

Hurricane Katrina Tax-Relief Legislation and Senate Finance Subcommittee Hearing on “Charities on the Frontline: How the Nonprofit Sector Meets the Needs of America’s Communities”

September 27, 2005

There has been some significant activity in Congress over the past couple of weeks on tax issues affecting the charitable sector. On September 21, 2005, Congress enacted temporary tax relief legislation related to Hurricane Katrina. There are several temporary provisions in this legislation that support charitable giving. Also, on September 13, 2005, the Senate Finance Committee’s Subcommittee on Social Security and Family Policy held a hearing in which the CARE Act and charitable reform proposals were discussed.

Hurricane Katrina Tax-Relief Legislation

The tax relief bill passed by both the Senate and the House on September 21 follows informal negotiations between tax writers from both chambers to resolve differences between bills enacted two weeks ago. The most significant provision in the legislation, signed by the President September 23, allows individuals to deduct cash donations equivalent to up to 100 percent of their adjusted gross income, up from the current 50 percent. These contributions are not included in the overall itemized deduction limitations for individual taxpayers. Interestingly, these incentives do not apply to gifts made to donor-advised fund organizations, supporting organizations, and private non-operating foundations. This provision applies to gifts made between August 28, 2005, and December 31, 2005. Other important provisions, with their expiration dates included in parentheses, are:

- allowing cash corporations charitable deductions for relief efforts equivalent to up to 100 percent of their taxable income, rather than 10 percent (12/31/05)
- extending the enhanced deductibility for food donations currently available to chapter C corporations to small businesses and for educational book donations provided to school districts throughout the country (12/31/05)
- increasing the value of the mileage deduction available to volunteers for expenses incurred related to the Katrina relief effort and excluding from volunteers’ income reimbursements for use of personal automobiles in the relief effort (12/31/06)

Senate Finance Committee Chairman Charles Grassley (R-Iowa) was quoted in the media describing the purpose of the charitable provisions in the tax bill as "to encourage charitable giving outside of Katrina relief to prevent the rest of the nation's charities from seeing a downturn in giving as they did after September 11."

The final bill is more modest, particularly for charities, than the original Senate bill which included several provisions taken from the CARE Act (though generally applied on a temporary basis). For example, the initial Senate legislation contained a provision permitting the tax-free rollover of funds from Individual Retirement Accounts (IRAs) for taxpayers over the age of 70½ and a similar opportunity for taxpayers over the age of 59½ to roll over funds into charitable remainder trusts. Both the House and Senate are considering further long-term hurricane relief tax provisions that are likely to be introduced in the coming weeks. These and other provisions from the CARE Act could be included in this second round of legislation.

The current focus on enacting tax provisions aimed at hurricane relief may result in further delays in other legislation relating to charitable organizations, particularly the reform proposals currently under consideration by the Senate Finance Committee.

The Subcommittee Hearing

The hearing was held before Subcommittee Chairman Rick Santorum (R-PA) and Ranking Member Kent Conrad (D-ND), who were the only Senators present. In his opening statement, Senator Santorum discussed his long-standing support for the CARE Act. Regarding the Finance Committee's current focus on reform in the charitable sector, Senator Santorum said that he believed increased scrutiny and enforcement has likely cleaned up some of the problems identified, and he further expressed hope that any reform legislation would not impose undue burdens on the charitable sector.

Senator Conrad focused his opening remarks generally on praising the relief effort currently underway, but did highlight both the itemized charitable deduction and the estate tax deduction as two provisions currently in the tax code that encouraged charitable giving.

There were five witnesses, three representing charitable relief organizations and two economists to provide their policy views and to discuss scholarship in this area:

Luke Hingson, president, Brother's Brother Foundation, Pittsburgh, PA

Maj. George Hood, director, Nat'l Community Relations and Development, The Salvation Army, Alexandria, VA

Dr. Bob Reccord, president and CEO, North American Mission Board, Southern Baptist Convention, Alpharetta, GA

Dr. William G. Gale, senior fellow, the Brookings Institute, Washington, D.C.

Dr. C. Eugene Steuerle, senior fellow, Urban Institute, Washington, D.C.

The first three witnesses all provided summaries of the current relief work underway in the Gulf region, before commenting on current legislative proposals. All three organizations are active in the relief effort and they discussed the remarkable outpouring of support in the form of both cash and in-kind donations. Regarding the CARE Act, the three witnesses expressed general support for the legislation and discussed the importance of specific provisions.

The extension of the charitable deduction to non-itemizers and the provision permitting taxpayers to roll over funds from IRAs to charitable organizations on a tax-free basis were cited as important priorities.

Regarding charitable reform proposals currently under development in the Finance Committee, the three witnesses expressed a shared voice of concern that additional administrative burdens that could be imposed by new legislation. Maj. Hood in particular argued against reducing the availability of charitable deductions for in-kind donations. He noted that the tax law changes regarding donated cars had already resulted in a negative impact on The Salvation Army, and that further limitations could seriously harm organizations that depend on thrift store sales for revenue.

The final two witnesses are the co-directors of the Tax Policy Center, a joint venture of the Urban Institute and Brookings Institute and both are frequent witnesses in Congressional tax hearings. According to their remarks, Dr. Gale had been asked to discuss the role the estate tax plays in charitable giving and Dr. Steuerle's role was to discuss ways to "maximize the bang per buck" in a legislative package.

Dr. Gale described recent scholarship on the interaction between charitable giving and the estate tax. First, the deduction to the estate tax reportedly results in greater giving via decedents' estates. Also, the deduction apparently encourages greater giving during an individual's life because such charitable giving produces an immediate charitable deduction and also reduces the potential estate tax cost at the time of death (because the asset is no longer a part of the estate). According to Dr. Gale, estate tax repeal could result in a five percent reduction in total annual charitable giving. Finally, Dr. Gale cited recent scholarship that suggests different proposed reductions in the estate tax could have markedly different results in overall giving. Reducing the top marginal rate of the estate tax would apparently result in a greater drop in charitable giving than would increasing the amount of the estate tax exemption because the largest estates produce a disproportionate amount of charitable giving and they are most sensitive to marginal tax rate changes.

Dr. Steuerle described his recommendations for getting "the most bang for the buck" out of changes to the tax code provisions governing charitable organizations and the deductibility of donations. He argued that ending less effective tax incentives would provide revenues that could fund more effective charitable giving incentives. On the incentive side, he included expanding the charitable deduction to nonitemizers, removing current limitations and phase-outs, and allowing taxpayers to make charitable donations through April 15 of the year following the tax year in which the donation would be made as three effective ideas. On the reform/limitation side, he called for more IRS enforcement resources, e-filing of all Form 990s, using foundation pay-out rules to encourage more spending during economic downturns, limiting deductions for in-kind donations, and preventing deductions for cash contributions with no supporting records or receipts.

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