

# WebMemo



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## Obama's Proposal to Reduce Charitable Deductions Would Hurt Civil Society, Expand Government

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In February, the Obama Administration announced its proposals to raise tax rates on high-income earners and to reduce their tax deduction rate on gifts made to charities. These strategies are intended to raise funds for Obama's health care plan.

The Senate Budget Committee passed an amendment by Senator Robert Bennett (R-UT) to the budget resolution that would prevent this policy from going into effect. Congress should give this amendment full consideration. In so doing, it can resist government crowd out of the valuable charitable work performed by individuals and nonprofits.

**The Proposal.** American citizens in the highest marginal personal income tax bracket are taxed at a rate of 35 percent.<sup>1</sup> If they donate to a charitable organization, they can receive a tax deduction at the same 35 percent rate. For example, if a couple in this marginal bracket gives \$10,000 to a hospital, they can write off \$3,500 when filing their taxes.

Under Obama's proposal, beginning in 2011, families making over \$250,000 a year would see their marginal personal income tax rate rise from 35 percent to 39.6 percent.<sup>2</sup> Rather than keeping the charitable deduction rate consistent with the tax rate, Obama proposes reducing it to 28 percent. At this reduced rate, the possible tax write off from a \$10,000 donation would drop from \$3,500 to \$2,800, a difference of \$700.<sup>3</sup>

The Obama Administration estimates that its proposed tax changes will fill government health care coffers with around \$630 billion over 10 years.

**The Likely Consequences.** The President claims that his tax plan will only have a small negative affect on charitable giving. Percentage-wise, this may be true, but the estimated reduction in giving means billions of dollars less each year for charities, especially if weak economic conditions continue.

Scholars at the Center on Philanthropy at Indiana University estimated that, had Obama's proposed changes been in place in 2006, total itemized contributions from wealthy households would have dropped almost \$4 billion.<sup>4</sup>

While this amount is only a small percentage of total charitable donations given each year, it represents more than the annual operating budgets of the American Cancer Society, World Vision, St. Jude's Children's Hospital, Habitat for Humanity, and the American Heart Association combined.<sup>5</sup> Moreover, other scholars estimate that under Obama's proposal charitable organizations would see donations drop possibly by as much as \$9 billion every year.<sup>6</sup>

In addition to receiving less money from wealthy donors, charitable organizations under Obama's plan could face a more subtle yet significant challenge: government crowding them out of social wel-

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fare provision. This phenomenon occurs when government claims increasing responsibility for tasks once performed by civil society, absorbing a larger percentage of the resources dedicated to carrying out those tasks.<sup>7</sup>

**Shifting Focus.** Obama defends his proposal as a way of “equalizing” tax breaks for donors in different tax brackets. In his March 24 prime-time news conference, Obama said it would not be fair to allow wealthy donors to write off more than lower- or middle-income donors who give the same amount. “Ultimately,” he added, “if we’re going to tackle the serious problems that we’ve got, then in some cases those who are more fortunate are going to have to pay a little bit more.”<sup>8</sup>

But Obama ignores the fact that wealthy citizens get a higher deduction precisely because they *already* pay more—a lot more—in taxes. In fact, although families making over \$250,000 a year represent less than 5 percent of income earners in America, they pay 48 percent of all federal income taxes.<sup>9</sup> That a portion of their giving may go to private charities instead of to the government does not change the fact that, under the present tax system, the wealthy already shoulder a larger burden for social welfare. But Obama seems to believe that

federal government bureaucracy can deploy the resources of the wealthy more effectively than non-profit civil society organizations can.

President Obama has stated his desire to help “folks who have fallen on very hard times.”<sup>10</sup> Yet he is standing by his proposal to lower deductions for charitable giving, which would hamper efforts by nonprofits to help needy families. The President seems to be letting his desire to equalize differences undercut his desire to help the poor.

**Mediating Institutions.** Perhaps most importantly, Obama’s proposal says something about who Obama thinks can best determine how to distribute people’s money.

In their influential book *To Empower People*, Peter Berger and the late Richard John Neuhaus describe the importance to a healthy democratic society of “mediating institutions”—i.e., forms of association like the family, church, and nonprofit organization that stand between citizens and the large institutions of public life.<sup>11</sup>

Mediating institutions are essential for generating and maintaining the operative values of society. They are also well-equipped to provide a helping hand to people in the context of face-to-face rela-

1. The marginal tax rate is the statutory rate at which a taxpayer’s last dollar of income is taxed.
2. Those in the second highest income bracket would also see their personal income tax rate increase, from 33 percent to 36 percent.
3. If the charitable deduction instead stayed consistent with the increased tax rate at 39.6 percent, the difference in tax savings would be even greater. According to that scenario, the couple making a \$10,000 gift would go from a \$3,960 deduction to a \$2,800 deduction, a difference of \$1,160.
4. “Obama’s Tax Plan Could Cause Giving by the Wealthy to Drop by Several Billion Dollars Annually,” *Chronicle of Philanthropy*, February 27, 2009, at <http://philanthropy.com/news/updates/index.php?id=7285> (April 2, 2009).
5. Based on 2007 and 2008 figures available on the organizations’ Web sites.
6. “The Charity Revolt: Liberals Oppose a Tax Hike on Rich Donors,” *The Wall Street Journal*, March 10, 2009, at <http://online.wsj.com/article/SB123664427493678121.html> (April 2, 2009); Ryan J. Donmoyer, “Rich Donors May Be Undeterred by Tax Caps on Charitable Gifts,” *Bloomberg.com*, March 4, 2009, at <http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aRLx2HwnWyWs> (April 2, 2009).
7. See Arthur C. Brooks, *Who Really Cares: The Surprising Truth about Compassionate Conservatism* (New York: Basic Books, 2006), p. 58.
8. Transcript available at [http://www.nytimes.com/2009/03/24/us/politics/24text-obama.html?\\_r=1&pagewanted=all](http://www.nytimes.com/2009/03/24/us/politics/24text-obama.html?_r=1&pagewanted=all).
9. See “Who’s paying how much to IRS—December 10, 2008,” *The Heritage Foundation A La Chart* No. 39, at [http://www.heritage.org/Press/ALaChart/alachart-detail.cfm?customel\\_datapageid\\_244663=288290](http://www.heritage.org/Press/ALaChart/alachart-detail.cfm?customel_datapageid_244663=288290).
10. Transcript available at [http://www.nytimes.com/2009/03/24/us/politics/24text-obama.html?\\_r=1&pagewanted=all](http://www.nytimes.com/2009/03/24/us/politics/24text-obama.html?_r=1&pagewanted=all).
11. Peter L. Berger and Richard John Neuhaus, *To Empower People: From State to Civil Society*, ed. Michael Novak, 20th anniversary edition (Washington, D.C.: The AEI Press, 1996), p. 158.

tionships. They have intimate knowledge of those in need—they understand social problems in up-close and personal ways. Driven by deep convictions and compassion, such organizations can provide loving forms of assistance and care that government programs cannot offer. And they often do so for less money. Smaller and more flexible than most government bureaucracies, local congregations and charities can also spawn creative social innovations that benefit those in need.

Berger and Neuhaus claim that public policy should “cease and desist from damaging mediating structures.”<sup>12</sup> More than that, though, public policy should protect mediating institutions and, where possible without co-opting them, empower them in their efforts to promote the common good.

The tax plan put forward in Obama’s 2010 budget blueprint, however, implies that the state should assume responsibility for people’s needs even at the expense of vital mediating institutions. And it communicates the notion that America is better off with expansive and intrusive—rather than limited—government.

In short, Obama’s proposed tax plan penalizes those who can give the most, shifts dollars from citizens and local private charities to distant govern-

ment bureaucracy, and prioritizes mandatory taxation to voluntary tithing and giving.

Unfortunately, Obama’s proposed tax changes move the dial of social responsibility one more notch in the direction of the state. This sets a course for adopting many future policies that could chip away at local, personal, mutual obligation and increase dependence on government. For an example of this, one need look no further than Obama’s vision of expanding government control over health care, which is the very objective behind proposals to raise taxes and reduce charitable deductions for wealthy citizens.

**The Bully Pulpit.** Obama should use his presidential authority and influence to encourage voluntary giving and protect nonprofit groups, especially during tough economic times. President Obama speaks articulately and often of the important role charitable institutions play in America. He should send an equally clear message in his policy. Reconsidering the tax changes proposed for charitable donations would be good place to begin.

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12. *Ibid.*, p. 163.