CHAPTER 4

Philanthropic Contributions

THE present status under the 1954 Revenue code of the allowance for deduction of philanthropic contributions in computing taxable income, the reader will recall, is deduction of such gifts up to 30 per cent of annual income, provided that 10 per cent of income is given to certain institutions. The brief legislative history of personal deductions given in Chapter 1 will now be supplemented by a sketch of the background of current legislation on contributions.

Legislative Background

Until recently, public debate of any consequence concerning the tax treatment of philanthropic gifts had occurred only twice. The first time, in 1917 when the United States entered World War I, there was widespread anxiety that established habits of giving and periodic appeals might no longer be sufficient to maintain the flow of private philanthropy. The general consensus, among those of the press and in Congress who were seriously concerned, tended toward the notion that persons in the habit of contributing to philanthropic causes would now seek to offset increases in tax liabilities with cuts in their philanthropic giving. From then on, until the limit was raised in 1952, gifts to philanthropic organizations were deductible up to 15 per cent of the taxpayer's income.

The question arose once more after the United States entered World War II. The 1944 proposal to extend the standard deduction to tens of millions of taxpayers was, for many, a threat to the continued existence of private non-profit activity. Obviously, the standard deduction made gifts to philanthropy no cheaper than any nondeductible expenditure. There was, therefore, a justifiable fear that the generous flow of funds to private, nonprofit institutions might shrink to a mere trickle. As in 1917, some of the more vociferous advocates of undiminished nongovernmental financing and control of such activities saw in it the first steps toward their nationalization.[1] But the predominant Congressional opinion in 1944, unlike that in 1917, appeared to be that most contributions are made independently of tax considerations. Representative Robert L. Doughton, then chairman of the House Ways

[1] Representative Carl T. Curtis of Nebraska expressed the fear that the standard deduction would cripple the institutions supported by private donations, and thus start us on "the road toward totalitarianism" (*Congressional Record*, 78th Cong., 2nd Sess., 1944, pp. 3972, 4029). Similar fears had been expressed in 1917: a *Wash-*

and Means Committee, argued that the mass of contributors do not give "for the purpose of securing a tax reduction, but because of the worthy causes such contributions advance."[2] And Senator Walter F. George, chairman of the Senate Finance Committee, stated that "the committee does not believe it can be proved that a tax incentive has been an important factor in the making of such gifts by individuals having less than $5,000 of adjusted gross income, and certainly the $500 standard deduction will not remove the tax incentive for persons in the higher brackets, upon whom the charities depend for contributions in substantial amounts."[3] It might be argued that this statement suggests no real departure from the thinking of 1917, since the committee believed only those with modest incomes to be insensitive to the influence of the tax upon giving. But the tax rate on the lowest bracket of taxable income in 1944 exceeded all but the marginal rates on the very highest brackets in 1917.

The change in Congressional thinking may be accounted for in part by the intense pressure on Congress in the early 1940's to simplify the tax return form. The "simplification" of the deductions seemed a key point in this task. But the change in thinking was also the result of the common belief that giving to philanthropic causes had become an ingrained habit with most Americans, irrespective of any tax concessions. As far back as 1933, a member of the President's Research Committee on Social Trends concluded, on the basis of the 1922 to 1929 income tax experience, that "the ratio between income and contributions is so consistent throughout the period as to suggest that giving is more definitely regulated by habit or tradition than by changes in income, tax rate, or any external circumstance."[4]

Whatever the reasons underlying the change in Congressional philosophy, the statistical record of the past three decades may throw light on some of the questions raised. Of course, the available data give little information about the donors' ultimate motives, which were not an object of the statistical study. In addition to personal values that ac-

ington Post editorial, inserted into the *Congressional Record* (65th Cong., 1st Sess., 1917, p. 6728), warned that unless a citizen's donations for the public good are allowed as a deduction the government itself will have to "support all those works of charity and mercy and all the educational and religious works which in this country have heretofore been supported by private benevolence. . . ."

[2] *Congressional Record*, 78th Cong., 2nd Sess., 1944, p. 3975.

[3] *Ibid.*, p. 4702.

[4] Sydnor H. Walker, "Privately Supported Social Work" in *Recent Social Trends in the United States* (Report of the President's Research Committee on Social Trends), Vol. II, New York, 1933, p. 1219.

count for the volume of philanthropic giving (religious beliefs, interest in particular causes such as education or science, social emulation, and so on), the tax saving may reduce the cost to the donor—in some cases even match it.[5] The complex motives are frequently not clear cut even to the donor. Our figures do, however, indicate somewhat the trend in volume of individual philanthropic contributions in the course of changing incomes, tax rates, and allowances for deductions. The statistical data may shed light on some of the policy problems raised above. And their examination is valuable because tax return data have been the chief reliance in past studies of philanthropic giving.[6]

Trend in Amounts Deducted for Contributions, 1917-1956

The total amounts annually deducted as philanthropic contributions by individuals on their tax returns through nearly four decades are shown in Table 13. The totals for 1920 to 1939 stayed within the range of $250 to $550 million. Since 1942 the amounts have exceeded $1 billion in every year, despite the introduction of the standard deduction which has been taken by the majority of taxpayers. For 1956 a total of $4.9 billion was reported. Of this $4.7 billion, or 95 per cent, was reported on taxable returns and hence had a direct effect on the total tax revenue and its distribution among taxpayers. On the basis of estimated adjusted gross income for 1957, total itemized contributions may be close to $5.5 billion. The steep rise since the beginning of World War II is largely explained by many newcomers to the tax-return universe whose incomes had previously been below the filing requirements.[7] Thus to distill some meaning from the fig-

[5] A gift made in property rather than cash can be costless to the donor. In such a transfer of property any accrued capital gains are not considered realized, and hence not taxed; yet the gift is deductible at the full market value of the property. The tax saving from the deduction from income of the gift may, in a few cases, exceed what the donor could have realized had he sold the asset and paid the tax on the accrued capital gain.

[6] See, among others, Sydnor H. Walker, *op.cit.*, pp. 1216-1220; Seymour E. Harris, *How Shall We Pay for Education?*, 1948, Chapters 8 and 9; F. Emerson Andrews, *Philanthropic Giving*, Chapter 1, and *Philanthropic Foundations*, Chapter 13 (both published by Russell Sage Foundation, New York, 1950 and 1956); John Price Jones, *The American Giver*, 1954; Thad L. Hungate, *Financing the Future of Higher Education*, Teachers College, Columbia University, New York, 1946, Chapter 5.

[7] It is occasionally overlooked that a time series based on tax returns is likely to have an upward growth bias. Thus Harris (*op.cit.*, p. 133), compared changes in contributions between 1941 and 1943 as reported on tax returns with changes in national income: "In 1943 income was about 55 per cent above that of 1941; and

TABLE 13

Philanthropic Contributions and Adjusted Gross Income on Tax Returns with Itemized Deductions, 1917-1956

(dollars in millions)

YEAR	*Taxable Returns* Contributions (1)	Adjusted Gross Income (2)	Ratio of Contributions to AGI (per cent) (1) ÷ (2) (3)	*All Returns* Contributions (4)	Adjusted Gross Income (5)	Ratio of Contributions to AGI (per cent) (4) ÷ (5) (6)
1917[a]	235	11,004	2.14	245	11,664	2.10
1920[b]	348	21,880	1.59	387	25,571	1.51
1922	343	16,678	2.06	425	23,577	1.80
1923	422	19,396	2.18	535	27,481	1.95
1924	441	21,541	2.05	533	28,468	1.87
1925	371	19,280	1.92	442	24,356	1.81
1926	395	19,355	2.04	484	24,606	1.97
1927	423	20,157	2.10	508	25,368	2.00
1928	459	23,307	1.97	541	28,473	1.90
1929	441	22,725	1.94	540	28,225	1.91
1930	357	15,429	2.31	434	21,116	2.06
1931	242	10,405	2.32	354	16,067	2.20
1932	231	9,006	2.56	317	13,830	2.29
1933	185	8,290	2.23	282	12,964	2.18
1934	200	9,331	2.14	280	14,524	1.93
1935	227	11,140	2.04	310	16,683	1.86
1936	312	15,664	1.99	390	21,241	1.84
1937	352	16,897	2.08	445	23,478	1.90
1938	310	14,123	2.20	414	21,026	1.97
1939	387	17,467	2.22	499	25,518	1.96
1940	570	25,875	2.20	740	39,921	1.85
			RETURNS WITH ITEMIZED DEDUCTIONS ONLY			
1941	876	38,780	2.26	1,002	45,501	2.20
1942	1,320	54,134	2.44	1,450	59,594	2.43
1943	1,813	74,315	2.44	1,836	75,062	2.45
1944	1,235	32,468	3.80	1,258	32,694	3.85
1945	1,424	34,779	4.09	1,450	34,955	4.15
1946	1,559	38,173	4.08	1,639	39,569	4.14
1947	1,875	44,499	4.21	1,974	45,862	4.30
1948	1,756	42,912	4.09	1,881	44,890	4.19
1949	1,897	44,795	4.23	2,032	46,825	4.34
1950	2,129	53,109	4.01	2,260	55,116	4.10
1951	n.a.	63,236	—	n.a.	65,261	—
1952	2,968	71,682	4.14	3,116	73,643	4.23
1953	3,383	80,817	4.19	3,556	82,871	4.29
1954	3,671	89,381	4.11	3,893	92,334	4.22
1955	n.a.	104,641	—	n.a.	108,528	—
1956	4,650	119,731	3.88	4,878	123,719	3.94

Figures include returns of fiduciaries up to 1944, and after that exclude fiduciary return figures.
[a] For net incomes above $2,000 only.
[b] For net incomes above $1,000 only.
Source: *Statistics of Income.*

ures shown, we must view them against the background of another series, such as income reported on tax returns and the countrywide aggregate of philanthropic contributions.

For the two decades up to 1940 it is possible to compare total contributions and total income reported on taxable returns for the years up to 1940. For those years we observe a fairly stable relationship, contributions remaining close to 2 per cent of total income reported (Chart 3). In the 1920's annual contributions on taxable returns varied typically between 1.9 and 2.2 per cent of reported income; in the four depression years 1930-1933 they rose to a level of 2.2 to 2.6 per cent; and thereafter (1934-1940) the relation of contributions to income dropped back to a level of 2.0 to 2.2 per cent.[8]

The gradual introduction, beginning with 1941, of the standard deduction makes it difficult to compare philanthropic gifts and income as reported on tax returns for recent years. For 1941-1943 the standard deduction applied only to taxpayers with less than $3,000 income. Assuming for this group a contributions-to-income ratio similar to that for 1940, we obtain the following figures for all returns comparable to the 1917-1940 series shown in Table 13:[9]

	Taxable Returns	All Returns
1941	2.13	1.98
1942	2.14	2.03
1943	2.18	2.12

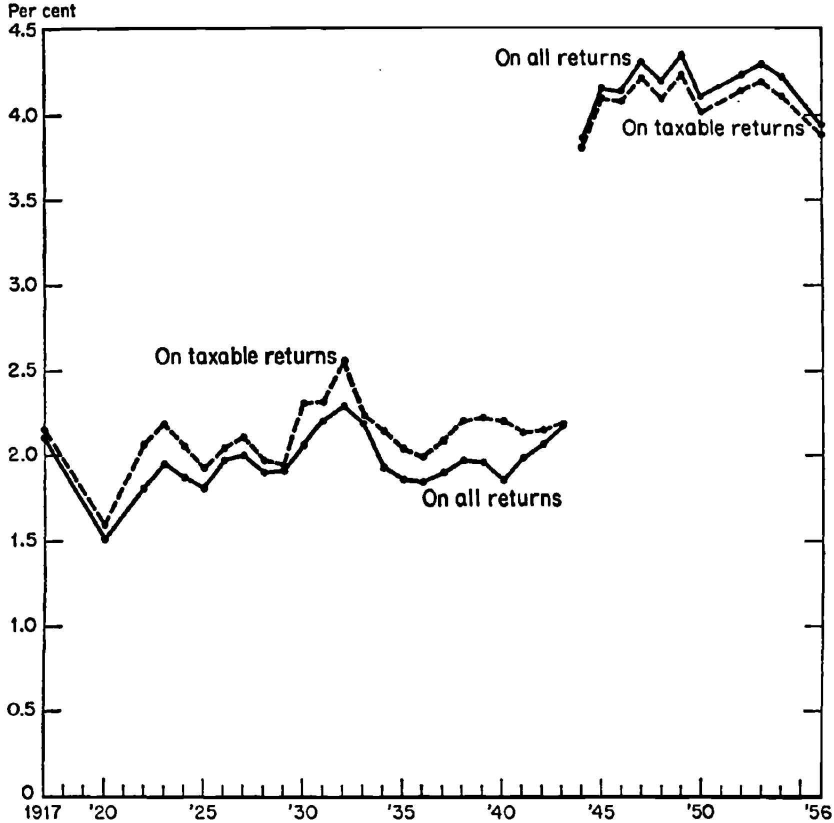
contributions and gifts were about 100 per cent above the 1941 figure. *In other words, contributions and gifts seem to have a high income elasticity: with a given percentage rise (decline) of income, the increase (reduction) in the percentage of gifts and contributions is large.*" (Author's italics.) It is widely thought, and with good reason as we shall see below, that the opposite is the case: contributions tend to change relatively less than income.

[8] On nontaxable returns, contributions were relatively lower in the interwar period. Thus for all returns (taxable and nontaxable) the percentages were typically 1.8 to 2.0 per cent in the 1920's; 2.1 to 2.3 for 1930-1933; and 1.8 to 2.0 for 1934-1940.

[9] The figures underlying these percentages are:

	Contributions			
	Reported	Estimated	Total	Adjusted Gross Income
		(taxable returns)		
1941	876	174	1,050	49,319
1942	1,320	233	1,553	72,670
1943	1,813	462	2,275	104,562
		(all returns)		
1941	1,002	252	1,254	63,032
1942	1,450	304	1,754	85,310
1943	1,836	466	2,302	106,149

CHART 3



Source: Table 13 and footnote 9, Chapter 4.

Contributions as Per Cent of Adjusted Gross Income on Tax Returns with Itemized Deductions, 1917-1956

This projection appears not unreasonable in the light of the reported figures for returns with incomes under $3,000 for 1922-1940, and for returns with incomes over $3,000 for 1922-1943 (Table 14 and Chart 4). On average, contributions on taxable returns with incomes over $3,000 remained practically unchanged relative to incomes: they averaged 2.10 per cent of adjusted gross income in 1922-1924 and 2.09 per cent in 1941-1943. For the group with incomes under $3,000 we observe a similarly stable relation between reported gifts and income from 1932 to 1939. But the stable ratio represents a sharp upward shift from that of 1922 to 1932, the year when personal exemptions were lowered with a consequent increase in the number of family-tax

TABLE 14

Reported Philanthropic Contributions and Estimated Adjusted Gross Income on Taxable Returns of Three Income Groups, for Three Periods, 1922-1956

(dollars in millions)

	Under $3,000			$3,000 and Over			$50,000 and Over[a]		
YEAR	Contributions (1)	Adjusted Gross Income (2)	Ratio of Contributions to AGI (per cent) (1) ÷ (2) (3)	Contributions (4)	Adjusted Gross Income (5)	Ratio of Contributions to AGI (per cent) (4) ÷ (5) (6)	Contributions (7)	Adjusted Gross Income (8)	Ratio of Contributions to AGI (per cent) (7) ÷ (8) (9)
1922	67	4,015	1.66	276	13,334	2.07	63	2,063	3.08
1923	80	4,618	1.74	341	15,677	2.17	73	2,140	3.43
1924	82	4,739	1.72	360	17,469	2.06	91	2,649	3.45
1925	31	2,165	1.42	340	17,797	1.91	112	4,190	2.68
1926	34	2,258	1.50	361	17,532	2.06	125	4,257	2.92
1927	34	2,098	1.64	389	18,225	2.13	145	4,922	2.95
1928	34	2,102	1.59	425	21,599	1.97	176	7,041	2.49
1929	29	1,996	1.44	412	21,149	1.95	173	6,721	2.58
1930	33	2,025	1.66	324	13,986	2.32	104	2,790	3.74
1931	24	1,367	1.78	217	9,123	2.38	59	1,361	4.36
1932	50	2,132	2.37	180	6,584	2.74	40	586	6.76
1933	42	1,877	2.23	143	6,251	2.29	29	770	3.77
1934	37	1,718	2.13	163	7,878	2.07	34	981	3.47
1935	41	2,035	2.03	186	9,403	1.98	42	1,304	3.25
1936	57	2,779	2.06	255	13,244	1.92	70	2,194	3.21
1937	70	3,417	2.04	282	13,990	2.02	73	2,014	3.62
1938	69	3,208	2.16	241	11,340	2.12	43	1,273	3.41
1939	96	4,331	2.21	291	13,542	2.15	57	1,454	3.89
1940	220	10,108	2.18	350	16,107	2.17	65	1,694	3.84

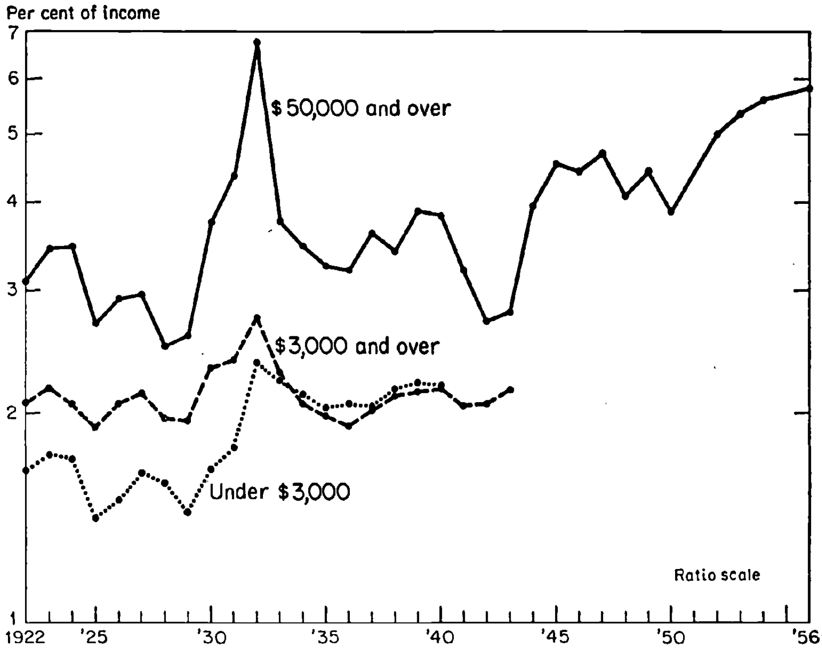
(concluded on next page)

TABLE 14, *concluded*

YEAR	*Under $3,000*			*$3,000 and Over*			*$50,000 and Over*[a]		
	Contributions (1)	*Adjusted Gross Income* (2)	*Ratio of Contributions to AGI (per cent)* (1) ÷ (2) (3)	*Contributions* (4)	*Adjusted Gross Income* (5)	*Ratio of Contributions to AGI (per cent)* (4) ÷ (5) (6)	*Contributions* (7)	*Adjusted Gross Income* (8)	*Ratio of Contributions to AGI (per cent)* (7) ÷ (8) (9)
1941				443	21,572	2.05	73	2,266	3.21
1942				611	29,593	2.06	76	2,799	2.71
1943				973	44,996	2.16	95	3,423	2.79
1944							130	3,285	3.96
1945							173	3,801	4.55
1946							198	4,466	4.43
1947							209	4,460	4.69
1948							249	6,084	4.09
1949							240	5,404	4.44
1950							298	7,676	3.88
1951							n.a.	7,888	n.a.
1952							363	7,246	5.01
1953							352	6,583	5.35
1954							438	7,826	5.60
1955							n.a.	9,116	n.a.
1956							574	9,892	5.80

[a] Returns for individuals with itemized deductions only, beginning 1944.
Source: *Statistics of Income.*

CHART 4



Source: Table 14.

Philanthropic Contributions Reported on Taxable Returns as Per Cent of Income Reported, for Three Selected Income Groups, 1922-1956

returns filed in the low-income ranges. Further lowering of exemptions in 1940 might be expected to produce a similar effect in the years up to 1944, but available evidence does not suggest it (see Table 19 below). It appears that the relation between reported gifts and income on tax returns remained virtually unchanged from the early 1920's through 1943.

No simple conjectures are possible for years after 1943, which are marked by extension of the optional standard deductions to all taxpayers. The upper limit on its dollar amount, however, tended to make its choice relatively most frequent among taxpayers with low or modest incomes. For those continuing to itemize their deductions, contributions fluctuated around a fairly stable level of 4 per cent of income between 1944 and 1956 (Table 13). For 1956, the percentage was 3.9 per cent, and for the intervening 9 years for which there are figures, they were consistently somewhat over 4 per cent of income. But interpretation of this apparent stability is more difficult when it is viewed in conjunction with the steady rise since 1944 in the proportion of taxpayers choosing to file itemized returns. Between 1944 and 1956, the number of taxable returns with standard deduction declined from 82 to 63 per cent of the total; and the dollar amount of standard deductions declined from 63 to 37 per cent of total personal deductions.[10]

The pronounced shift from the standard to itemized deductions raises the possibility that the level trend of 1944-1956 in the ratio of contributions to income, as reported on returns with itemized deductions, does not genuinely indicate a stable relation for those years comparable to that for 1917-1943. Table 14 and Table 19 below show that for income groups of $50,000 and over, the ratio of contributions to income has risen considerably since 1943. Because of the $1,000 limit on the standard deduction, only a small number of taxpayers in those groups made use of it; consequently, the relation between gifts and incomes revealed on these returns does not suffer the same distortion as that on returns farther down the income distribution. The same upward trend in the ratio of reported contributions to income might have obtained for taxpayers in all income groups, had it not been for the sustained changeover, at lower levels of income, from the standard to itemized deductions.

The changeover appears to be strongly associated with the postwar rise in homeownership, that is, with itemized deduction of property taxes and mortgage interest, and the liberalization of the medical expense deduction allowance. As a result, returns with contributions somewhat below the previous average for those who itemize, may have been swept into several income groups, covering up an over-all rising trend of contributions to income reported. This reasoning is supported, when we observe the change in number, between 1944 and 1956, of tax returns reporting deductions for contributions and for the three other items. The frequencies for the $3,000 to $10,000 income range, from which about 60 per cent of the deducted contributions for 1956 were reported are shown in the tabulation below.

	NUMBER WITH				
	Philanthropic Contributions	Taxes Paid	Interest Paid	Medical Deductions	Itemized Deductions
			(in thousands)		
1944	2,764	2,691	1,786	1,038	2,923
1956	12,581	12,734	10,523	7,549	13,010
	PER CENT OF RETURNS WITH ITEMIZED DEDUCTIONS				
1944	94.6	92.1	61.1	35.5	100.0
1956	96.7	97.9	80.9	58.0	100.0

10 See Tables 54 and 55 in Chapter 8.

Returns with deductions for interest on personal indebtedness rose from three-fifths to four-fifths of the total number itemizing, and the number with medical expense deductions from 35 to 58 per cent in the $3,000 to $10,000 income group. The number with deductions for taxes paid, less than the number with deductions for contributions in 1944, exceeded that number in 1956. The same developments were even more pronounced for the $5,000 to $10,000 income group, which accounted for two-fifths of all itemized contributions in 1956. The decline of its ratio of contributions to income (from 4.1 in 1949 to 3.5 in 1956; see Table 19) supports the hypothesis that it was the rise in homeownership with its attendant deductions, and the liberalization of the medical deduction, rather than the size of contributions, that influenced the increasing choice of the long-form return. The observed movement in the ratio of contributions to income for returns with itemized deductions cannot be assumed to characterize standard deduction returns, for which the trend could well have been upwards for recent years.

Tax Equivalent of Deductions for Philanthropic Contributions

Figures for the annual flow of philanthropic contributions as deducted on personal income tax returns, the subject of our discussion so far, tell us little about the resulting tax reduction for contributors and the so-called revenue cost to the government. Estimates are presented in Table 15 for the period 1924-1956. Successive rises in tax rates chiefly account for the continuing rise of the government's participation in deductible gifts: from an average of over 10 per cent before 1932, to about 15 per cent in the years before World War II, and to about 30 per cent in the years since our entrance into World War II (Chart 5). We estimate that the tax cost of itemized contributions reached 38 per cent, or $539 million in 1945, when tax rates were at their wartime peak, and about 32 per cent or nearly $1.5 billion in 1956.

To round out the picture, there are other ways in which the federal government, through the tax system, offers rebates on funds donated for philanthropic purposes. The laws for the corporation income tax, estate tax, and gift tax (property transfers) all permit deductions for gifts to philanthropy. In addition, the income of nonprofit organizations is also tax free. Finally, there is the revenue foregone on some

TABLE 15

Contributions Reported on Taxable Returns, Cost of Deductions to Government, and Net Cost of Contributions to Taxpayers, 1924-1956

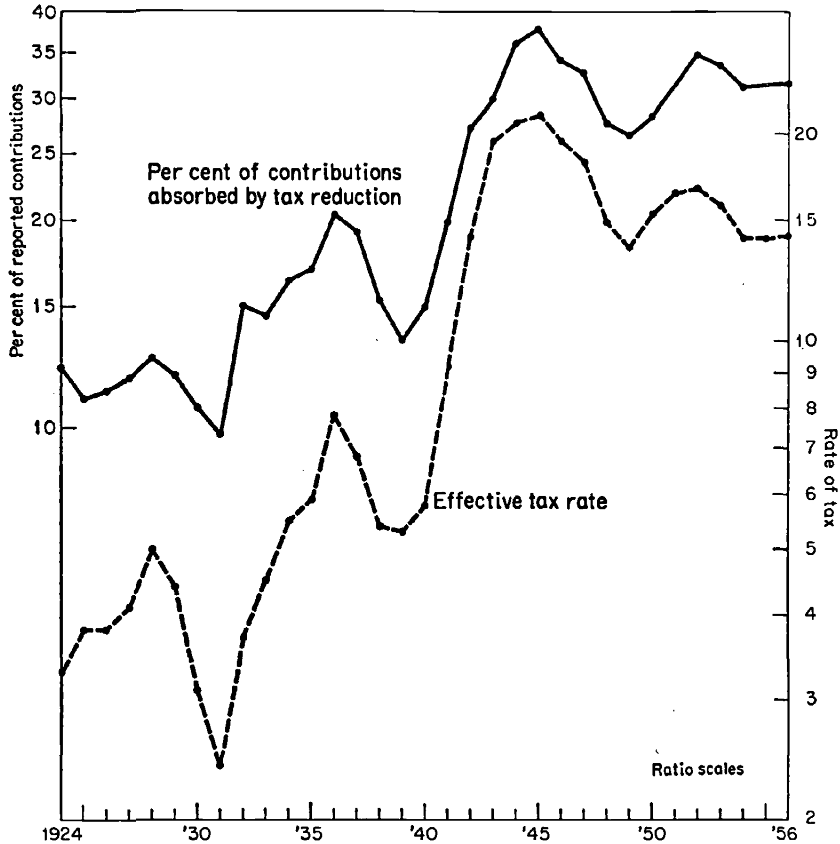
(dollars in millions)

YEAR	*Contributions Reported on Taxable Returns* (1)	*Cost to the Government*[a] (2)	*Net Cost to the Contributors* (1) — (2) (3)	(2) ÷ (1) *(per cent)* (4)	*Effective Rate of Tax Liability*[b] *(per cent)* (5)
1924	441	54	388	12.2	3.3
1925	371	41	330	11.0	3.8
1926	395	45	350	11.3	3.8
1927	423	50	373	11.8	4.1
1928	459	58	401	12.6	5.0
1929	441	52	388	11.9	4.4
1930	357	38	319	10.7	3.1
1931	242	24	218	9.8	2.4
1932	231	35	196	15.0	3.7
1933	185	27	158	14.5	4.5
1934	200	33	167	16.3	5.5
1935	227	39	189	17.0	5.9
1936	312	64	248	20.4	7.8
1937	352	68	285	19.2	6.8
1938	310	47	262	15.3	5.4
1939	387	52	335	13.4	5.3
1940	570	85	485	15.0	5.8
1941	876	175	701	19.9	9.2
1942	1,320	358	961	27.2	14.2
1943	1,813	542	1,271	29.9	19.5
1944	1,235	445	791	36.0	20.7
1945	1,424	539	885	37.8	21.2
1946	1,559	531	1,028	34.1	19.5
1947	1,875	613	1,262	32.7	18.2
1948	1,756	487	976	27.7	14.9
1949	1,897	504	1,393	26.6	13.7
1950	2,129	603	1,526	28.3	15.3
1951	n.a.	n.a.	n.a.	n.a.	16.4
1952	2,968	1,030	1,939	34.7	16.6
1953	3,383	1,133	2,251	33.5	15.7
1954	3,671	1,144	2,527	31.2	14.1
1955	n.a.	n.a.	n.a.	n.a.	14.1
1956	4,650	1,465	3,185	31.5	14.2

[a] For method of calculation, see Appendix G.

[b] Tax liability as reported in *Statistics of Income* divided by adjusted gross income on taxable returns (as shown in Table 13).

CHART 5



Source: Table 15.

Per Cent of Taxpayers' Reported Contributions Absorbed by Tax Reduction, and Effective Rate of Tax Liability on Returns with Itemized Deductions, 1924-1956

fraction of the standard deduction. In round numbers, the 1956 tax cost of $1.5 billion on individual itemized returns would be raised to around $2.6 billion by addition of the tax cost of corporation gifts, property transfers, income of nonprofit organizations,[11] and the por-

[11] This estimate takes account only of tax concessions accorded philanthropy in particular. No attempt is made to estimate the tax equivalent of the income of philanthropic organizations received in the form of gifts. Since gifts are not taxable to the recipient in the federal income tax, philanthropy is in this instance accorded no tax concession that is not equally available to others. Only the deductibility for the donor of gifts made to philanthropic organizations is unique. Many hold that gifts should be taxable as income to the recipient in the same manner as any other receipts that add to his spending power (see, for instance, Henry C. Simons, *Personal Income Taxation*, Chapter 6). But we are not concerned with this larger problem here.

tion of the standard deduction allotted to philanthropic contributions.[12]

Comprehension of the figures showing the amount of tax reduction to contributors is not as simple as the frequent descriptions of a "tax loss" to the government and a subsidy to philanthropy suggest. The tax cost must be interpreted in the light of the effect on government expenditures if part of the deducted contributions were not made. Whether the tax reduction is actually an indirect subsidy to philanthropy depends upon the influence of the deduction allowance on private gifts. The significance of the tax cost of the deduction depends on both considerations.

To the extent that government expenditures might have to replace a part of private expenditures in the absence of allowable deductions, larger tax collections would be required. To avoid this, public action can be attempted, as it has been, in the form of tax relief measures.[13] To the extent that such measures are successful, the government's budget understates its share in the determination of output. In the case of tax relief for donors to philanthropy, no government subsidy is active unless private gifts increase with tax relief. If gifts show little or no sensitivity to the tax rebate conditional on them, then the cost of the deduction simply amounts in effect, though not by intent, to rewarding taxpayers for contributing to socially desirable activities.

Thus the tax cost of the deduction has differing significance depending on two considerations: (1) The degree of public interest in the activities financed by the contributions. The tax cost figures, as

[12] Estimated tax cost of the four categories outside itemized personal deductions was obtained as follows: for the corporation tax 43 per cent of the $413 million of gifts reported by net income corporations in *Statistics of Income*, 1956-1957, was included. For bequests and gifts of property, the amount reported in *Statistics of Income*, 1954, was multiplied by the ratio of reported gross tax to net estate after specific exemption. Hypothetical tax liability on income of nonprofit organizations was reached by assuming a 4 per cent rate of return on $15.8 billion of corporate securities and mortgages, and 3 per cent on $5.8 billion of government securities, owned in 1955 (see Morris Mendelson, *The Flow of Funds through the Financial Markets, 1953-1955*, unpublished mimeo, National Bureau of Economic Research, Table 24-1). On $800 million of investment income thus computed, we estimated tax liabilities at $300 million. Finally, we computed the fraction for the standard deduction under the personal income tax by assigning about 17 per cent of the standard deduction to philanthropy. Tax liability on this amount was then computed in the manner set forth in the note to Table 15, given in Appendix G.

[13] For a recent discussion of this point, see Clarence D. Long and Selma Mushkin, "Welfare Programs and Economic Growth and Stability," in *Federal Expenditure Policy for Economic Growth and Stability*, Subcommittee on Fiscal Policy, Joint Economic Committee, 85th Cong., 1st Sess., 1957, pp. 1,028-30.

shown by Table 15, are relevant in a consideration of costs, but their meaning depends on whether the absence of some of the contributions would require increased government outlays, and hence increased tax collections, or not. (2) The first consideration is important only to the extent that contributions vary with the amount of tax rebate. It matters little whether or not private expenditures stand as substitutes for public expenditures (as they may in education, health, and welfare) if the flow of contributions is not significantly affected by the deduction. If the flow were maintained without the deductions, the government would not have to increase its expenditures in areas where private and public expenditures supplement each other.[14] In that case the deduction allowance would become only an equity question: should the allowance be given mainly in recognition of the consignment by taxpayers of part of their income to the public good without direct and immediate benefit to themselves?

Whether the subsidy or the equity motive underlay enactment of the deduction is a question to which Congress has so far not directly addressed itself. While the deduction is usually regarded as an encouragement of socially desirable expenditures, its form—a deduction from income rather than a tax credit—would lead one to infer that it was intended as an equity measure.

Tax Cost in Relation to Fields of Philanthropy

What factual evidence can we present on the question of the degree of public (governmental) interest in the purposes for which private contributions are made, and on the related question of the sensitivity of contributions to the amount of tax rebate?

To begin, we have the estimated distribution of contributions by broad areas of activity. In 1954, about two-thirds of the contributions made by living donors went to religious purposes; somewhat over one-fifth to health, education, and welfare; and the remainder to private foreign aid, foundations, and miscellaneous activities.[15] It is of course

[14] But even if the deduction were found unnecessary to maintain private gifts, the tax cost need not be viewed as a loss to the Treasury in the usual sense. To the extent that the loss in tax base caused by the deduction is compensated by higher rates, there is no actual revenue loss to the Treasury. Rather, there is a redistribution of the tax load, and possibly some loss to the community because of the economic effects of higher marginal rates.

[15] For the estimates on which this distribution is based, see Appendix F. F. Emerson Andrews has made similar estimates for gifts to philanthropy from all sources (living donors, bequests, and corporations). He estimates that one-half went to

difficult to measure the degree of public interest attached to those categories. Philanthropy now encompasses a wide variety of activities, some so recognized as in the public interest that for them a high degree of substitutability may be said to exist between private and governmental spending; in others the governmental interest is negligible. In some areas of health, education, and welfare, the government has tended, for some time, to supplement, if not at times to supplant,[16] private nonprofit institutions. In contrast, government's participation in the arts, literature, and religion has been slight—almost nonexistent in areas touching religion.

Substitutability, therefore, does not appear to be the only test that has been applied in determining what areas are appropriate for indirect government participation.[17] The 1954 Tax code, as noted previously, raised the deduction ceiling from 20 to 30 per cent for those taxpayers who contribute at least 10 per cent of their income to churches, hospitals, or educational institutions. While substitutability of public for private activity is high in health and education, both are areas into which the federal government has moved tardily and, especially in education, with great reluctance. That religious organizations were included among those for which the allowance was extended suggests that official public interest in a field is not Congress' sole criterion for selecting contributions to merit favorable treatment under the income tax.

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organized religion, and 43 per cent to education, health, and welfare in 1954. See Andrews, *Philanthropic Giving*, p. 73. (The percentages cited are Andrews' unpublished revisions of his earlier estimates.)

16 Andrews estimates that "government expenditure (including federal, state, and local) is now about nine times voluntary giving for purposes which a generation or two ago would have been deemed to lie wholly within the field of private 'charity'." *Ibid.*, pp. 43ff.

17 However, see the opinion of Sylvester Gates and John R. Hicks quoted in note 36 below. Gates and Hicks argue that total exemption from tax should be reserved to philanthropies performing functions "which are a well recognized responsibility of the state. When this condition is satisfied, it may be argued that, since any tax which was levied would have to be offset by a grant or subvention, the one can be cancelled against the other." They hold that the bulk of philanthropic activity, though desirable, is not indispensable and hence "will not appreciably diminish the State's own responsibilities or, consequently, the amount of money required to be raised by taxation. If, the amount to be raised by taxation remaining constant, the sector of income on which tax can be levied is reduced, a correspondingly added burden is cast on the remaining sector."

Effect of Income Tax on Level of Philanthropic Contributions

Next, we inquire, how sensitive have contributions by individuals been to changes in the amount of tax rebate offered to them? The data in Table 13 suggest that, despite significant changes in tax rates during the 1930's and 1940's, reported contributions showed little, if any, change in relation to income. Beginning with 1941, however, figures for reported contributions do not include amounts contributed by taxpayers choosing the standard deduction, and therefore give only a partial picture (see the section of this chapter dealing with the trend in contributions reported on tax returns). For a more reliable picture, annual figures of total contributions by living individuals would be preferable. Unfortunately we have only rough estimates in the area of private philanthropy, be it of income or of assets. To some extent the lack of information may be ascribed to the vagueness of the term philanthropy, making it often more difficult to compare figures from different sources, and to the fact that nonprofit and charitable organizations, because of their very nature, do not report systematically on their receipts and financial condition.

In Table 16, three estimates of total gifts by living donors are shown with the totals of itemized contributions reported on tax returns for the period 1929-1954. The series in columns 1 and 2 are based largely on various institutional reports. The third series, by F. Emerson Andrews, is based primarily on tax returns with some "correction allowance for the probably too-high rate for reported incomes."[18] Despite Andrews' correction, the annual figures in his series based on tax returns exceed those of the other two by large amounts from 1941 on. This is shown graphically in Chart 6. While the Andrews series shows a very steep rise in the early forties, the two other series show a much less pronounced rise during that period. For 1954, our estimate, extending the Commerce Department figures, is $4.15 billion and that by Andrews $4.79 billion. Either of these estimates may approximate the true figure. The Commerce estimates and our extrapolation of them may have omitted significant amounts, or Andrews' correction for overstatement may be too small.[19]

[18] Andrews, *op.cit.*, p. 292.

[19] A recent estimate of $4.5 billion for 1954 by Surveys and Research Corporation came to our attention too late for use in this study. See *Stimulating Voluntary Giving to Higher Education and Other Programs,* American Association for the Advancement of Science, Washington, D.C., 1958, p. 40.

TABLE 16

Philanthropic Gifts by Individuals, Three Estimates, 1929-1954

(dollars in millions)

YEAR	*Extrapolated Commerce Series* (1)	*Jenkins* (2)	*Andrews* (3)	*Returns with Itemized Deductions*: *Contributions Reported* (4)	*Returns with Itemized Deductions*: *Income Reported as % of Total Income* (5)
1929	1,449	1,206	1,067	540	37.3
1930	1,378	1,190	981	434	33.9
1931	1,264	1,329	843	354	32.8
1932	990	1,188	702	317	37.4
1933	806	982	637	282	35.6
1934	832	862	662	280	32.9
1935	902	868	727	310	34.4
1936	952	919	830	390	36.8
1937	1,099	1,000	943	445	38.1
1938	990	1,006	884	414	37.8
1939	970	1,068	967	499	39.5
1940	1,053	1,044	1,064	740	56.9
1941	1,060	1,089	1,556	1,002	53.5
1942	1,259	1,277	2,108	1,450	55.6
1943	1,568	1,456	2,535	1,836	58.2
1944	1,824	1,852	2,691	1,258	23.8
1945	2,045	2,103	2,772	1,450	24.9
1946	2,151	2,242	2,929	1,639	25.4
1947	2,191	2,219	3,240	1,974	26.7
1948	2,446	2,366	3,319	1,881	24.3
1949	2,549	—	3,447	2,032	25.4
1950	2,729	—	3,688	2,260	27.4
1951	2,931	—	4,286	n.a.	28.8
1952	3,350	—	4,545	3,116	30.6
1953	—	—	4,779	3,556	32.6
1954	4,141	—	4,789	3,893	36.5

Source, by column

(1) For 1929-1942, from *Survey of Current Business*, Department of Commerce, June 1944, Table 3. Figures for 1943-1951 are projections based on data for only a small number of components. The figures for 1952 and 1954 are our rough estimates based on a variety of sources as explained in Appendix F.

(2) Edward C. Jenkins, *Philanthropy in America*, pp. 172-173.

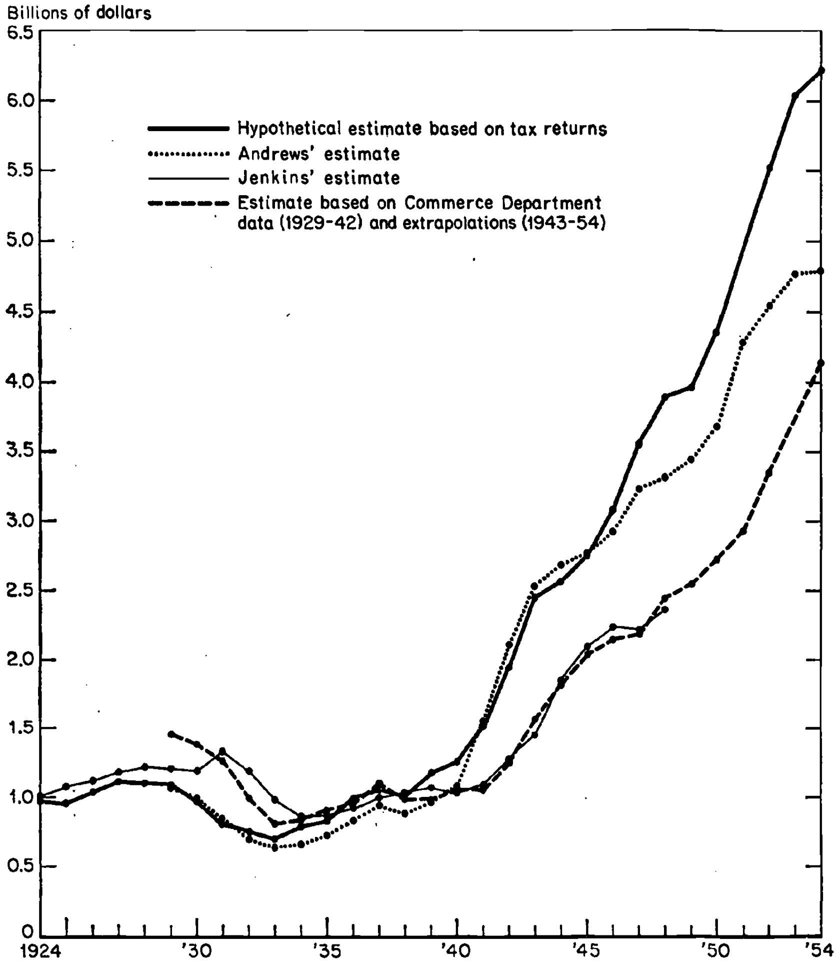
(3) F. Emerson Andrews, *Philanthropic Giving*, p. 72. The figures in this column are a revised series supplied by Andrews.

(4) *Statistics of Income.*

(5) Adjusted gross income reported on tax returns as a per cent of total adjusted gross income (countrywide) as derived from Commerce Department statistics on personal income.

The correct figure for 1954 may well be within the range of those two estimates, $4.2 to $4.8 billion. If the lower one based on a variety of institutional reports were more nearly correct, it would suggest the

CHART 6



Source: Tables 16, 17, and 18.

Total Philanthropic Contributions by Individuals, Four Estimates, 1924-1954

possibility of extensive overreporting of contributions on itemized returns, which amounted to $3.9 billion for 1954. This would leave contributions of only $0.26 billion for returns with the standard deduction on which the reported income was $137 billion. The implied ratio of contributions to income would be less than 0.2 per cent in contrast to 4.2 per cent for returns with itemized deductions. But even the higher estimate of $4.8 billion would leave contributions of only $0.90 billion for taxpayers electing the standard deduction, implicitly less than 0.7 per cent of income.

The Commerce Department estimates for 1929-1942, our extension of them up to 1954, and the other two estimates all suggest a sizable overstatement in the reported contributions on tax returns after 1940. We might hazard a guess at the size of the overstatement by attributing to standard deduction returns for all the years 1944-1954 the same ratio of contributions to income as may reasonably be assumed would have been reported on these returns for 1944.[20] When this amount is added to the reported figures in column 4 of Table 16, the tax return figures become conceptually comparable to the estimates for all individuals shown in the first three columns of the table. It amounts to attributing to returns with standard deductions contributions of somewhat over 1.5 per cent of income reported on these returns and assuming that the ratio would have been stable during 1944-1954. In view of the findings for itemized returns (Tables 13 and 14), it is unlikely that the ratio would have shown a decline, hence the assumption that it remained stable is more likely to give the hypothetical estimate a downward bias than an upward one.

The figures are shown in Table 17, plotted along with the other three series in Chart 6. The hypothetical estimates, like Andrews', exceed the other two from 1941 on by large absolute amounts. From 1945 on, the hypothetical estimates based on tax returns consistently exceed those by Andrews, whose corrections for overreporting appear to have been larger from after that date.[21] For 1952 and 1954 the three estimates are given below.

[20] The ratio of contributions to income for all returns in 1943 was used to obtain an estimate of the amount of contributions that would have been reported in 1944 in the absence of the 10 per cent standard deduction. This does not seem unreasonable in view of the percentages shown in Table 14 and Chart 3. An estimate of contributions that would have been reported on returns with standard deduction in 1944 was derived residually, by subtracting from the estimated total the amount actually reported.

[21] Andrews gives no explanation of the kind of correction allowance he used. For 1944 he imputes to those who reported no contributions a ratio of 0.4 of the reported ratio for that year, and lowers this rate to 0.35 for 1945, 0.3 for 1946 and 0.25 thereafter (*op.cit.*, p. 292).

TABLE 17

Contributions Itemized on Tax Returns and Hypothetical Estimates for All Individuals, Assuming Tax Return Ratios of Contributions to Income, 1924-1954

(millions of dollars)

YEAR	*Itemized Contributions* (1)	*Hypothetical Estimate of Total Contributions* (2)	*Total Adjusted Gross Income* (3)
1924	533	973	62,049
1925	442	954	67,137
1926	484	1,031	69,431
1927	508	1,114	70,130
1928	541	1,100	73,545
1929	540	1,084	75,597
1930	434	969	62,233
1931	354	805	48,969
1932	317	751	36,978
1933	282	700	36,445
1934	280	790	44,127
1935	310	828	48,447
1936	390	985	57,676
1937	445	1,057	61,559
1938	414	1,001	55,561
1939	499	1,177	64,674
1940	740	1,254	70,152
1941	1,002	1,520	85,101
1942	1,450	1,944	107,172
1943	1,836	2,449	129,035
1944	1,258	2,567	137,495
1945	1,450	2,762	140,185
1946	1,639	3,088	156,065
1947	1,974	3,559	171,563
1948	1,881	3,898	184,795
1949	2,032	3,966	184,292
1950	2,260	4,359	201,446
1951	n.a.	—	226,603
1952	3,116	5,521	240,645
1953	3,556	6,036	254,450
1954	3,893	6,216	252,987

Source: Column 1: *Statistics of Income*; column 2: see Appendix F; column 3: see Appendix A, Notes to Table 1, line 1.

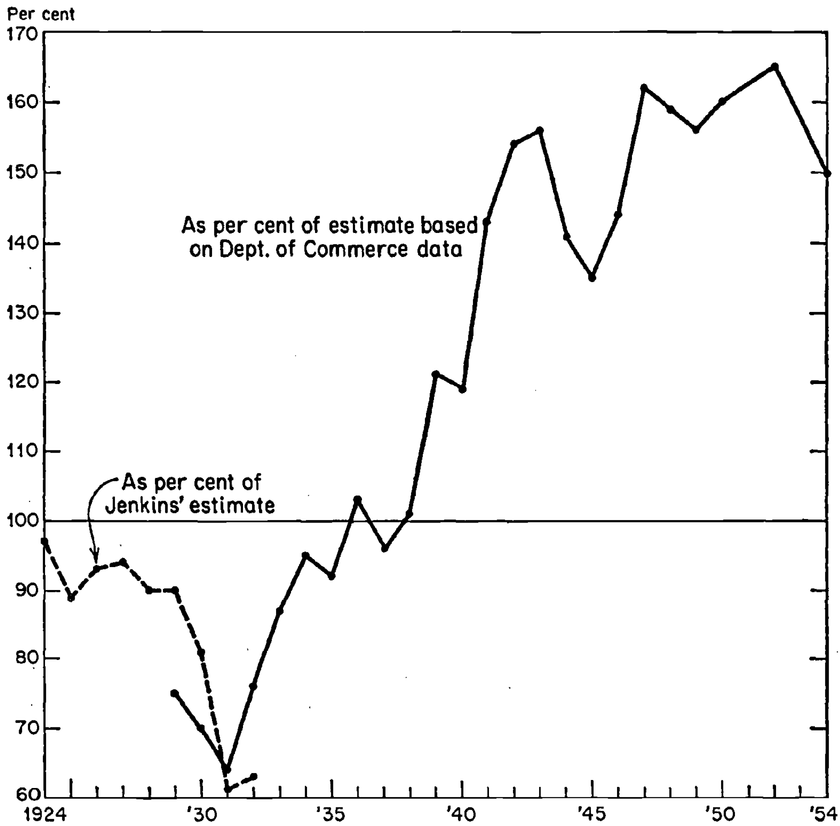
	1952	1954
	(billions of dollars)	
(1) Based on tax returns (Andrews)	4.5	4.8
(2) Based on reports of organizations	3.35	4.1
(3) Hypothetical, based on tax returns (assuming 1944 ratio of contributions to income for returns with standard deduction)	5.5	6.2
(3) ÷ (1)	1.2	1.3
(3) ÷ (2)	1.6	1.5

A number of explanations are possible for the large gap between the hypothetical tax return figure and the estimate based on institutional sources. First, there may be definitional differences. Taxpayers may have included a wider area under philanthropy than is covered by the estimates which start at the other end of the transactions. The concept of philanthropy is vague and fuzzy. Second, gifts of property may be evaluated at higher figures by donors than by recipients. Third, the roughness of some components of the estimates based on reports of organizations are subject to error: for example, the component estimate of gifts to foundations, particularly family foundations, may be on the low side. Fourth, we have made no allowance for gifts to so-called "rackets" (from which no reports could be available), but such gifts reported as deductions would also constitute a form of overreporting. Finally, the previously noted possibility that taxpayers may have considerably overstated their contributions under the impact of high tax rates in the 1940's and 1950's, suggests an explanation for the discrepancy between the estimates.[22] The explanations for discrepancies between estimates may in varying degrees be related to changes in the level of tax rates. Differences in values reported for property transfers are likely to have increased with the rising importance of the income tax. The unknown, but certainly rising, number of family foundations are a product of the tax structure.

[22] Overstatement of contributions on tax returns is difficult to check because of the present form of the deduction allowance. A revamping of the provisions for the deduction along the lines of the current British method would remove practically all possibility of tax evasion due to faulty reporting. The British tax law allows what amounts to a flat-rate tax credit for charitable contributions. The rebate goes to the eligible institution directly, upon its submission of a claim. The taxpayer merely remits his "net gift" to the philanthropy in question. For a more detailed discussion of the method, see pp. 87ff. of this chapter.

A casual inspection of Chart 6 may tempt one to attribute the large gap between the two tax-return series and the two series obtained from recipients' reports to the sharp rise in tax rates during World War II. But the evidence is not clear cut. In Chart 7 we compare the movements of the two types of series by expressing the hypothetical estimates based on tax returns as a per cent of estimates based on

CHART 7



Source: 1924-32: column (2), Table 17 ÷ Jenkins' estimates shown in Tables 16 and 18; 1929-54: column (2), Table 17 ÷ column (1), Table 16.

Estimates of Contributions Based on Tax Data as Percentage of Estimates Based on Recipients' Reports, 1924-1954

recipients' reports. While there is no clear indication of a trend until after 1935, it is nevertheless clear that the tax-return figures began to rise relative to the Commerce Department estimates, and to exceed them before 1940. Is it likely that the turning point in the taxpayers' zeal to report gifts to philanthropy came well before the 1940's?

The fraction of contributions reported on taxable returns that represented a cost to the government was shown in Table 15 and Chart 5 above. There was a significant jump in this fraction in the early '30's. Some tax increases occurred in 1932 and 1936.[23] They may have had sufficient influence on subsequent taxpayer behavior to produce the results observed, although the early rises were mild compared to those that took place in the '40's. The amount of reported contributions that was paid for by the Treasury rose from a level of 10 per cent of the total in 1929-1931 to 15 per cent in 1932, and reached a high of 20 per cent in 1936. During World War II there were further increases in this percentage to a level well above 20 per cent. In 1945, the peak year, 38 per cent of the amount reported acted as a reduction in tax rather than in income. A similar pattern is produced when we plot the average effective rate of tax liability on income reported on tax returns (Chart 5). It rose from 2.4 in 1931 to 7.8 per cent in 1936; and again from 5.3 in 1939 to 21.2 per cent in 1945. This evidence is consistent with the hypothesis that the rise in deducted contributions, relative to the estimates developed independently of reports by donors, may have occurred in response to taxation developments of the 1930's as well as the 1940's.

In addition to some indication of how taxation developments have affected the reporting of contributions, we want to know whether, and how, taxation may have influenced the actual volume of contributions. Even with excellent estimates of the actual volume of contributions—currently not available—the answer would require some knowledge of what the volume of contributions would have been in the absence of rising tax rates. We possess no such knowledge. Nevertheless, rather than retreat from the question entirely, we can reach a partial and qualified answer.

In Table 18 and Chart 8 the estimates by Andrews and those from reports of recipient institutions are expressed as percentages of estimated total adjusted gross income for the period 1924-1954. In the period 1937-1942 the Andrews estimates rise relative to total income, whereas the Commerce Department estimates for that period decline relative to income; but outside that five-year period, their movements

[23] Exemptions were lowered and rates increased in 1932. In 1934 taxes were lowered slightly on "earned" income and raised, also slightly, on some property income. In 1936 taxes were again raised on dividend income, and on net incomes over $50,000. The increases in 1932 were the sharpest and most widespread among income groups.

TABLE 18

Estimated Total Philanthropic Contributions by Individuals as Per Cent of Total Adjusted Gross Income, 1924-1954

YEAR	*Estimated Contributions as Per Cent of Total AGI* (1)	(2)
1924	1.6	1.6
1925	1.6	1.4
1926	1.6	1.5
1927	1.7	1.6
1928	1.7	1.5
1929	1.6	1.4
1930	1.9	1.6
1931	2.7	1.6
1929	1.9	1.4
1930	2.2	1.6
1931	2.6	1.7
1932	2.7	1.9
1933	2.2	1.7
1934	1.9	1.5
1935	1.9	1.5
1936	1.7	1.4
1937	1.8	1.5
1938	1.8	1.6
1939	1.5	1.5
1940	1.5	1.5
1941	1.2	1.8
1942	1.2	2.0
1943	1.2	2.0
1944	1.3	2.0
1945	1.5	2.0
1946	1.4	1.9
1947	1.3	1.9
1948	1.3	1.8
1949	1.4	1.9
1950	1.4	1.8
1951	1.3	1.9
1952	1.4	1.9
1953	—	1.9
1954	1.6	1.9

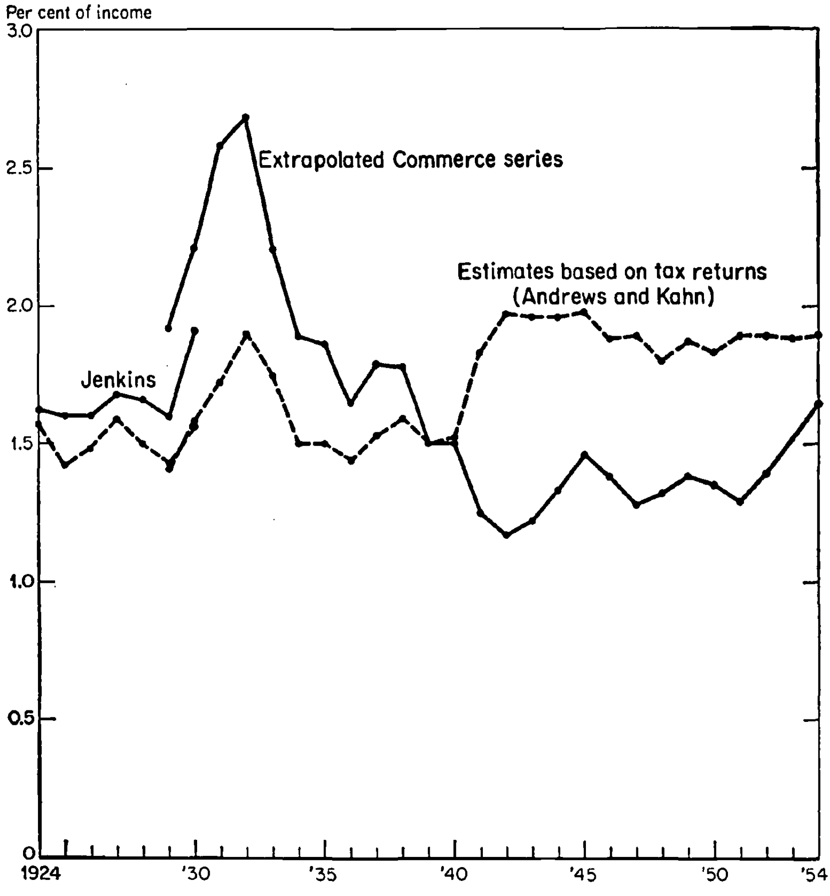
Source: Column 1, *1924-1931*: Jenkins, Table 16, column 2. Jenkins' estimates for 1924-1928 (divided by total AGI) are: *1924*, 1,003; *1925*, 1,073; *1926*, 1,114; *1927*, 1,179; *1928*, 1,218.

1929-1954: Commerce Department and our extrapolations as in Table 16, column 1.

Column 2, *1924-1931*: Table 17, column 2. *1929-1954*: Andrews, Table 16, column 3.

are essentially parallel, that is, they show roughly identical trends. During 1940-1954, neither series shows a pronounced trend up or down, relative to income, though both are somewhat higher in 1954 than in 1940. This is of interest in view of the introduction of the standard

CHART 8



Source: Table 18.

Estimated Total Contributions by Individuals as Per Cent of Total Adjusted Gross Income, 1929-1954

deduction in the early 1940's, which severed the connection between giving and tax reduction for most taxpayers with incomes below $10,000, and also for many above that level. If there is a connection between philanthropic giving and the deductibility of gifts in the income range from which most returns with the standard deduction come, a decline in the per cent of total income contributed to philanthropic enterprises might have been expected.

That, apparently, no decline has occurred is not proof of the absence of such a connection. It is also possible that the rise in tax rates of the early 1940's sufficiently stimulated contributions by taxpayers filing the itemized return to offset any possible decline in contributions blanketed by the standard deduction. Some evidence bearing on the possible effect of the standard deduction on the flow of contributions is given in the next section dealing with contributions by income groups. Briefly, consumer survey data for 1941 and 1950, in Table 23, show that for units with incomes below $5,000, most of whom choose the standard deduction, the ratio of contributions to income has risen somewhat over that period. There is no evidence that the institution of the standard deduction had a repressive effect on the share of income devoted to philanthropy. A large segment of the public, subject to marginal rates ranging from 20 to 30 per cent, may not be influenced by tax incentives in making such gifts. Our observations are in line with Sydnor H. Walker's conclusion, on the basis of tax return data of the 1920's, "that the lowering of tax rates and the increase of general prosperity, which characterized the years from 1922 to 1929 inclusive, had little effect upon the contribution rate."[24] While the tentative conclusion from our data about the contributions of taxpayers with low and modest incomes is not extended to those of taxpayers with much higher incomes, its significance is extensive. We shall see below that the bulk of philanthropic contributions by living donors comes from those with incomes below $10,000.

The two possibilities that much philanthropic giving is independent of tax incentives and that deducted contributions are considerably overreported bring us back to the question whether the revenue cost of the contribution deductions is justified. In 1954, the cost came to $1.1 billion at the prevailing tax rates; inclusion of a fraction of the standard deduction raises the cost to $1.6 billion. The last figure is one-third as large as the amount living donors contributed to philanthropy in that year, according to one estimate; 38 per cent of the total, according to another. That is, the Treasury "sacrificed" on average one dollar, at existing tax rates, for every three that individuals donated to philanthropy. Whether this is too high a price to pay for a tax subsidy that possibly stimulates contributions to some undertakings in

[24] See "Privately Supported Social Work," p. 1219.

which the national interest is high cannot be answered within the context of this study. The issue is not solely one of arithmetic. Even if we could state with certainty that the tax rebate on contributions is not responsible for gifts of an equivalent amount, the further question remains, whether the public would prefer an increase in giving smaller than the tax rebate, rather than an alternative—direct use of those funds by government or rate reduction. The community may well decide that even a small fraction of the tax rebate diverted to private philanthropic enterprises is preferable to use of the full tax equivalent of the deduction for governmental enterprises. In the areas covered by private philanthropy the value of a given amount of privately allocated funds, though smaller in dollar amount, may exceed the value to society of direct governmental expenditures somewhat larger in dollar amount.

Reported Contributions by Size of Income on Tax Returns

A glance at Table 19 is sufficient to see that for the income groups[25] shown, the average percentage of deductions claimed for contributions has been well under the allowed limits (to 1951, 15 per cent of income; 1952-1953, 20 per cent; from 1954, 30 per cent). Until 1943 the contributions reported on taxable returns were less than 3 per cent of adjusted gross income at levels below $100,000, except briefly during the deep depression years when the relative decline in incomes was much greater than that in contributions. Over this wide range of income the rates of reported contributions show only slight increases. For example, between the two income groups $3,000 to $5,000 and $50,000 to $100,000, the rates are: 1.6 and 2.3 per cent in 1925-1929; 1.9 and 3.6 in 1932-1934; 1.8 and 2.3 in 1939; 2.2 and 2.4 in 1943. Comparison of rates for the under $2,000 income group and for the higher of the two shows even smaller differences, for the curve describing the

[25] The reader is reminded again that our presentation by income groups has several limitations: (1) the reporting unit is the individual tax return, meaning there are fewer persons included than in the family or spending unit; (2) the income concept is adjusted gross income, which has an important bearing upon intertemporal comparisons of high incomes, since the amounts of such items as capital gains and tax-exempt interest affect the reported income of taxpayers in accordance with the current tax law definition, rather than with a consistent income concept; (3) the reported contribution figures are subject to the twin evils of the forgetfulness and fabrications of some taxpayers. We have no clue to how these offset each other by income groups. But it may be in the nature of this type of deduction that the error is more significant at low income levels than at higher.

TABLE 19

Philanthropic Contributions as Per Cent of Income, and Distribution of Total, by Size of Income on Taxable Returns, Selected Years, 1922-1956

INCOME GROUPS[a] (*$000's*)	*1922*	*1924*	*Average 1925-29*	*Average 1932-34*	*1937*	*1939*	*1941 Itemized*	*1941 All Returns*	*1943 Itemized*	*1943 All Returns*
				CONTRIBUTIONS AS PER CENT OF ADJUSTED GROSS INCOME						
Under 2	1.8	1.8	1.6	2.5	2.2	2.3	2.9	1.6	3.3	1.4
2-3	1.5	1.6	1.5	1.9	1.8	2.0	2.2	1.5	2.4	1.4
3-5	1.6	1.7	1.6	1.9	1.7	1.8	1.9		2.2	
5-10	2.1	1.7	1.6	2.0	1.7	1.9	2.0		2.1	
10-25[b]	1.9	1.9	1.8	2.2	1.8	2.0	1.9		1.9	
25-50[b]	2.2	2.2	2.0	2.7	2.1	1.7	2.1		2.0	
50-100	2.6	2.8	2.3	3.6	2.8	2.3	2.5		2.4	
100-500	3.5	3.4	2.6	5.0	4.0	4.3	3.4		3.0	
500 and over	6.7	5.7	3.4	5.5	6.4	6.1	5.4		4.5	
Average	2.0	2.0	2.0	2.3	2.0	2.2	2.2	1.8	2.4	1.7
				PER CENT OF TOTAL CONTRIBUTIONS						
Under 2	12.7	10.2	3.7	13.8	13.7	15.1	22.8		22.6	
2-3	6.8	8.2	4.0	7.2	6.4	7.2	26.7		23.7	
3-5	19.1	24.5	10.3	18.1	18.4	20.5	18.5		29.0	
5-10	18.8	13.1	16.6	19.5	17.8	19.7	10.7		9.2	
10-25[b]	15.0	14.1	18.8	15.6	15.1	15.6	8.7		6.7	
25-50[b]	9.2	9.1	11.6	9.2	9.0	7.9	4.4		3.5	
50-100	7.3	7.7	9.9	6.7	6.2	5.3	3.2		2.4	
100-500	8.0	8.2	14.0	6.8	9.0	5.9	3.5		2.2	
500 and over	3.2	4.7	11.2	3.2	4.4	2.9	1.6		0.7	
Total[c]	100.0	100.0	100.0	100.0	100.0	100.0	100.0		100.0	

(concluded on next page)

TABLE 19, *concluded*

INCOME GROUPS[a] ($000's)	1945 Itemized	1945 All Returns	1947 Itemized	1947 All Returns	1949 Itemized	1949 All Returns	1954 Itemized	1954 All Returns	1956 Itemized	1956 All Returns
				CONTRIBUTIONS AS PER CENT OF ADJUSTED GROSS INCOME						
Under 2	5.3	0.7	5.5	0.8	5.8	0.7	6.2	0.8	6.1	0.8
2-3	4.6	0.8	4.8	0.9	5.1	0.9	5.5	1.1	5.2	1.2
3-5	4.2	1.0	4.4	1.1	4.4	1.2	4.4	1.5	4.2	1.5
5-10	3.8	1.6	4.0	1.7	4.1	1.3	3.8	1.6	3.5	1.7
10-25[b]	3.1	2.1	3.2	2.2	3.7	1.8	3.7	1.9	3.5	2.1
25-50[b]	3.0	2.6	3.1	2.7	3.1	2.5	3.3	2.7	3.3	2.8
50-100	3.5	3.3	3.6	3.4	3.3	3.1	3.9	3.7	4.1	3.8
100-500	4.8	4.7	4.8	4.7	4.6	4.5	6.7	6.5	6.9	6.8
500 and over	6.7	6.6	6.7	6.6	6.6	6.6	11.7	11.7	11.9	11.8
Average	4.0	1.2	4.1	1.4	4.1	1.4	4.1	1.8	3.9	1.9
				PER CENT OF TOTAL CONTRIBUTIONS						
Under 2	12.0		7.3		4.0		1.7		1.4	
2-3	16.8		15.4		10.6		5.1		3.8	
3-5	24.5		28.1		30.0		24.7		19.0	
5-10	13.6		16.8		21.9		36.2		40.2	
10-25[b]	13.4		13.9		13.1		10.9		16.1	
25-50[b]	7.6		7.3		7.8		9.5		7.0	
50-100	5.4		4.8		5.2		4.6		4.9	
100-500	5.1		4.6		5.5		5.1		5.1	
500 and over	1.6		1.8		2.0		2.2		2.4	
Total[c]	100.0		100.0		100.0		100.0		100.0	

Fiduciary returns are included in years up to and including 1949.

[a] Net income classes until 1943; adjusted gross income classes thereafter.

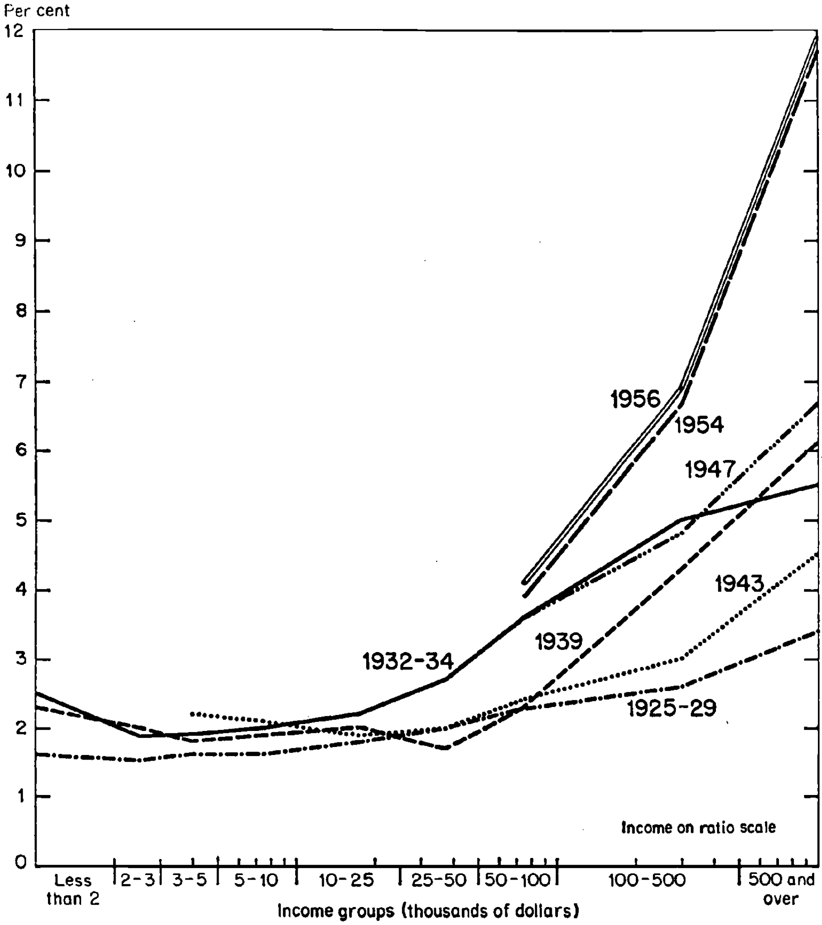
[b] For 1954 group limit is $20,000 instead of $25,000.

[c] Percentages may not add up to total because of rounding.

Source: *Statistics of Income.*

reported contribution rates is slightly U-shaped at the bottom with the trough occurring in the $2,000 to $5,000 income range (Chart 9). Above $100,000 the contributions-to-income ratio turned up appreciably.

CHART 9



Source: Table 19.

Philanthropic Contributions Reported on Taxable Returns as Per Cent of Income Reported, by Income Groups, Selected Years, 1925-1956

As indicated in the last section, an appreciable increase is evident in the reported rate of giving after 1943. Because the standard deduction became available to all income groups, beginning with 1944, it is not possible to compare the percentages for incomes below the $10,000 level with those before that year. The ratios of contributions to income for returns with itemized deductions and for all returns constitute upper and lower limits of the "actual" reported contribution rate which must lie somewhere between them. For the lower income groups the range offered by the two extremes is too wide to be useful, but as it narrows, going up the income scale, it gives us a good idea of the actual rate of reported giving for that income group. We can see that the possible range in the $10,000 to $25,000 group was 2.1 to 3.1 per cent in 1945 and 2.2 to 3.2 in 1947, a level not previously attained except in the early '30's. The same can be observed for the other income groups above that level: the lower limit of the possible range was above the level prevailing before the mid-'40's. For the highest group, the returns with incomes over $500,000, the contribution rate stayed above 6 per cent after 1943 and reached nearly 12 per cent in 1956.

The contribution rates presented in Table 19 are for all taxable returns, regardless of whether they reported such gifts or not. If we eliminate from each group's total the incomes reported on returns with no contributions, we get the rates for taxable donors' incomes rather than for all reported taxable incomes. The percentages are shown in Table 20.[26] Since the number claiming deductions for contributions is high relative to the total (Table 21), we find that the ratios for donors are only slightly higher than the ratios for all returns with itemized deductions. In 1937 the average deduction for contributions was 3 per cent of the income of donors in the lowest income group and almost 7 per cent in the highest, with a dip to 2.1 per cent in the middle of the income range. Again, comparison with recent years is not possible except for the upper income groups. For the latter the reported rate of giving has risen sharply since prewar years: in the $100,000 to $500,000 group from somewhat less than 5 per cent prewar to 7 per cent in 1956; and for the over $500,000 group from between 5 and 7 to 12 per cent. The increase in the rate of giving among donors further down in the income scale appears to have been much milder. Apparently the spread in the reported rate of giving between high and low income donors has increased somewhat in recent years.

The above discussion and tables give little indication of how many taxpayers approach the limit on the deduction in their claim of de-

[26] We possess no data distinguishing the incomes of those who claimed contributions from those who did not. However, on the assumption that the average income in a given income group is the same for claimants as for all returns, we closely approximated the average ratio of contributions to income of donors.

TABLE 20

Contributions as Per Cent of Income on Taxable Returns with that Deduction, by Income Groups, Selected Years, 1934-1956

INCOME GROUP[a] ($000's)	1934	1937	1939	1941	1945	1947	1949	1950	1952	1954	1956
Under 2	n.a.	3.1	n.a.	n.a.	6.2	6.6	6.7	6.6	7.1	6.9	6.8
2-3	n.a.	2.6	n.a.	n.a.	4.6	5.3	5.5	5.5	5.8	5.8	5.6
3-5	n.a.	2.2	n.a.	n.a.	4.5	4.7	4.5	4.4	4.6	4.5	4.4
5-10	2.4	2.2	2.3	2.3	4.1	4.3	4.2	4.0	3.9	3.9	3.6
10-25[b]	2.4	2.1	2.3	2.2	3.4	3.5	3.8	3.7	3.8	3.8	3.6
25-50[b]	2.8	2.5	2.0	2.4	3.2	3.3	3.3	3.1	3.4	3.4	3.4
50-100	3.3	3.2	2.6	2.8	3.8	3.9	3.6	3.1	3.8	4.0	4.1
100-500	4.1	4.5	4.8	3.8	5.3	5.4	5.0	4.2	5.9	6.8	7.0
500 and over	5.8	6.9	6.8	6.2	7.6	8.1	7.8	6.6	10.0	11.9	12.1
Average amount of contributions reported per return (dollars)	n.a.	139	n.a.	n.a.	198	225	251	254	271	277	284

[a] Net income classes up to 1944; adjusted gross income classes thereafter.
[b] For 1952 and 1954, group limit is $20,000 instead of $25,000.
Source: *Statistics of Income.*

ductions for contributions, a point worth examining in view of the two recent extensions of the limit. Frequency distributions of tax returns by size of income and by size of contributions reported are available for the years 1949, 1954, and 1956. They include, of course,

TABLE 21

Per Cent of Taxable Returns with Deduction for Philanthropic Contributions, by Size of Income Reported, Selected Years, 1937-1956

INCOME GROUP[a]	*All Returns*			*Returns with Itemized Deductions*[b]				
($000's)	1937	1939	1941	1945	1947	1949	1954	1956
Under 2	72.4	—	—	87.4	86.3	90.7	90.2	89.9
2-3	71.1	—	—	92.5	92.1	94.3	93.7	93.5
3-5	76.2	—	—	94.5	94.5	96.5	96.6	96.0
5-10	79.1	83.4	85.7	95.0	94.7	97.0	97.8	97.1
10-25[c]	82.9	86.9	88.1	95.2	95.8	97.6	98.1	98.2
25-50[c]	86.4	90.5	90.8	95.7	96.1	97.7	98.2	98.3
50-100	90.5	93.0	92.5	96.3	96.4	98.0	98.5	98.7
100-500	93.0	95.7	94.9	97.0	97.4	98.6	98.6	98.9
500 and over	91.9	96.6	95.1	100.0	97.6	97.4	98.4	98.5
Average	74.9	—	—	92.0	92.5	95.6	96.6	96.3

[a] Net income groups for years before 1944; adjusted gross income group thereafter.
[b] Individual returns only. On fiduciary returns contributions are not separately reported but are included in the "amounts distributable to beneficiaries" category for the years shown, except 1954 and 1956.
[c] Income groups are $10-20,000 and $20-50,000 in 1954.

only returns with itemized deductions for philanthropic contributions, and no short form returns. To avoid any bias arising therefrom, we estimated how many of the returns listed contributions amounting to more than 10 per cent of the income reported, on the reasonable assumption that contributions of that relative size would be itemized. The estimated number of such returns, as a per cent of total returns in each income group, is shown in Table 22. Figures in the 20 per cent columns for 1954 and 1956 are as tabulated by the Internal Revenue Service.

TABLE 22

Estimated Per Cent of Returns with Deducted Contributions at Least Ten or Twenty Per Cent of Adjusted Gross Income, by Income Groups, 1949, 1954, and 1956

INCOME GROUP ($000's)	*Total Number of Returns* *1949* (in thousands)	*1956*	*Per Cent of Returns* *1949* 10%	*1954* 10%	*1954* 20%	*1956* 10%	*1956* 20%
Under 2	19,038.4	14,974.9	1.8	2.1	0.4	2.3	0.4
2-3	12,137.6	8,043.8	2.3	3.5	0.3	3.5	0.4
3-5	14,138.4	16,327.6	2.4	3.2	0.1	3.1	0.2
5-10	4,837.8	16,339.8	2.5	4.0	0.1	3.8	0.1
10-20	802.0	2,419.3	3.1	3.2	0.3	2.8	0.3
20-50	287.7	581.3	4.2	4.6	0.7	4.5	0.7
50-100	46.1	89.2	8.2	10.5	2.2	10.8	2.6
100-500	13.3	22.0	17.3	n.a.	7.7	n.a.	8.5
500 and over	0.5	0.9	n.a.	n.a.	23.4	n.a.	26.5
Total	51,301.9	58,798.8	n.a.	n.a.	0.2	n.a.	0.3

The estimates were made on the basis of a frequency distribution of tax returns showing a deduction for contributions, by size of income and by size of contributions. See *Statistics of Income*, 1949, Part I, pp. 39-40; for 1954, p. 55; and for 1956, p. 41. The income class intervals used to estimate the frequencies shown were narrower than those in the above table. The 10 per cent level of income was set for each income class at 10 per cent of the average income in the class. For the contributions-size class into which the 10 per cent value fell, the frequencies between that value and the lower limit of the class were estimated by straight line interpolation. The number equal to or exceeding 20 per cent in 1954 and 1956 is tabulated in *Statistics of Income*.

In all three years the relative frequency of returns reporting contributions in excess of 10 per cent of income changed little with rising incomes up to the $20,000 level. Within that range the average frequency is about 3 per cent. Above that level, the relative frequency rises somewhat with income, but still remains below 5 per cent for the $20,000 to $50,000 group. It reached 17 per cent in the $100,000 to $500,000 group in 1949—the highest income group and the only year for which an estimate of the number with contributions over 10 per cent of income was possible. Above that income figure, the percentage is undoubtedly large. An unpublished Treasury Department estimate suggests that about one-third of the returns in the over-$500,000 income group reported contributions of 12 per cent or more of adjusted gross income for 1949. For 1954 and 1956 about one-fourth of returns in that group tabulated by the IRS reported contributions over 20 per cent of income.

The relatively small number of returns with contributions in excess of the biblical tithe in the income range below $50,000—which accounts for well over 90 per cent of aggregate contributions[27]—suggests that the number of taxpayers whose contributions might be affected by the ceiling imposed on the amount deductible is quite small.[28] This is borne out by the ratios of contributions to income shown for 1950 and 1952 in Table 20.[29] The rise of the ceiling from 15 to 20 per cent in 1952 appears to have had only a negligible effect on the volume of contributions below the $50,000 level. But for returns in the $100,000 to $500,000 group itemized contributions rose from 4 to 6 per cent of income, and for returns with over $500,000 from 7 to 10 per cent.

The further lift of the ceiling from 20 to 30 per cent in 1954 is again reflected only in the percentages for the two highest income groups, which rose from 6 to 7 per cent and from 10 to 12 per cent, respectively, between 1953 and 1956 (Table 20). Less than 0.5 per cent of all returns reported contributions in excess of 20 per cent of their income for 1954 and 1956 (Table 22). This is also true of returns up to the $20,000 income level. Less than 3 per cent of returns with incomes $50,000 to $100,000 and about 8 per cent of the returns in the $100,000 to $500,000 group reported contributions that high. The total amount reported for 1954 in excess of 20 per cent of income was $68 million, or less than 2 per cent of total contributions for that year.[30] Some of that amount would have been contributed even in the

[27] In Table 19 we see that 88 per cent of itemized contributions were deducted on tax returns reporting less than $50,000 income. Obviously a considerably larger percentage of total contributions must have been made by taxpayers with incomes below $50,000.

[28] On the basis of unpublished Treasury Department data for 1949 we estimated the amount of contributions itemized by taxpayers who gave in excess of 14 per cent of income at roughly $282 million in that year. If we assume all of them, in a momentary burst of generosity, had made full use of the additional 5 per cent allowance, we find that the itemized contributions would have risen by $107 million, or 5.3 per cent. Expressed as a per cent of estimated aggregate contributions (Table 16) the rise becomes even less significant, between 3.1 and 4.2 per cent.

[29] No data are available for 1951.

[30] Total contributions were estimated at $4.2 to $4.8 billion so that the amount in excess of 20 per cent came to about 1.5 per cent of the total (see Table 16).

absence of the more liberal allowance; for instance, $13 million of the total in excess of 20 per cent was reported on nontaxable returns. The effect of raising the ceiling from 20 to 30 per cent was thus slight.

While the increased maximum allowable deduction appears to have had a negligible effect on the aggregate flow of funds to philanthropy, it may have had significant effect on gifts to particular types of nonprofit activities. The changing composition of gifts with rising income is evident in percentages for American families showing the relative amounts contributed to religious and to other organizations (such as for welfare and education) by income groups (Table 23.)

According to the data from three surveys (see source note to table), philanthropic gifts reported by families and individuals with incomes up to $10,000 went primarily to religious bodies; only about one-fourth was given for other activities in 1950. In the same year, over one-half of the gifts by groups with incomes $10,000 and over was made for nonreligious purposes. Since the incidence of returns with deductions close to the 15 per cent deduction limit was greater in the higher income groups than in the lower, it is probable that the effect of raising the limit was greater for some types of philanthropy than one might surmise from the over-all figures alone.

How do the survey figures compare with the tax return data presented above (Table 19)? With the tax-return data cast into comparable income groups, the survey figures for contributions as per cent of income are somewhat lower than the tax return figures. The tax return figures are summarized below.

Net Income ($000's)	Per Cent of Adjusted Gross Income on Tax Returns[a] 1935	1936	1941	1950
0-2	2.2	2.2	2.5[b]	
2-3	1.7	1.8	1.9[b]	
3-5	1.6	1.7	1.9	[c]
5-10	1.7	1.6	2.2	
10 and over	2.3	2.2		
Total	2.0	1.9	2.1	2.4

[a] Fiduciary returns included in 1935 and 1936 figures; excluded from 1941 and 1950.

[b] Contributions estimated on basis of 1940 figures to include returns with standard deduction in 1941.

[c] Because of the standard deduction no estimates by income groups for all returns were attempted. A contribution rate of 1.65 per cent was attributed to returns with the standard deduction on the assumption that the 1943 rate for such returns was applicable in 1950.

TABLE 23

Survey Data on Philanthropic Gifts of Individuals by Income Groups and by Type of Gift, as Per Cent of Income, 1935-1936, 1941, and 1950

	1935-36 (families)			*1941 (families and single persons)*			*1950 (families and single persons–urban)*		
INCOME GROUP[a]	*Total*[b]	*Religious Organizations*	*Other*[c]	*Total*[b]	*Religious Organizations*	*Other*[c]	*Total*[b]	*Religious Organizations*	*Other*[c]
Under $2,000	1.1	1.0	0.1	1.5	1.3	0.2	2.0	1.5	0.4
2,000-3,000	1.4	1.2	0.2	1.4	1.1	0.3	1.6	1.3	0.3
3,000-5,000	1.7	1.4	0.3	1.6	1.3	0.4	1.6	1.2	0.4
5,000-10,000	1.8	1.3	0.5	2.4	1.2	1.1	1.8	1.2	0.6
10,000 and over	0.9	0.5	0.4				2.9	1.2	1.7
Total	1.3	1.0	0.2	1.7	1.2	0.5	1.8	1.2	0.6

[a] For 1935-1936, aggregate income (that is, money and non-money); for 1941, money income; for 1950, income groups for net money income after tax, with percentages shown for net money income before tax.

[b] Figures in following two columns may not add to correct total because of rounding.

[c] Other contributions include gifts to community chests and other community projects; to Red Cross, USO, and other American and foreign welfare and relief agencies; and to scholarship, memorial, and alumni funds of schools and colleges.

Source: *1935-1936*: National Resources Committee, *Consumer Expenditures in the United States, 1935-36*, Washington, 1939, Tables 24A and 27A.

1941: Bureau of Labor Statistics, *Family Spending and Saving in Wartime*, Bulletin No. 822, 1945, Tables 1, 3, and 12. Average income of those with money incomes over $5,000 was obtained from the earlier tabulation in the BLS *Spending and Saving of the Nation's Families in Wartime*, Bulletin No. 723, Washington, 1942, Table 7. Contributions for that group were obtained as a residual after assuming that average contributions of those with negative income were the same as the average for units with 0 to $500 incomes.

1950: Wharton School of Finance and Commerce, *Study of Consumer Expenditures, Incomes, and Savings*, Vol. XI, University of Pennsylvania, 1956. The sample distributions of families by income groups for nine classes of cities were blown up to correspond to the estimated total urban population in the nine classes of cities, as given on p. XIII.

For 1935-1936, the results are as expected. The survey income concept, which includes nonmoney income, is more inclusive than the tax return concept. The omission of single persons from the 1935-1936 survey figures also affects comparability, although possibly in the opposite direction. The 1941 and 1950 survey figures are for money incomes reported by families and single consumers and are therefore more, though not entirely, comparable to the tax return figures. Both sets of ratios show only moderate variation in the percentage of income given to philanthropy over the income range shown. The survey figures indicate a tendency toward rising contribution ratios with rising income (except for the over $10,000 group in the 1935-1936 survey), which is not present in the 1935-1936 and 1941 tax return figures. The latter suggest a much higher contribution ratio for low incomes than the surveys do, which may account for the higher over-all contribution rate obtained from tax returns.[31] The 1941 survey figures suggest consumers contributed 1.7 per cent of their incomes, whereas the tax returns show a 2.1 per cent rate of giving. For 1950 the respective percentages are 1.8 and 2.4, but the tax return figure for that year is, as has been explained previously, merely an estimate.

Rate Progression and the Cost of Giving

As we have seen, the rate of philanthropic giving reported on tax returns rises with the income scale. Can this be partly attributed to government's increasing share in the cost of donations as incomes rise? At the tax rates prevailing in recent years, the government's share in the deductible donations of a taxpayer may rise from one-fifth to nine-tenths at the top of the income scale. It is dependent on the highest bracket rate to which a taxpayer is subject, the net cost of a given contribution therefore diminishing as taxable income and the marginal rate of tax increase. Though it might seem that the incentive to make use of the contribution allowance among taxpayers would be greater, the higher the rate of tax, it is also frequently shown that decreases in disposable income by high rates of taxation tend to be an influence in the opposite direction; high taxes, it is said, reduce both desire and ability to contribute to philanthropy.[32] The former may be

[31] For further comment on the tax return and survey figures, see the last pages of Appendix F.

[32] This is the position taken by Harris (*op.cit.*, p. 124, and pp. 32-33). Speaking of the rise in taxes over the last half century, he concludes: ". . . contributions to charity or education are affected adversely; and this is true even if it is allowed

considered the price effect of the income tax on philanthropic gifts; the latter the income effect.

On a priori grounds one might conclude that the price effect of the deduction outweighs the restrictive effect of taxes on disposable income. The reasoning would be that the cost of contributions to the taxpayer is reduced at his highest marginal rate, whereas his income is reduced by his average effective rate of tax. The marginal rate almost always exceeds a taxpayer's effective rate, and the reduction of the cost to him of his contributions is therefore relatively greater than the reduction of his income. It follows that the after-tax ratio of contributions to income is lower than the ratio before taxes.

Table 24 shows the net cost of contributions relative to net income after tax, for selected amounts of income with 1937, 1945, and 1952 tax rates. A hypothetical contribution deduction of 5 per cent of net income was used at each income level to facilitate comparison of the after-tax percentages. The so-called after-tax rate of giving tends to fall throughout most of the income range. Eventually, however, as the effective rate of tax catches up with the marginal rate (as the latter flattens out), the after-tax ratio of contributions to income rises, and at a very high level of income becomes equal to the before-tax ratio of gifts to income. At 1952 rates the hypothetical contributions of 5 per cent of income (before tax) resulted in a rate of 4.5 per cent of after-tax income for a married taxpayer with an ordinary income of $10,000; 2.9 per cent for a taxpayer with $100,000; but 4.7 per cent for one with as much as $1 million.[33]

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that the government through losses of taxes pays seven-eighths of the gift. With gross income cut by seven-eighths, potential donors prefer to hold on to what is left."

[33] For equivalent net incomes that include other than ordinary income, in particular capital gains, the ratios of net contributions to income after tax would often be different from those shown in Table 24. Let us assume, for example, two taxpayers, each with a statutory net income of $100,000, one of whom has $30,000 net realized capital gains taxable at the alternative rate. If both contribute 5 per cent of statutory net income, we find that for 1952 the first taxpayer contributes 2.9 per cent on an after-tax basis and the second 2.7 per cent. For 1945, the positions are reversed. The taxpayer with only ordinary income has a 1.6 per cent after-tax ratio, and the one with a realized capital gain contributes 2.3 per cent after tax.

The validity of the above treatment of the capital gains is somewhat questionable. It might be argued that the percentage for the capital gains taxpayer in our example should be compared with that of a taxpayer with $130,000 ordinary net income since under the tax law statutory net income includes only one-half of the capital gains realized. This, however, would require a different interpretation of the nature of capital gains from that implied in both the tax laws and the adjusted gross income concept underlying most of the statistics in this study.

TABLE 24

Net Cost of Hypothetical Contributions in Relation to Ordinary Net Income After Tax, at Selected Income Levels, 1937, 1945, and 1952

NET INCOME (*$000's*) (1)	*Contributions* (1)×.05 (2)	*Effective Rate* (*per cent*) (3)	*Marginal Rate* (*per cent*) (4)	*Net Income After Tax* (1)—[(1)×(3)] (5)	*Net Cost of Contribution* (2)—[(2)×(4)] (6)	*Net Cost of Contribution as % of Net Income After Tax* (6)÷(5) (7)
			1937[a]			
3	$ 150	0.3	4.0	$ 2,991	$ 144	4.81
5	250	1.6	4.0	4,920	240	4.88
10	500	4.2	9.0	9,580	455	4.75
25	1,250	10.0	21.0	22,500	987	4.39
50	2,500	17.7	31.0	41,150	1,725	4.19
100	5,000	32.5	59.0	67,500	2,050	3.04
500	25,000	60.8	72.0	196,000	7,000	3.57
1,000	50,000	67.9	76.0	321,000	12,000	3.74
			1945[a]			
3	150	15.8	23.0	2,526	116	4.59
5	250	19.5	25.0	4,025	188	4.67
10	500	25.9	37.0	7,410	315	4.25
25	1,250	41.2	62.0	14,700	475	3.23
50	2,500	55.2	75.0	22,400	625	2.79
100	5,000	69.4	90.0	30,600	500	1.63
500	25,000	88.8	94.0	56,000	2,000	3.57
1,000	50,000	90.0[b]	90.0	100,000	5,000	5.00
			1952[a]			
3	150	13.3	22.2	2,601	117	4.50
5	250	16.9	22.2	4,155	194	4.67
10	500	21.0	29.0	7,900	355	4.49
25	1,250	30.0	42.0	17,500	725	4.14
50	2,500	43.8	66.0	28,100	850	3.02
100	5,000	56.9	75.0	43,100	1,250	2.90
500	25,000	82.5	92.0	87,500	2,000	2.29
1,000	50,000	87.2	88.0	128,000	6,000	4.69

[a] Computations are for a married couple with an exemption of $2,500 in 1937, $1,000 in 1945, and $1,200 in 1952.

[b] Takes account of maximum effective rate limitation of 90 per cent in 1945.

The results of adjusting the actual contribution-income ratios for each income group (as given in Table 19) for the impact of the tax on both contributions and income are shown, for selected years in Table 25. For the previous hypothetical example, the curve now becomes nearly flat. Whereas the before-tax contributions ratio for 1937 rose from 2.2 to 6.4 per cent (Table 19), the after-tax percentage rose from 2.1 to only 3.5. For 1941 and 1943 the before-tax contribution ratio rose from about 2.4 to 5 per cent, but after tax there was a faint rise from 2.2 to 2.6 for 1941, and an actual decline from 2.3 to 1.3 for 1943. For the years after 1943 shown in the table, the data are for returns with itemized deductions only; this impairs comparisons with earlier years, particularly for returns below $25,000. In comparisons

TABLE 25

Net Cost of Actual Contributions as Per Cent of Income After Tax, by Income Groups, Selected Years, 1937-1956

ADJUSTED GROSS INCOME				*Itemized Returns Only*				
($000's)	*1937*	*1941*	*1943*	*1945*	*1947*	*1949*	*1952*[a]	*1956*[a]
Under 2	2.1	2.2[b]	2.3[b]	4.3	4.8	5.1	5.2	5.2
2-3	1.7	1.8[b]	1.8[b]	3.5	4.2	4.5	4.6	4.4
3-5	1.6	1.7	1.9	3.6	3.9	3.8	3.8	3.7
5-10	1.6	1.7	1.8	3.3	3.5	3.6	3.3	3.1
10-25[c]	1.6	1.5	1.5	2.3	2.5	3.2	3.0	2.9
25-50[c]	1.7	1.4	1.2	1.7	1.9	2.3	2.0	2.0
50-100	1.9	1.6	1.1	1.6	1.9	2.2	1.6	2.1
100-500	2.2	2.1	1.0	0.9	1.6	2.5	1.2	2.1
500 and over	3.5	2.6	1.3	1.0	2.0	2.5	3.0	3.2

[a] Excludes fiduciary returns.
[b] For 1941 and 1943, the 1940 before-tax contribution rate was assumed to hold for returns with $3,000 or less, to avoid the distorting effect of the standard deduction.
[c] For 1952, the group limit is $20,000 instead of $25,000.

restricted to returns above that level, the before-tax ratio rose from 3.0 to 6.7 per cent, whereas the after-tax ratio for 1945 declined from 1.7 to 1 per cent. In 1947 and 1949, the before-tax percentages again more than doubled, whereas the after-tax ratio for 1947 rose faintly from 1.9 to 2, and for 1949 from 2.3 to 2.5 per cent. In the 1950's the picture changed considerably. For 1956, before adjustment for taxes, the rate of giving rose from 3 to 12 per cent; the after-tax rate of giving from 2 to 3 per cent.

Such comparisons make it evident that increased taxes need not discourage the maintenance of a given relationship between philanthropic contributions and income. On the contrary, they may be an influence toward larger contributions, as long as they are deductible from income for tax purposes. While no definite conclusion may be drawn from the data here examined, on why the very rich contribute larger proportions of income to philanthropy than those with low and modest incomes, the favorable outcome of the deduction privilege to high-income taxpayers may be a partial explanation. Apart from the tax incentive, however, the "rich" may find it easier to part with a given percentage of their income for philanthropic causes than the "poor." Custom, the pressure exerted by society, and emulative display may also be of some importance.[34] The unequal tax benefit derived by deduction of an equivalent gift from taxable income by taxpayers in different income groups has many critics. One frequently suggested alternative is a tax credit, by which a fraction of contributions made could be credited against tax liability.[35] Some implications for policy of this proposal is the subject of the next section.

The Tax Credit as an Alternative Treatment of Contributions

A credit against tax is in principle the method used in Great Britain since 1946. Through it, the government's participation in a taxpayer's charitable gifts becomes equal to the standard rate of tax on an equivalent amount of his income.[36] A deduction in form of a tax credit is

[34] As far back as 1842, an Englishman travelling in the United States was struck by the extent of private finance for public purposes. "Munificent bequests and donations for public purposes, whether charitable or educational, form a striking feature in the modern history of the United States. . . . Not only is it common for rich capitalists to leave by will a portion of their fortune towards the endowment of national institutions, but individuals during their lifetime make magnificent grants of money for the same objects." Charles Lyell, *Travels in North America*, Vol. I, London, 1845, pp. 263-264.

[35] See, for instance, The President's Committee on Education Beyond the High School, *Second Report to the President*, July 1957, p. 90; Paul E. Klopsteg, "How Shall We Pay for Research and Education?" *Science*, November 16, 1956; Melvin I. White, "Deductions for Nonbusiness Expenses and an Economic Concept of Net Income," *Federal Tax Policy for Economic Growth and Stability*, Joint Committee on the Economic Report, 84th Cong., 1st Sess., 1955, p. 364; and William Vickrey, *Agenda for Progressive Taxation*, pp. 130-131.

[36] A taxpayer pays only the net sum of his contribution to a given recipient, which recovers from the Treasury, under the withholding-at-the-source system, the tax paid at the standard rate on an amount equivalent to the gross contribution. In recent times the standard rate has been 42.5 per cent, graduated by a system of so-called reliefs from the standard rate, by which a lower rate is levied on the first £360 of taxable income. The lower rate of tax for low-income taxpayers results in a lower rate of matching gifts by the government. More important to the low-income donor is the provision that a gift to be recognized as tax exempt must be made under a deed committing the taxpayer to a specified sum annually for not less than seven years. Among the effects of that provision is a probable bias of the tax deduction in favor of high-income taxpayers, whose gifts are subject to the full standard rate. The British Exchequer thus virtually matches the gifts to qualified philanthropies when made under the required deeds. For detail, see *Royal Commission on the Taxation of Profits and Income, Final Report* (Cmd. 9474), London, Her Majesty's Stationary Office, 1955, Chapter 7.

said to have two merits: (1) the relative amount of governmental participation in all gifts is the same, except where the possible amount of tax subsidy exceeds the initial amount of tax liability; and (2) it would be simple to procure the desired level of government participation, consistent with revenue requirements, by varying the rate at which taxpayers may credit their contributions against tax liability.

The tax credit accords with the reasoning that an allowance for philanthropic contributions is a deliberate instrument of public policy to encourage decentralized decision making in the allocation and administration of funds in areas commanding the public interest. In this view, the contribution allowance is not an appropriate adjustment for the determination of net income. It would be justified only if a relation between the deduction and the refinement of gross income to taxable income could be shown, and then there would presumably be little reason to limit the amounts deductible as under the federal tax.

The desirable form, if any, of a deduction depends ultimately upon acceptance of a rationale supporting the deduction. Two possible foundations, discussed previously, are: that the deduction is intended to assist by tax relief in the financing of activities in the public interest; and that its purpose is to refine income, as implied by current practice. The first interprets the deduction as an application of income, rather than as a reduction of income for tax purposes; the second interprets the deduction as a means of obtaining the best possible index of ability to pay—net taxable income. On the second premise, the argument that the cost of the gift dollar is less for the rich than the poor has little merit. The unequal tax value of the present deduction to individuals in different income classes results from the decision of Congress to impose graduated tax rates and to exclude eligible contributions from taxable income. There is nothing inherently unreasonable in this decision. The appropriate form for the allowance depends on whether Congress intended it as an indirect subsidy, or as part of the calculation of taxable net income. Arguments have been presented in favor of both views.[37]

[37] R. M. Haig wrote of the dual provision for contributions as deductible for the donor and tax exempt for the recipient that "on the ground of public policy much can be said for continuing this practice although it is also true that, speaking in terms of economic fundamentals, the man who makes a gift to some person or corporation outside his immediate family deliberately chooses that way of spending his money because it yields him a greater satisfaction than some alternative use" ("The Concept of Income," p. 26). Henry C. Simons held that "if it is not more pleasant to give than to receive one may still hesitate to assert that giving is not a

Whether the revenue cost of obtaining a given volume of contributions with a tax credit would differ from the present income deduction depends on the credit required, that is, the sensitivity of giving to tax rebates. Supposing a flat credit of 30 per cent of eligible contributions against tax liability, many taxpayers would get an increased tax abatement while a few would take drastic reductions. This might lead to a shift in the source of funds for philanthropic purposes toward the middle and low income groups, and possibly—as some authors put it[38]—a more democratic distribution of control over philanthropic institutions. It might lead also to some changes in the composition of major types of recipient institutions. If, at some time, a higher level of contributions to philanthropies should be desired, the tax credit device could easily be adapted. For instance, taxpayers might be granted a higher fractional credit allowance on contributions exceeding a given per cent of income; this method might be more effective than the recent increases in the deduction limit. The second merit claimed for the tax

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form of consumption for the giver. The proposition that everyone tries to allocate his consumption expenditure among different goods in such manner as to equalize the utility of dollars-worths may not be highly illuminating; but there is no apparent reason for treating gifts as an exception" (*Personal Income Taxation*, pp. 57-58). Similarly, White says (*op.cit.*, p. 364): "A charitable or other such contribution by an individual is a voluntary allocation of funds, presumably more gratifying than expenditure on goods and services. Its deduction is thus not an appropriate adjustment for the calculation of net income." Sylvester Gates and John R. Hicks (a minority opinion in the recent *Final Report of the Royal Commission on the Taxation of Profits and Income*, London, 1955, p. 352) state: "We cannot find any principle to justify the total exemption of charities from income tax, except in those cases where a charity performs functions which are a well-recognized responsibility of the state."

The majority of the Commission ended up on the opposite side of the dividing line: "A charitable contribution does not appear to us to be well compared with personal expenditure or investment of income. It is more truly an act by which a man surrenders his personal decision as to the employment of that part of his income in favour of the decision of the managers of the charity. In a real sense his income is transformed into income of the charity." This reasoning forced the majority to conclude, with much hesitation and ambiguity, that an allowance against taxable income, as practiced in the United States and Canada, rather than the British tax credit, would be in order. But the Commission seemed noticeably relieved at rejecting the recommendation on "practical and administrative" grounds (*ibid.*, p. 59). The idea that contributions properly constitute diminutions of income was widely held at the time the deduction was introduced into the federal tax law. A comment inserted into the *Congressional Record* in 1917 declared: "By means of this exemption contributions to recognized religious, charitable, and educational institutions are put on the same basis as the loss of money in business, or the payment of money in taxes. Since the taxpayer, or the bad investor, or the donor does not have the use of the money, he is not asked to pay the income tax on it" (65th Cong., 1st Sess., p. 6729).

[38] White, *op.cit.*, pp. 364-365; Klopsteg, *op.cit.*, p. 968; Vickrey, *op.cit.*, p. 131.

credit is that it gives the government freedom to review periodically its own position in underwriting philanthropic gifts.[39] Only partial review is possible at present, for under the deduction-from-income provision, governmental participation is tied to the existing rate structure and therefore difficult to control. Some students in the field, however, consider frequent legislative review a distinct disadvantage, especially of a field—education, for example—that invites strong feelings against governmental interference, even though it receives some indirect public assistance. Lack of such review appears to be a point in favor of the present form of deduction from income over the tax credit.[40]

With a tax credit even the rate of benefit to different types of philanthropy could be varied at the will of Congress, and to some extent this is attempted under the federal law now. At present philanthropy encompasses a wide variety of activities and enterprises, some of which may be considered public service programs, while others affect the public interest only remotely. In both cases there occurs a redistribution of the tax load whenever deductions are taken. But when the benefited philanthropies perform functions which would alternatively be governmental, the deductible donations may be thought akin to taxes, and the taxpayer's share in the contribution dollar the price he pays for retaining some control over its allocation to projects and institutions of his choice. With smaller private contributions, the government's responsibility for the functions would increase, tax collections would have to be higher, and those who give little or nothing might have to assume more of the tax load.[41]

39 Review and control of the government's action appears to have greatly concerned both the minority and the majority of the Royal Commission on the Taxation of Profits and Income. Gates and Hicks characterized the system of exempting all charities as a "blind and hidden subsidy contributed by the state [which] is never investigated or weighed" (*op.cit.*, p. 352). The majority was vexed over the lack of "public control of the object of a charity from the point of view either of importance or utility" (*op.cit.*, pp. 55, 56).

40 This is implicit in the conclusions drawn by J. Harold Goldthorpe, in a study sponsored by the American Council on Education. He writes that "these subsidy exemptions . . . to the institutions of higher education . . . are highly desirable for the following reasons . . . (2) such indirect grants are commonly provided by government without the intrusion of undesirable and insignificant governmental controls: (3) they are a continuing type of indirect aid and do not require periodic legislative review and action. . . ." *Higher Education, Philanthropy, and Federal Tax Exemptions*, 1944, p. 32.

41 Were the deduction privilege removed, the government's additional financial responsibilities would not necessarily exceed the added revenue accruing from the taxation of previously untaxed income. Nondonors might have no increased liability. Only a shrinking of gifts by more than the increase in tax liability might make

an increase in rates necessary for all taxpayers. Conversely, if donors reduce their gifts by less than the increase in their tax, there might even be a rate reduction and an absolute cut for nondonors.

This subject was explored earlier in discussing the severance of the connection between giving and the tax rebate for many taxpayers when the standard deduction was introduced into the tax system. It will be recalled that we found no evidence that philanthropic giving declined in the wake of the standard deduction.