Q. What is the tax treatment of charitable contributions?

A. Corporations and individual taxpayers who itemize can deduct charitable contributions to 501(c)(3) organizations.

Many nonprofit institutions are exempt from paying federal income tax, but taxpayers may deduct donations to organizations set up under Internal Revenue Code section 501(c)(3) on their income tax returns. Donations to other nonprofits are made after taxes.

Since 1917, individual taxpayers have been able to deduct charitable contributions from income that might otherwise be taxed. Individuals may deduct cash and certain other contributions up to 60 percent of adjusted gross income (AGI) in a given year and may carry forward any excess for deduction on future tax returns for up to five years. Before the 2017 Tax Cuts and Jobs Act, the limit was 50 percent of AGI. An important caveat: only taxpayers who itemize may take the charitable deduction. Most taxpayers instead claim a standard deduction, which generally is larger than their potential itemized deductions but which does not provide a tax incentive to make charitable contributions. The Tax Cuts and Jobs Act nearly doubled the standard deduction amounts, which will greatly reduce the number of taxpayers who itemize and hence the number who have a tax incentive to make charitable contributions.

In 1935, Congress extended the right to deduct charitable contributions to corporations. Corporations may not deduct more than 10 percent of their pretax income in a given year but, like individuals, may carry forward excess donations for five years. Some corporate contributions, however, might also qualify as business expenses.

Contributions by individuals or corporations can take the form of cash, financial assets, or other noncash property such as real estate, clothing, or artwork. Certain contributions face greater restrictions than cash contributions, whereas others receive more generous treatment than cash. The limit for donations of appreciated real property is generally 30 percent of AGI, and the limit for contributions to private nonoperating foundations is the same. But donors may deduct the full current market value of appreciated property. This effectively allows them to deduct capital gains twice: donors pay no tax on the capital gains of the appreciated property, and then reduce their other income subject to tax by the full amount of their contribution, thereby effectively deducting from income the capital gains that had never been included in income. However, those capital gains would also be excluded from income tax if held until death, even if not given away so unless that provision is simultaneously addressed, removal of the special tax break for gifts of appreciated property would discourage such gifts.

Key Elements of the U.S. Tax System

What is the tax treatment of charitable contributions?

Further Reading

Boris, Elizabeth T., and C. Eugene Steuerle, eds. 2016. *Nonprofits and Government: Collaboration and Conflict*, 3rd ed. Lanham, MD: Rowman & Littlefield.

Office of Management and Budget. 2015. *Analytical Perspectives, Budget of the United States Government, Fiscal Year 2016*. Washington, DC: US Government Publishing Office.