{262}

3. Provide Tax Credit to Businesses that Second their Employees to Non-profit Organizations

While encouraging corporations to donate money and goods to non-profit organizations is certainly desirable, these organizations may actually benefit more if corporations are encouraged to donate services. Donations of services may have added benefits if employers are simultaneously deterred from reducing their payrolls.

One of the most severe consequences arising from the current recession has been a drastic increase in unemployment, a trend that occurs whenever the American economy undergoes a downturn. For example, more than 1,288,030 layoffs were recorded in 2009, which is the largest year for downsizing since 2002.\textsuperscript{263} The negative effects of unemployment on a

\textsuperscript{261} Id.

\textsuperscript{262} See supra Section III.B.1.

\textsuperscript{263} Challenger, Gray & Christmas, Inc., December Job Cuts drop 34%, 5 THE CHALLENGER INDEX 4 (January, 2011). Moreover, employees who lose their jobs often
worker extend far beyond the loss of income; the unemployed also lose health benefits, feel stigmatized by family members and peers, are unable to develop their on-the-job skills during the time they are unemployed, and can suffer from depression precisely at a time when their lack of healthcare leaves them least able to afford mental health services. Moreover, such workers often have difficulty finding a new job, even after the economy recovers.

On the other side of the equation, employers also suffer when they are forced to scale back their workforce. Not only might they have to pay severance to the workers who are let go, but employers may also suffer from lost morale among their remaining employees. Once the economy recovers and the employer begins to rebuild its workforce, it will face costs related to finding and hiring qualified employees. Moreover, the employer may suffer a reputational hit after a layoff, as prospective employees may not want to work for an employer with a reputation for downsizing. Taken together, these factors suggest that the best proposals from the perspectives of both employees and employers are the ones that will prevent or reduce downsizing in the first place.

One way the government could encourage volunteering is by providing

remain unemployed for six months or longer. *Id.*
additional tax benefits to employers that “second” underutilized employees to charitable organizations. An employee who is seconded would temporarily provide services to a non-profit organization while still retaining his or her position with his or her employer; compensation, either in the form of a regular salary or a stipend, would come from the employer rather than from the non-profit organization. Seconding could alleviate the issues currently faced by unemployed youth, who are unable to get the training and experience they would generally receive during this stage in their lives and therefore face the danger of becoming a “lost generation” without the skills to move up in the workforce even as the economy improves. Currently, employers who second their employees may deduct the salaries of those employees as an ordinary business expense; however, providing those employers with a tax credit rather than a deduction would encourage even more employers to consider seconding as an alternative to laying off underutilized employees.

Encouraging volunteering within the private sector is not necessarily a novel concept; law firms, for example, have encouraged attorneys to provide services on a pro bono basis for years. Corporations could take a

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264 See American Bar Ass’n Model rule 6.1: Voluntary Pro Bono Publico Service (“[a] lawyer should aspire to render at least (50) hours of pro bono publico legal services per year”). New organizations like the Taproot Foundation have attempted to tap into the
cue from some law firms that have allowed incoming associates to work for non-profit organizations in exchange for a stipend and other benefits provided by the firms. For example, in February of 2009, the law firm Simpson Thacher & Bartlett offered stipends and health benefits to associates who agreed to leave the firm to work for non-profits for one year.\textsuperscript{265}

A tax credit paid to employers who second their employees could lead to a glut of paid volunteers and could leave non-profits with the problem of how to effectively train and manage an increase in their workforce.\textsuperscript{266} Conversely, these organizations may be less inclined to hire paid workers if they feel they can receive those services for free; as a result, individuals who are genuinely dedicated to working for charitable organizations may desire for corporate volunteering by supporting large-scale corporate volunteering programs that emphasize contributions of technical expertise, and individual companies like Capital One and Deloitte encourage skills-based volunteering in their corporate strategies. However, such programs are still in their nascent stage, and many are not as effective as they could be. Giving USA 2010: Giving by Corporations, The Center on Philanthropy at Indiana University, at 8, available at http://www.givingusa2010.org (internal citations omitted).

\textsuperscript{265} Zahorsky, \textit{supra} note 189, at 27.

\textsuperscript{266} See Section VI.A.2, \textit{supra}. 
find themselves squeezed out by self-interested workers who return to the for-profit sector as the economy improves. Despite these concerns, an additional tax credit for companies who second their workers may be worth considering as an effective means of combating both the increased needs of the charitable sector during a recession and the increased unemployment that is likely to occur during those times.

4. Conclusion

While the concept of corporate philanthropy continues to be problematic, corporations constitute too large a source of aid to be ignored completely during an economic downturn, particularly if measures can be implemented that simultaneously benefit non-profit organizations and retain jobs. In particular, measures aimed specifically at corporations, like enhanced tax deductions for cause-related marketing could enhance donations to non-profit organizations while also improving corporations’ public images (and, ultimately, their bottom lines). Moreover, a tax credit for employers who second their employees could not only aid non-profit organizations that are in need of assistance but also help both employers and employees avoid the negative consequences associated with downsizing.
V. CRITICISMS

A. Additional Tax Expenditures Will Hurt Economic Growth

Some may argue that government should not be increasing tax expenditures aimed at the non-profit sector during a recession, when both the government and the private sector are in dire need of financial help as well. After all, “[t]ax preferences, which are legally known as tax expenditures—result in forgone revenue for the federal government…” In other words, tax expenditures like the charitable deduction are really nothing more than “a replacement cost for the federal spending that otherwise would have been made to attain the same social, economic, or policy goals.” Some, like Surrey and Tolan, argue that, given the inequities, confusion and administrative difficulties surrounding tax

267 See, e.g., Listokin, supra note 89, at 13 (“All else equal, a government spending program is preferable to a tax expenditure program from a stabilization perspective”).

268 Tolan, supra note 121, at 69 (quoting General Accounting Office, Tax Expenditures Represent a Substantial Federal Commitment and Need to be Reexamined, Doc 2005-19600).

269 Tolan, supra note 121, at 69.
expenditures, they should be used only as a last resort.\(^{270}\)

While we should certainly bear in mind Surrey and Tolan’s concerns about relying too much on tax expenditures to accomplish financial goals, the proposed reforms would probably have a relatively small impact on the federal fisc.\(^{271}\) The amount of federal revenue lost due to the charitable deduction constituted less than 1.7\% of the total estimated federal tax receipts in 2008, and there is little reason to believe the additional measures discussed above would have a significantly greater impact on the budget.\(^{272}\) Moreover, the current provisions related to charitable relief are considerably smaller than other tax expenditures, such as the mortgage deduction and the exemption for health benefits.\(^{273}\) While we should always tread lightly when dealing with tax expenditures, particularly during times of economic

\(^{270}\) Id. (citing Surrey, \textit{supra} note 12, at 734). Professor Tolan also observes that tax expenditures are “must pay” items that cannot be easily adjusted later and that such expenditures are generally not subjected to the same congressional scrutiny as direct expenditures. \textit{Id.} at 70.

\(^{271}\) \textit{See supra} Section IIIA

\(^{272}\) Benshalom, \textit{supra} note 10, at 1081 n. 125. (citing Office of Mgmt. & Budget, \textit{Analytical Perspectives: Budget of the United States Government Fiscal Year 2008}, 239, 296-99 (2007)).

\(^{273}\) \textit{Id.}
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crisis, the benefits to both the non-profit and for-profit sectors of the expenditures outlined above seem to outweigh their costs.

B. Charitable Organizations Would Benefit More from Direct Government Intervention

Others may argue that it would be more practical for the government to provide direct assistance to charities. In other words, the federal government could attempt to stabilize charitable budgets by providing direct relief during a recession in order to counteract the reduction in charitable contributions from other sources. Such measures would not be unheard of, given that most countries have significantly lower levels of charitable giving than the United States, in part because they have higher levels of direct governmental support of charitable activities.274

While direct governmental spending may seem appealing at first, such support would increase government involvement in the non-profit sector beyond its already high levels.275 As noted by the Filer Commission, “[t]he

274 Clotfelter, supra note 3, at 12 (“direct and indirect governmental support of the private philanthropic sector varies inversely with the involvement of government itself in providing social services”).

275 GIVING IN AMERICA, supra note 1, at 16. (“As a direct supporter of nonprofit
more an organization depends on government money for survival, the less ‘private’ it is, and the less immune to political processes and priorities.”

The Commission argued in 1975 that “no single institutional structure should exercise a monopoly on filling public needs, that reliance on government alone to fill such needs not only saps the spirit of individual initiative but risks making human values subservient to institutional ones, individual and community purposes subordinate to bureaucratic conveniences or authoritarian dictates.”

Furthermore, “government money obviously comes with strings attached, however invisible and unintentional they may be.” As a result, private support is often considered crucial in maintaining a nonprofit organization’s independence.

Another reason for preferring measures that can be implemented through the Code over direct government spending is that individuals often

organizations and activities, government today contributes almost as much as all sources of private philanthropy combined”).

276 Id. at 17.

277 Id. at 103.

278 Id. at 96.

279 Id. at 17.
have their own, personal motivations for giving, which can be stimulated through tax relief. For example, Tomer Blumkin and Efraim Sadka note that one motivation for making charitable contributions is to demonstrate wealth.\textsuperscript{280} Similarly, Gergen notes that donors may be motivated by the pleasure they get from voluntary giving, a pleasure that would be lost in a system that substituted mandated government spending for a deductible contribution.\textsuperscript{281}

Finally, any attempts to aid non-profit organizations at the federal level may simply lead donors to scale back their contributions. This phenomenon, referred to as “crowding out,” is best described by Richard Steinberg: “The relationship between government spending and private donations is not simple, but theory suggests that there will usually be partial


\textsuperscript{281} Gergen, \textit{supra} note 20, at 1407. However, direct government spending does have its proponents. For example Susan Rose-Ackerman suggests that government grants may in fact encourage greater private giving. Rose Ackerman, from Economics of Non-Profits 325. Matching grants may stimulate giving by lowering the cost of giving, while fixed sum grants may stimulate giving by, for example, increasing public confidence in the beneficiaries of government grants or allowing for economies of scale. Rose Ackerman, from Economics of Non-Profits 325.
simple crowdout; that is, that government expenditure increases (decreases) are partly neutralized by donative decreases (increases)”. 282 For all these reasons, enhancing the current system of encouraging charitable contributions by private actors is vastly preferable to a system of direct government intervention.

C. Donors Will Alleviate the Burden on Charitable Organizations on their Own

Others may argue that emergency measures are not necessary because donors, aware of the economic crises brought on by a recession, will respond by increasing donations to those non-profit organizations that are likely to experience an increase in need. Some scholars speculate that giving is influenced, at least in part, on one’s “relative income,” so that donors may give more when they feel that their income is greater than the incomes of others. 283 Alternatively, donors may give more when they feel


283 Clotfelter, supra note 3, at 12.
that others are also increasing their giving, either because they are inspired by the example of others or feel a certain peer pressure to match the apparent altruism of others.\textsuperscript{284}

Some evidence of this can be seen in the fact that health organizations and organizations providing human services saw an increase in donations in 2009, shortly after the current economic crisis began.\textsuperscript{285} The closest analogy may be to large-scale disasters, like the terrorist attacks of September 11, 2001, the Asian tsunami in 2004, Hurricanes Katrina and Rita in 2006, and the Haitian earthquake in 2009. Donations to organizations that provide emergency services to victims of these disasters tend to see a rise in donations immediately after their occurrence, and this effect has been attributed at least in part to media coverage of these disasters and the immense suffering they cause.\textsuperscript{286}

Certainly, the current recession has received its share of media coverage; however, the widespread effect of the recession and the relative lack of powerful images showing dramatic pain and suffering will undoubtedly dampen the urgency that people might otherwise feel to help

\textsuperscript{284} Id.

\textsuperscript{285} Annual Report, \textit{supra} note 87, at 19.

\textsuperscript{286} Id.
those who have become victims of the economic crisis (and people may feel that, unlike in the case of an event that affects only a limited geographic area, we have all become victims of this “disaster”). Moreover, with the possible exception of the terrorist attacks of September 11, 2011 (which were followed by an economic recession), most of the previous disasters were relatively contained in that they only had a negative impact on a discrete sector of the population. A financial crisis, on the other hand, has a much more wide-ranging impact on all sectors of the economy. As a result, we cannot rely on the public to meet the needs of non-profit organizations in the wake of an economic crisis and must take additional measures in order to make sure that already struggling non-profits do not risk further financial hardship.

D. These Measures Will Have Little Effect

Another potential criticism of these above measures is that they will have little actual effect on the charitable sector. Although there is some disagreement as to how elastic charitable contributions are, most studies estimate elasticity to be around -1.0, i.e., that charitable contributions decline by a dollar for each dollar reduction in income.287 This finding of

287 Laura Tiehan, Tax Policy and Charitable Contributions of Money, 54 Nat’l Tax J.
elasticity is important, since “[i]f the policy behind the charitable contribution deduction is to spur donations, then tax subsidies are wasted on donations that would have been made anyway.”

Moreover, donors tend to “smooth their annual giving relative to transitory changes in income,” making bigger adjustments to their donations in response to temporary changes in the cost of giving, but adjusting their giving in response to changes in income only when such changes appear to be relatively permanent.

All this suggests that changes that appear to affect the cost of giving (e.g., changes in the rate associated with the charitable deduction or the


288 Brody, supra note 66, at 715.

conversion of the deduction to a credit) may have a larger effect on charitable contributions than temporary changes in donors’ income (e.g., a temporary tax rebate). Furthermore, despite arguments to the contrary, studies have found that households at all income levels respond to tax incentives to contribute, although the effect may differ between low and high income households.  

Although some research suggests that most taxpayers are unaware of marginal tax rates or incentives related to charitable contributions and therefore would not adjust their giving in response to those rates or incentives, Clotfelter and Steurle argue that “it seems just as likely that many taxpayers, particularly itemizers, use approximations and rules of thumb that render their behavior very similar, on average, to a perfectly informed optimizer.” This finding suggests that, while changes to the charitable deduction may have only marginal

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290 Clotfelter, supra note 3, at 686. Elasticity does vary across organizations, as “gifts to religious organizations and to health and welfare organizations have lower price and income elasticities than gifts to the other types of charities.” Martin Feldstein & Amy Taylor, The Income Tax and Charitable Contributions, 44 ECONOMETRICA 1201, 1217 (1976).

effects on donor behavior, such effects reflect rational decisions by those donors about the costs and benefits, including the tax benefits, of giving. 292

CONCLUSION

As the debate continues about the effectiveness of the charitable deduction in facilitating the relationship between the private, public, and non-profit sectors, we should take a closer look at how these relationships change during an economic downturn. In particular, we need to consider how an economic crisis can negatively impact the charitable sector and what we can do to alleviate those effects. The most effective way to stimulate charitable giving by individuals is to convert the current deduction into a tax credit for contributions that is available to all taxpayers. In addition, providing a credit to corporations who pay their employees to work for charitable organizations may not only benefit those organizations but also reduce unemployment rates, thereby alleviating one of the most

292 Another important factor to keep in mind is that taxpayers may be slow to respond to changes in the charitable deduction, not only because of delays in communicating those changes to the public but also because donors may need time to absorb the full impact those changes will actually have on their finances. Clotfelter, supra note 3, at 12 (finding that “taxpayers do not adjust to changes in tax policy immediately, resulting in smaller effects in the short run than in the long run”).
devastating impacts of an economic downturn. While both of these proposals, as well as the others discussed in this Article, have their drawbacks, the worst thing we could do at the moment is nothing.

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