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Charities Can Expect New Regulations and Increased Giving in an Obama Administration

By Peter Panepento

Charity leaders can expect President-elect Barack Obama and Congress to push for changes in the federal tax structure that could spur giving and add new regulations for charities and donors, tax experts say.

With Mr. Obama and Congress facing a recession and grappling with establishing a new strategy for the war in Iraq, those changes aren't likely to come quickly. Nonetheless, they could be significant.

One of the key pieces of Mr. Obama's tax platform during the campaign — a pledge to roll back some of the tax cuts extended by the Bush administration to those earning more than \$250,000 annually — would probably increase charitable giving among wealthy donors by 4 percent to 8 percent according to Robertson Williams, principal research associate at the Urban Institute and the Brookings Institution's Tax Policy Center in Washington.

Here's why: A gift of \$100,000 effectively costs \$70,000 at a 30-percent tax rate, and \$60,000 at a 40-percent tax rate.

"It would make it cheaper for them to give money to charities and, therefore, if all things are the same, they will give more money away," Mr. Williams says. "You're essentially lowering the cost to 'taxpayers of giving money away.'"

That increase in taxes, however, isn't likely to happen immediately, Mr. Williams says.

Mr. Obama will probably hold off on proposing a tax increase on individuals during a recession. Instead, he is likely to wait until the economy improves before pushing ahead.

Examining Endowments

More immediately, though, Mr. Williams says he expects the new administration to find other ways to produce new revenue and reduce the federal deficit.

One likely move would be changing a tax law that allows universities, foundations, and other institutions to use overseas tax shelters to guard hedge fund investments from taxes.

The law requires nonprofit investors that invest directly in hedge funds to pay unrelated business income taxes on their gains. But many groups avoid the tax by investing those gains in overseas accounts.

Some Senate leaders, including Sen. Max Baucus, the Montana Democrat who chairs the Senate Finance Committee, and Sen. Charles Grassley, an Iowa Republican, have been pushing for rules that would prevent groups from taking that approach.

The new administration is likely to follow through on that effort, experts say.

Reviewing Charity Tax Breaks

The new Congress is also likely to move ahead with plans by senior members of the Senate Finance Committee to discuss more wide-ranging questions related to the how the tax code treats charities.

Senator Baucus and Senator Grassley have been discussing plans to hold hearings on the basic tax code for charities in early 2009, aides have said.

The new makeup of Congress is not likely to change those plans, observers say.

“I don’t know that things have changed that much in terms of outlook,” says Dean Zerbe, a former tax aide to Mr. Grassley who now works as a lawyer in Washington. “The working relationship that Senator Baucus and Senator Grassley have will continue.”

That hearing could include questions about whether new regulations are needed for nonprofit hospitals and universities with large endowments.

Incentives for Donors

Lawmakers have also floated the idea of allowing people who do not itemize their tax returns to write off their donations to charity and whether donors should receive the same tax benefits for all donations. Some lawmakers say they believe gifts to institutions that primarily aid the poor deserve a different tax treatment than those made to institutions such as museums and universities.

Given Mr. Obama’s emphasis on change and the state of the economy, Mr. Zerbe says he believes conditions are right for such discussions.

“There’s a lot more that can be accomplished in the charitable sector. The large charities have the assets of Tarzan but they punch like Jane in terms of what they are accomplishing,” he says. “The economy kind of heightens some of these issues. Hopefully, that will be a positive thing.”