

# Gilded Giving 2022

How Wealth Inequality Distorts Philanthropy  
and Imperils Democracy

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Charity Reform Initiative • Institute for Policy Studies

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The **IPS Charity Reform Program** (see: <https://inequality.org/action/charity-reform-initiative/>) was founded in 2020 to study the intersection of inequality and philanthropy. We house the Charity Data Lab and we have published numerous reports, including: *Gilded Giving 2016: Top Heavy Philanthropy in an Age of Extreme Inequality*, *Warehousing Wealth: Donor Advised Funds Sequestering Billions in the Face of Growing Inequality*, and *Gilded Giving 2020: How Wealth Inequality Distorts Philanthropy and Imperils Democracy*.

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# A Reckoning for the Charitable Sector

As inequality has grown in the U.S., the nation's charitable system is in danger of becoming a taxpayer-subsidized platform of private power for the ultra-wealthy. This poses risks to the independent nonprofit sector and our society as a whole.

In fact, concentrated private philanthropic power imperils democratic norms. When a small number of wealthy donors dominate charity, they usurp the public's power to define what problems are, which ones get addressed, and what their solutions should be. But as taxpayers, we subsidize the tax deductions taken by wealthy donors—giving us both the right and the responsibility to oversee and fix it.

Since our first edition of *Gilded Giving 2016: Top Heavy Philanthropy in Age of Extreme Inequality*, we have shown that charities are receiving shrinking amounts of revenue from donors at lower- and middle-income levels, and that they are more reliant on larger donations from smaller numbers of wealthy donors. And we have shown that wealthy donors tend to pour their dollars into foundations and donor-advised funds—charitable intermediary vehicles they control—rather than into public operating charities.<sup>1</sup>

Philanthropy is now more top-heavy than ever. Mega-philanthropists have intensified their influence over nonprofit giving with record-breaking splashes in the charitable world. The world's richest men—Jeff Bezos, Elon Musk, and Bill Gates—have all made multi-billion-dollar contributions to their own foundations and donor-advised funds, reducing their taxes by millions of dollars with charitable tax breaks. Meanwhile, the share of regular Americans who give has steadily continued to fall.

On top of all of this, the nonprofit sector has had to cope with two years of global pandemic, four years under a new tax law that discourages charitable giving, and many years of growth in for-profit investment options that further erode the tax advantages charities offer.

If we continue on our current trajectory, our charitable sector will be more and more dominated by large legacy foundations and donor-advised funds while working charities face greater fiscal austerity. An ever-greater share of charitable dollars will be diverted into wealth warehousing vehicles rather than going to nonprofits serving critical needs. Wealthy donors will increasingly be able to use their charitable giving to opt out of paying their fair share in taxes to support the public infrastructure we all rely on. And they will increasingly be able to deploy philanthropy to advance their narrow self-interests.

U.S. charities face a reckoning. Without intervention, ultra-wealthy philanthropists will continue to divert more and more charity dollars from operating nonprofits, and will rival state and local governments in their ability to shape public policy in their interest. We must take immediate action to remedy this before the independent sector loses its independence.

And the public agrees. According to a new Ipsos poll, 81 percent of Americans do not believe that taxpayers should subsidize the wealthy to create perpetual private foundations. And the overwhelming majority also want private foundations and donor-advised funds to pay out funds to charity much faster than they currently do.<sup>2</sup>

This updated edition of *Gilded Giving* describes the extent of the capture of our charitable sector by the wealthy, the risks this poses, and how it has been exacerbated by the pandemic and other external factors. We also propose a large set of strong reforms that would reverse these trends and realign our charitable system to serve the public interest.

## Key Findings

- **Fewer than half of all U.S. households now give to charity.** Over the past two decades, the share of households that donate has declined significantly. From 2000 to 2018, the most recent data available, the proportion of households giving to charity has dropped from 66 percent to just under 50 percent.<sup>3</sup> These declines track indicators of economic insecurity such as employment, wages, and homeownership rates.
- **The share of households that claim charitable deductions fell significantly after sweeping tax reform in 2017.** Following the passage of the Tax Cuts and Jobs Act, the proportion of taxpayers who itemized their charitable giving fell from 25 percent in 2017 to just 10 percent after the bill took effect in 2018. And the effect stuck: just 9 percent of households claimed charitable deductions on their returns in 2019. These changes most affected middle-income households earning \$50,000 to \$400,000 per year.<sup>4</sup>
- **Top heavy philanthropy worsens.** The proportion of charitable contributions coming from donors at the top of the income and wealth ladder has increased significantly over the past three decades. In the early 1990s, households earning \$200,000 or more accounted for less than 25 percent of all charitable deductions. By 2019, the most recent year available, this group accounted for 67 percent.<sup>5</sup> The share of charitable deductions claimed by those at the top of the income scale has grown particularly quickly: households making over one million dollars accounted for just 10 percent of charitable deductions in 1993, but accounted for 40 percent in 2019.
- **Mega-giving is booming.** The data analysts behind *Giving USA*, the gold standard of reporting on nationwide charitable giving, define a mega-gift as one that is large enough to require a manual adjustment to their estimate models. That threshold has been increasing rapidly as ultra-wealthy donors dole out ever-greater gifts. In 2011, *Giving USA*'s threshold for mega-gifts was just \$30 million, and gifts of that size or larger amounted to \$2.7 billion.<sup>6</sup> By 2021, just ten years later, the mega-gift threshold had jumped to \$450 million, and gifts of that size or larger added up to nearly \$14.9 billion.<sup>7</sup>

- **The top two charitable causes of ultra-wealthy donors are their own private foundations and donor-advised funds.** In early 2022, the *Chronicle of Philanthropy* published its annual list of the top fifty philanthropists in the U.S.<sup>8</sup> Of the \$25 billion in identifiable gifts that the group donated in 2021, 69 percent of it—more than \$17 billion—went to private foundations. The second-largest chunk, more than \$2.6 billion, went to donor-advised funds. Both of these intermediary giving vehicles are favored by wealthy donors because of the significant tax advantages they offer. But funds may or may not flow from them to active charities in a timely way; there is no guarantee that they will fulfill the public interest.
- **Contributions to donor-advised funds are skyrocketing.** Donor-advised funds, or DAFs, have been the fastest-growing recipients of charitable dollars in the U.S. in recent decades. In 2020, for the first time, donations to DAFs caught up with contributions to private foundations; both received roughly \$48 billion from donors that year. The largest single recipient of charitable giving in the U.S. for the past six years has been the Fidelity Charitable Gift Fund—a commercial DAF sponsor.<sup>9</sup> And, for the past three years, six of the top ten charities have been DAF sponsors.<sup>10</sup>
- **Gifts to private foundations and donor-advised funds now divert nearly a third of charitable giving in the U.S.** Giving to private foundations has increased from 6 percent to 15 percent of all charitable giving since 1992.<sup>11</sup> And giving to DAFs has increased from 4 percent to 15 percent of all charitable giving since 2007.<sup>12</sup> Together, these charitable intermediaries now soak up 30 percent of all U.S. donations—more than quintupling their share of the charitable pie in less than thirty years.

## Key Recommendations

We urgently need to overhaul the rules governing philanthropy to discourage the warehousing of charitable wealth, to align tax incentives with the public interest, and to encourage broad-based giving across all segments of society. The Fixing Philanthropy section of this report contains a large menu of steps we can take to fix the system. Below are some of the most critical.

Among other benefits, implementing these reforms would result in a significant amount of additional revenue flowing to working charities. We estimate, for example, that if foundations had a 10 percent minimum payout and DAFs had a three-year mandated payout between 2018 and 2020, at least \$193 billion in additional donations would have flowed to nonprofits.

### Reforms to Donor-Advised Funds

**Require donor-advised funds to have a payout.** We should require that DAFs pay out the entirety of any donations within three years after donations have gone into the fund, including any income earned on the donations during that time.

**Limit tax deductions for donations of complex assets to their sale value.** To prevent inappropriately-inflated charitable deductions, we should base the deductions for donations of complex, non-cash appreciated property such as artwork, real estate, and cryptocurrency on their actual sale value, rather than their assessed value, and should delay that deduction until the year the property is sold.

**Increase DAF transparency and reporting.** Donations to and from DAFs should be publicly disclosed and reported on an account-by-account basis. This could be done in such a way as to protect anonymous givers.

## Reforms to Private Foundations

**Increase the annual foundation payout requirement.** We propose increasing the requirement to 10 percent of assets.

**Reform foundation payout exclusions.** We should exclude both administrative overhead and grants to donor-advised funds from counting towards the foundation's minimum payout requirement.

## Reforms to Encourage Broad-Based Giving

**Replace the itemized charitable deduction with a universal charitable tax deduction.** We should implement a universal tax deduction for any households—not just those that itemize—that give more than 2 percent of their adjusted gross income to charity.

## Reforms to Reverse Top-Heavy Philanthropy

**Establish a lifetime cap on charitable gift deductions.** To prevent donors from using charitable giving to reduce their taxes to zero indefinitely, we should implement a lifetime cap of \$500 million on charitable tax deductions.

**Establish a cap on the charitable estate tax deduction.** There is currently no limit on the amount of money that a person can pass tax-free to charity in their estate. To ensure that every person contributes to the costs of government, we should limit the estate tax charitable deduction to 50 percent of a donor's estate.

**Levy a wealth tax on donor-advised funds and closely-held private foundations.** We should implement an annual wealth tax of 2 percent on assets over \$50 million that applies to donor-advised funds and to private foundations that are managed by founders or their family members.

# Philanthropy Is More Top-Heavy Than Ever

Over the past two decades, philanthropy has become more and more unbalanced. Fewer people at lower and middle-income levels are giving to charity, so nonprofits are becoming increasingly dependent on donations from smaller numbers of extremely wealthy donors.

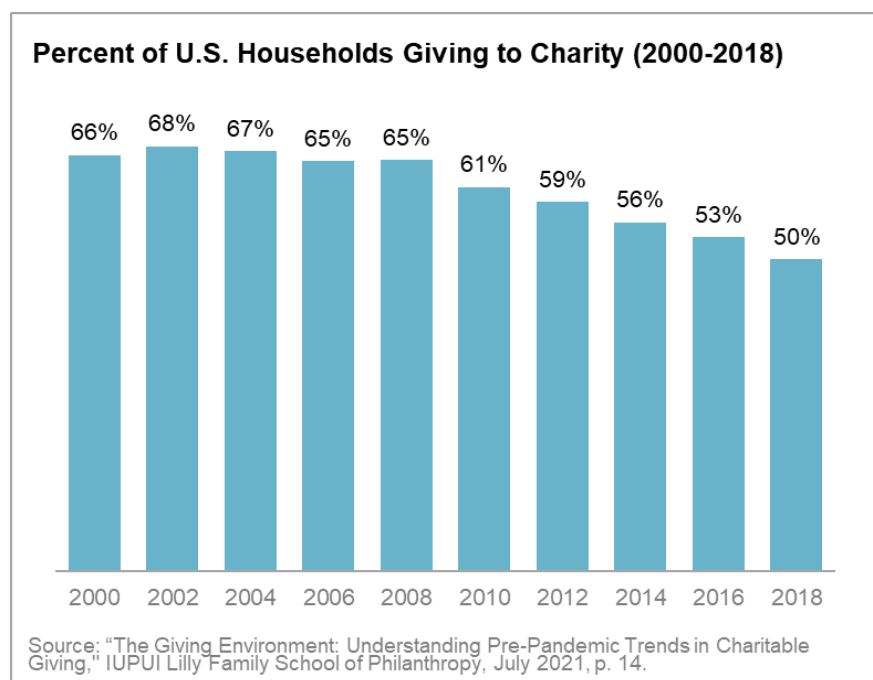
The two parts of this trend—declining giving by ordinary Americans and rapidly growing giving by those at the top—are a reflection of four decades of stagnant wages and a simultaneous tremendous updraft of wealth to the top one percent of households. We explore both of these parts in depth below.

## As Inequality Grows, Non-Wealthy People Give Less

### Fewer Americans are giving to charity

The share of households in the United States that give to charity has declined significantly over the past decade.

The latest results from the Lilly School of Philanthropy's Philanthropy Panel Study, or PPS, revealed that the percent of U.S. households giving to charity had slipped below 50 percent for the first time since the study began twenty years ago.<sup>13</sup>



The PPS, which is a part of the Panel Study of Income Dynamics at the University of Michigan, surveys the same set of more than 9,000 households every two years to learn about their giving behavior. According to the survey, in 2008, 65 percent of the households surveyed gave to



charity. In 2018, just ten years later, that had dropped to just under 50 percent. The declines in donor participation showed up consistently when controlling for all sociodemographic characteristics.<sup>14</sup>

The effect of these declines in donor populations is that individual donors are giving a smaller share of total charitable dollars as well. The Giving USA Foundation reported that more than thirty years ago, in 1991, individual giving accounted for 79 percent of all charitable revenue. But by 2021, donations by individuals accounted for just 67 percent of all charitable revenue, with a higher proportion coming from foundations, corporations, and bequests.<sup>15</sup>

### **Donor declines are greater for households at the lower end of the income ladder**

In 2017, the *Chronicle of Philanthropy* examined giving by households who itemized charitable deductions. According to their analysis, about 30 percent of all itemizing households had given to charity from 2000 to 2006, but that had declined to just 24 percent by 2015. At the time, the *Chronicle* wrote that this “suggests a narrowing of support in America for philanthropy. Whether running capital campaigns, annual-giving drives, or direct marketing efforts, nonprofits are relying on fewer, more affluent supporters.”<sup>16</sup>

Because of changes to charitable deductions in the 2017 Tax Cuts and Jobs Act<sup>17</sup>, we can no longer directly compare the numbers of itemizers and non-itemizers in 2018 and 2019 to previous years. But the Philanthropy Panel Study did find that income was still a significant factor in charitable giving after the tax bill passed. Almost 80 percent of households with more than \$200,000 of wealth gave to charity in 2018, the study said, but less than 40 percent of households with wealth less than \$50,000 made donations. As the *Chronicle* wrote in their reporting on the study, “donations to charitable causes are reaching record highs, but the giving is done by a smaller and smaller slice of the population.”<sup>18</sup>

Donors in higher tax brackets are more likely to itemize charitable deductions on their tax returns because they stand to benefit more from those deductions (in addition to other advantages they get for itemizing). In fact, research by the Giving Institute has found that the deductibility of charitable gifts is one of the greatest drivers of charitable giving each year.<sup>19</sup> So it stands to reason that high-income and high-net-worth individuals would tend to increase their giving to charity as their assets increase in value.

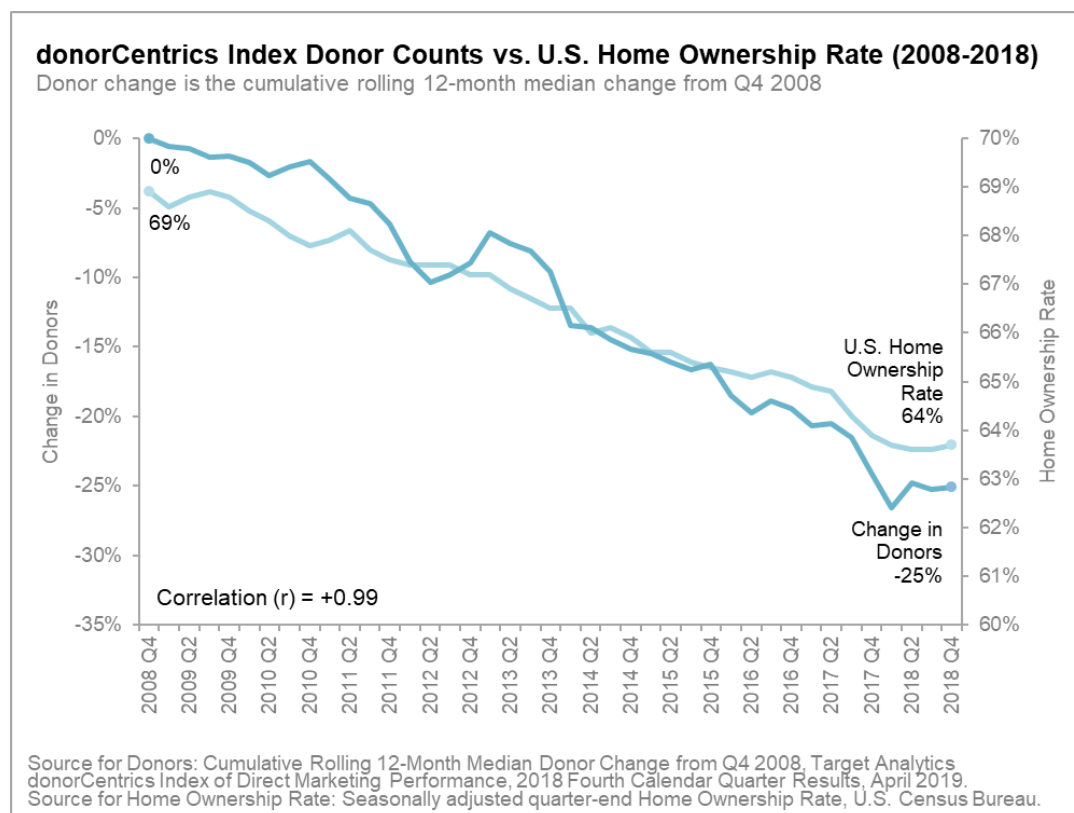
### **Donor declines are closely tied to rising economic insecurity**

Giving by everyday Americans has been declining for decades, reflecting the escalating wealth and income inequality in our society and the growing economic precariousness for those not at the top. As economic times get tougher for ordinary Americans, they can’t afford to give as much of their spending money to charity.

The Philanthropy Panel Study researchers acknowledged this in their latest analysis, writing that a good portion of the decline in giving participation they were seeing could be explained by “declines in income, wealth, and home values.” These factors explained 36 percent of the decline in overall giving and a full 44 percent of the declines in secular giving.<sup>20</sup>

In one of the only long-term, quantitative examinations of this relationship, Target Analytics compared the donor counts in their 2015 Index of Charitable Direct Marketing Performance against the U.S. labor force participation rate, and found that the two had an extremely close +0.80 degree of correlation. “While we do not have enough data to say that this is causative,” Target Analytics concluded, “these trends make intuitive sense; when people are not employed, they are likely to have less disposable income, and will not be as disposed to give to charity.”<sup>21</sup>

In our own analysis of later data, we found that Target Analytics’ donor declines correlated even more closely to another key indicator of economic security, the rate of home ownership; the two had a close-to-perfect 0.99 degree of correlation from 2009 to 2018. This is further evidence that harmful economic conditions undermine non-wealthy donors’ sense of financial security—and thereby their capacity and willingness to donate to charity.<sup>22</sup>



The Giving USA Foundation also confirms that there is a measurable correlation between charitable participation and societal economic health. They have reported for years that

personal disposable income is a “key determinant” of giving for households that do not itemize—households of the non-wealthy.<sup>23</sup>

In fact, individual giving has been remarkably consistent, hovering at roughly 2 percent of personal disposable income for more than fifty years. It goes slightly up when economic times are good, and slightly down when times are tough, but rarely strays from a narrow range between 1.8 and 2.2 percent.<sup>24</sup>

The most recent edition of *Giving USA*, the Foundation’s comprehensive annual report on U.S. charitable giving, reported that individual giving was just 1.77 percent of personal disposable income in 2021.<sup>25</sup> The last time it was lower than that was in 1995, when the U.S. economy was still feeling the effects of the 1990-1991 recession.

In other words, the average American gave a smaller chunk of their disposable income to charity in 2021 than they had in the previous twenty-six years.

### **Charities Are More Dependent on Wealthier Donors**

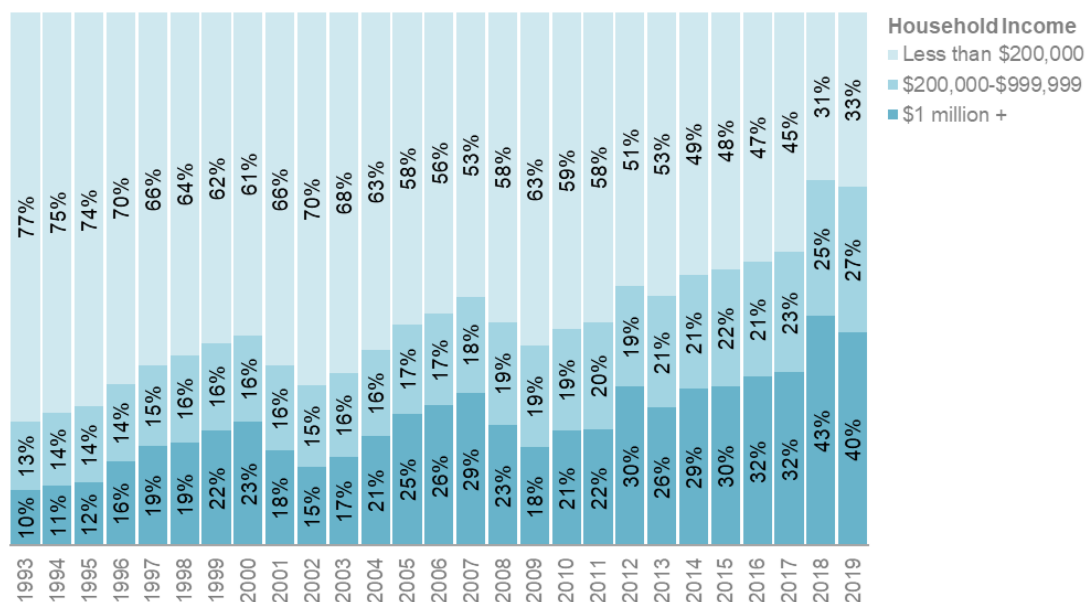
As charities face a loss of broad-based support, they rely more and more on smaller numbers of major donors to stay afloat. These major donors then gain increasing influence over charities’ activities and even their core missions. And this endangers not only the charities themselves, but also those who depend on their work.

According to IRS data, households earning \$200,000 or more accounted for just 23 percent of itemized contributions in 1993, but that share had grown to 67 percent by 2019, the most recent year available.<sup>26</sup> In 2018 and 2019, this shift was accelerated by changes to the deductibility of charitable gifts in the 2018 Tax Cuts and Jobs Act.<sup>27</sup>

Households at the very top of the income scale have been stepping up their use of the charitable deduction at an even faster rate than those of merely moderate wealth: the share of itemized contributions claimed by households with incomes over one million dollars increased from just 10 percent in 1993 to 40 percent in 2018.

In other words, the top 1 percent of income earners in the United States have rocketed from just one-tenth to two-thirds of all charitable deductions in just 26 years—allowing them to significantly reduce their tax obligations while giving them an even more outsized voice in what happens to our public charities.

**Percent of Charitable Deductions by Household Income Level (1993-2019)**



Source: IPS analysis of statistics from Internal Revenue Service SOI Tax Stats, Individual Statistical Tables by Size of Adjusted Gross Income, Table 2.1: Individual income Tax Returns with Itemized Deductions: Sources of Income, Adjustments, Itemized Deductions by Type, Exemptions, and Tax Items, for tax years 1998-2018

A new study by research firm Wealth-X on giving by ultra-high-net-worth donors bolsters this finding. According to the study, donors who are worth \$30 million or more gave \$85 billion to U.S. charities in 2020—more than a quarter of all individual giving in the country.<sup>28</sup>

## Skyrocketing Influence by Those at the Very Top

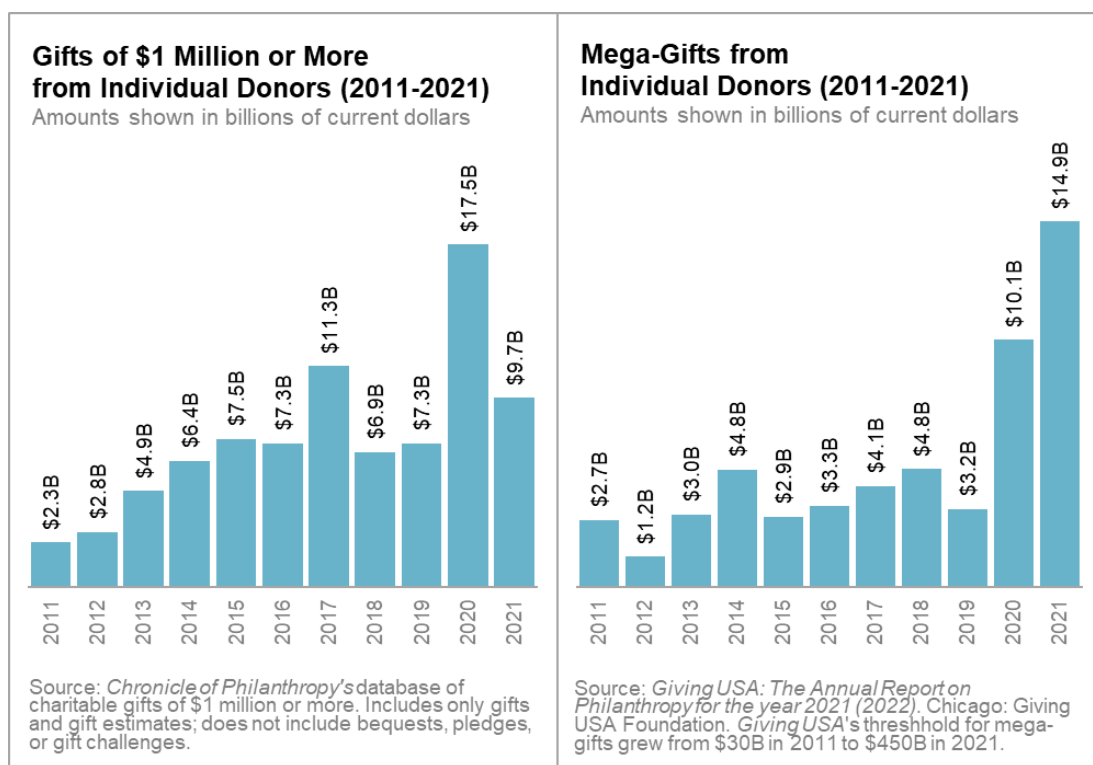
### Mega-giving is booming

Mega-donations create a big splash when they are bestowed on one or another lucky nonprofit. And mega-sized gifts to charity from some of the wealthiest among us have become more frequent in recent years. According to data from the *Chronicle of Philanthropy*, gifts of \$1 million or more from individuals added up to just \$2.3 billion in 2011, but that rose to almost \$10 billion in 2021, just ten years later.<sup>29</sup>

Ultra-enormous mega-gifts—which are gifts that *Giving USA* defines as those large enough to require a manual adjustment to their estimate models<sup>30</sup>—have grown even faster. In 2011, the threshold for mega-donations was \$30 million and mega-donors gave a total of just \$2.7 billion.<sup>31</sup> In 2021—again, just ten years later—the mega-gift threshold jumped to \$450 million, and mega-donors gave \$14.9 billion between them.<sup>32</sup>

Some of the record-breaking mega-gifts given just in 2021 include Tesla CEO Elon Musk’s \$5.7 billion gift to an undisclosed recipient, likely a donor-advised fund<sup>33</sup>; MacKenzie Scott’s \$2.7

billion in giving to various working charities, and Michael Bloomberg's \$1.7 billion in giving to his foundation and other nonprofits.<sup>34</sup>



## The Perils of Top-Heavy Philanthropy

Ideally, we would have a vibrant independent sector supported by a broad and diverse range of donors, so that no single benefactor has outsized power over what charities do with their donations. But when wealthy donors dominate the philanthropic sector, the dangers are manifold. Top-heavy philanthropy takes away the broader public's power to decide which problems to address, and how to address them. It siphons money away from working charities. And it allows some donors to abuse our publicly-financed charitable system for personal gain.

### Top-Heavy Philanthropy Means Charities Lose Out to Intermediaries

**Wealthy donors give far more to intermediaries than to working charities.**

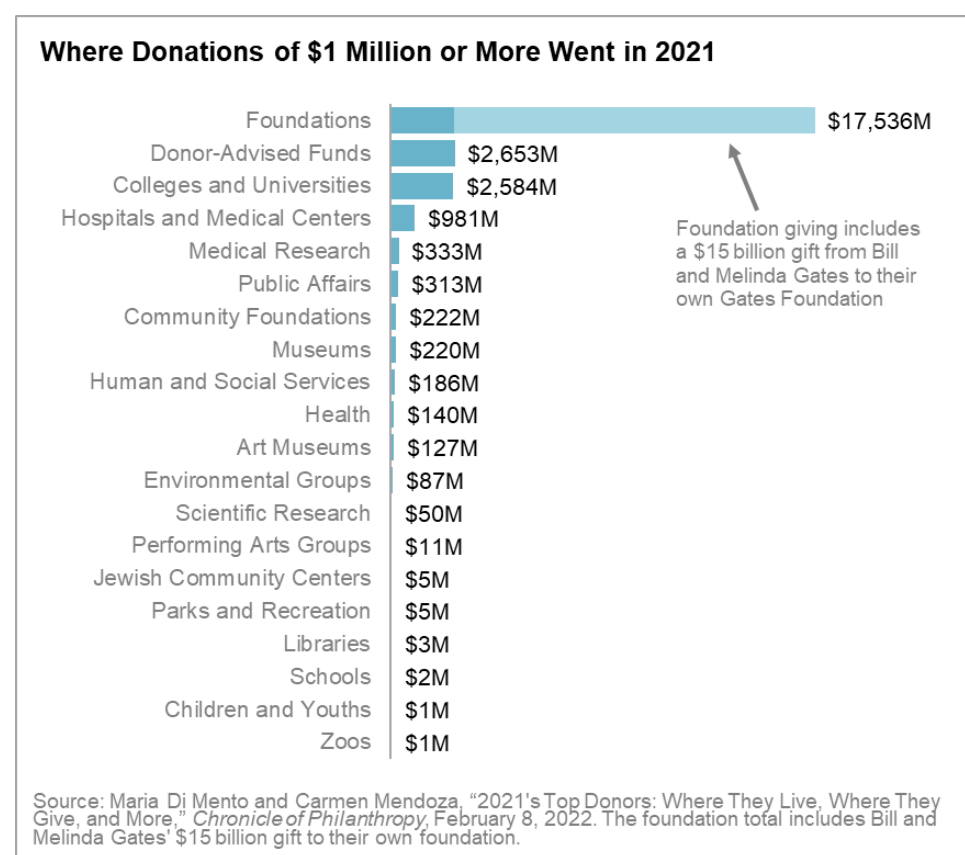
"Rich people give to causes that rich people want to give to," says University of Chicago economics professor John List. "You have a very different supply of goods and services from the charitable community when the rich people give versus when the middle-class or lower-class gives."<sup>35</sup>



List is entirely correct. More than anything, in fact, wealthy donors prefer to give not to active charities, but to intermediaries. For the past several years, the favorite cause of wealthy donors has been their own private foundations. And the second-favorite cause this year, leapfrogging over all other types of charities, are the donors' own donor-advised funds.

In early 2022, the *Chronicle of Philanthropy* updated its annual list of the fifty top philanthropists in the United States. Of the \$25 billion in identifiable gifts of over \$1 million that the group donated to charity in 2021, 79 percent of it—more than \$20 billion—went either to private foundations or to donor-advised funds.

Colleges and universities, the top category of working-charity recipients, received 10 percent of the total, and hospitals received 4 percent, leaving the remaining 7 percent to be distributed across all other types of nonprofits.<sup>36</sup>



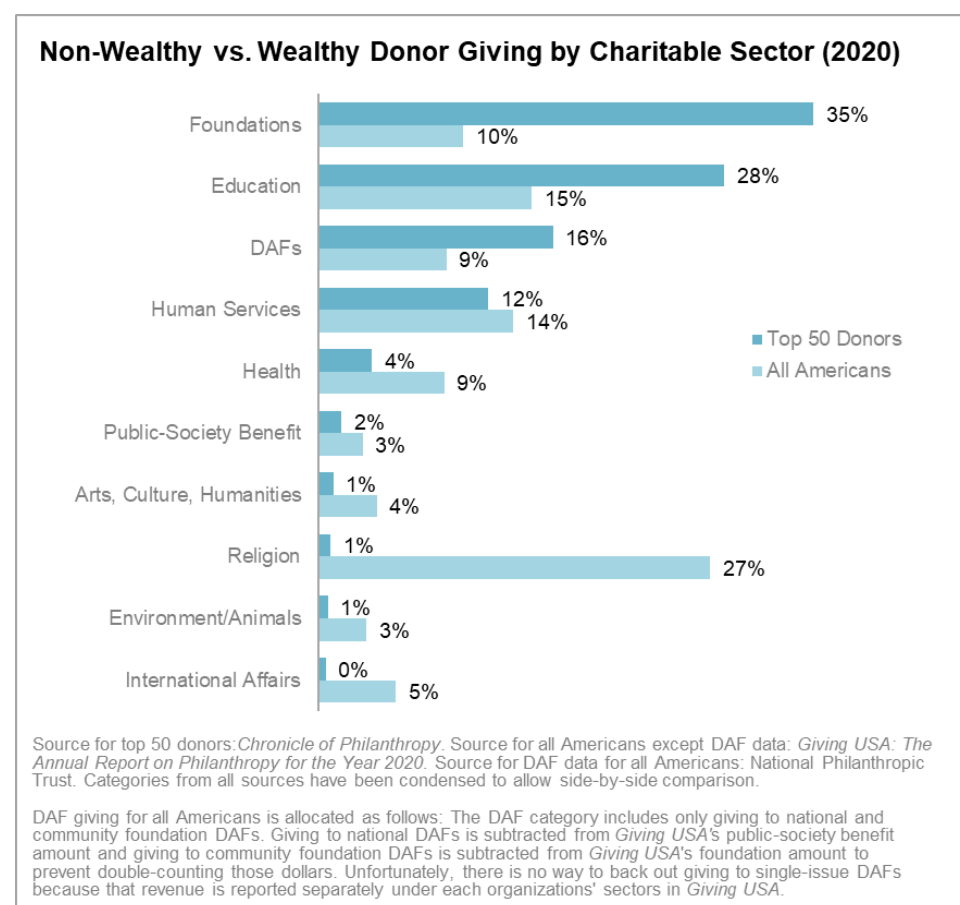
2021 could certainly be considered an atypical year for wealthy donor philanthropy, since it included Bill and Melinda Gates' \$15 billion gift to their own foundation.<sup>37</sup> But private foundations have ranked either first or, more rarely, second on the *Chronicle's* list of the wealthy's favorite charitable recipients for at least the past six years.

Higher education and hospitals have also consistently ranked as top causes among America's wealthiest donors, and donor-advised funds have been growing exponentially in recent years. In fact, if it had not been for the Gates' gigantic gift to their foundation, donor-advised funds would have broken into the top spot on the *Chronicle's* list for the first time in history.

**Even when the wealthy give directly, they choose different recipient causes than the rest of us.**

The giving priorities of the wealthy stand in stark contrast to those of everyday Americans. Wealthy donors' gifts tend to go disproportionately to institutions that can help them establish personal legacies—institutions such as colleges, universities, and medical centers—and less to the causes most of us choose to support.

We compared the giving of the *Chronicle of Philanthropy's* top 50 donors to that of all Americans as reported in *Giving USA*<sup>38</sup> and the National Philanthropic Trust's annual report on DAFs<sup>39</sup>, condensing some of the categories used by all sources so that they could be evaluated side by side. Because the most recent information from the National Philanthropic Trust is from 2020, all data in our analysis is for that year.<sup>40</sup>



In 2020, wealthy donors gave disproportionately more to private foundations, educational institutions—including colleges and universities—and donor-advised funds.

The typical American doesn't have access to a private foundation or donor-advised fund, so those options are off the table for most of us from the start. And when it comes to working charities, non-wealthy donors give less to education and more to almost all other types of causes—particularly religion, international affairs, and health care.

The causes chosen by the wealthiest in our society indicate a profound myopia about our most critical problems. As we observed about mega-donor philanthropy in 2021, “From this list, you would not know that we’re living through a global pandemic, and you would not know that as a society we’re grappling with racial inequity. This gift list is completely disconnected from the reality of our society right now.”<sup>41</sup>

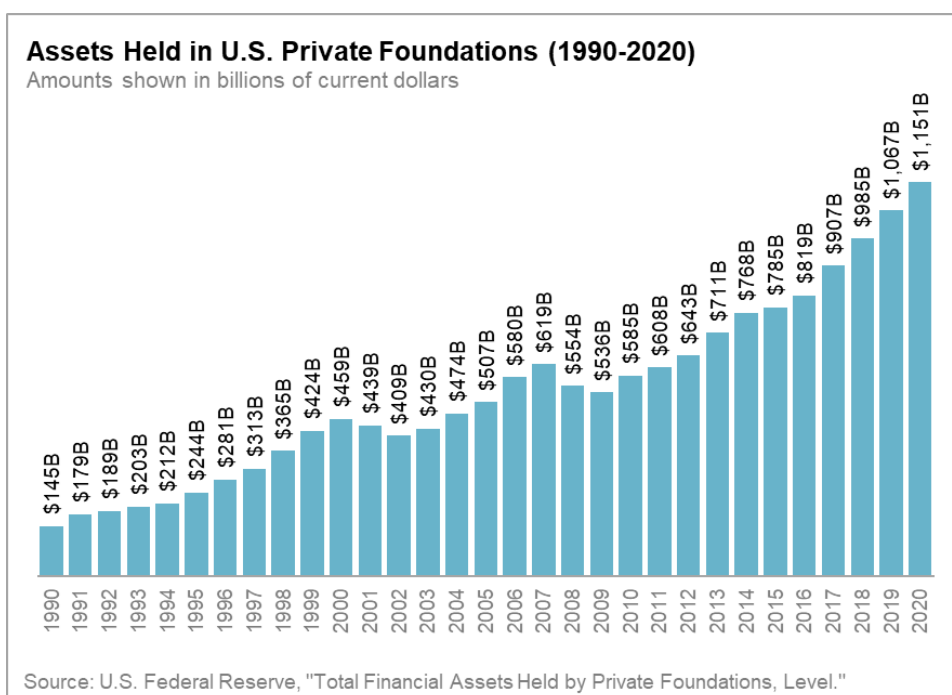
This is by necessity a broad back-of-the-envelope comparison. It would be difficult, for example, to parse out how much of the typical American's health care giving goes to cure-related charities that fundraise through mass-market solicitations, rather than the high-profile medical centers that receive mega-donations from the wealthy. It is also impossible to fully judge the scale of DAF giving for all Americans against other sectors because reporting on those vehicles is so opaque. But this analysis paints at least a rough picture of how the funding priorities of wealthy donors differ from those of the public at large.

### **The wealthy are pouring donations into private foundations.**

Private foundations are charitable giving vehicles that are generally available only to the affluent, since establishing and maintaining one usually requires a significant financial investment.<sup>42</sup> Over the past three decades, wealthy philanthropists have been directing more and more of their charitable giving towards foundations, creating them at a rapid clip and endowing them with increasingly large donations.

According to the U.S. Census and Candid, the number of foundations in the United States grew from 32,401 in 1990 to 127,595 in 2020—nearly tripling over thirty years.<sup>43,44</sup> The amount of assets held in those private foundations has increased more than twice as fast as their number, growing a whopping 693 percent from \$145 billion in 1990 to \$1.2 trillion over the same period.<sup>45</sup>

And, in spite of recent competition from DAFs, foundations are still proliferating impressively. The number of U.S. foundations grew by 67 percent over the past decade, from 76,545 in 2010 to 127,595 in 2020.<sup>46,47</sup>



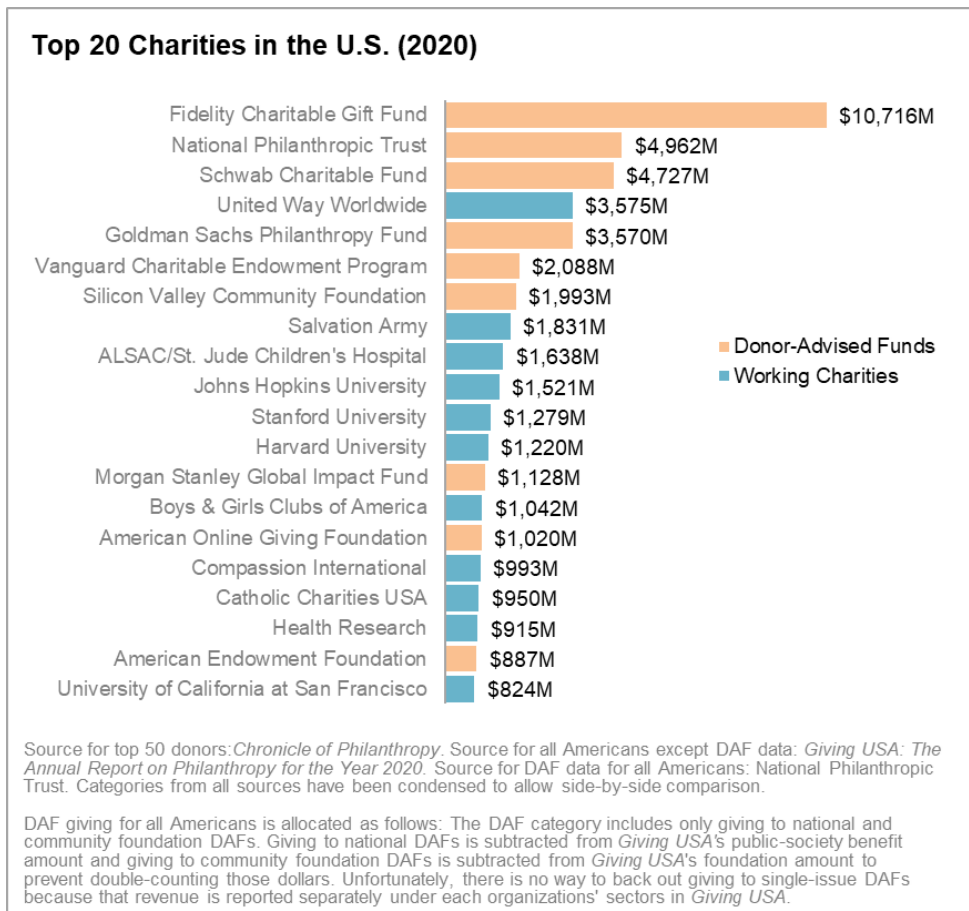
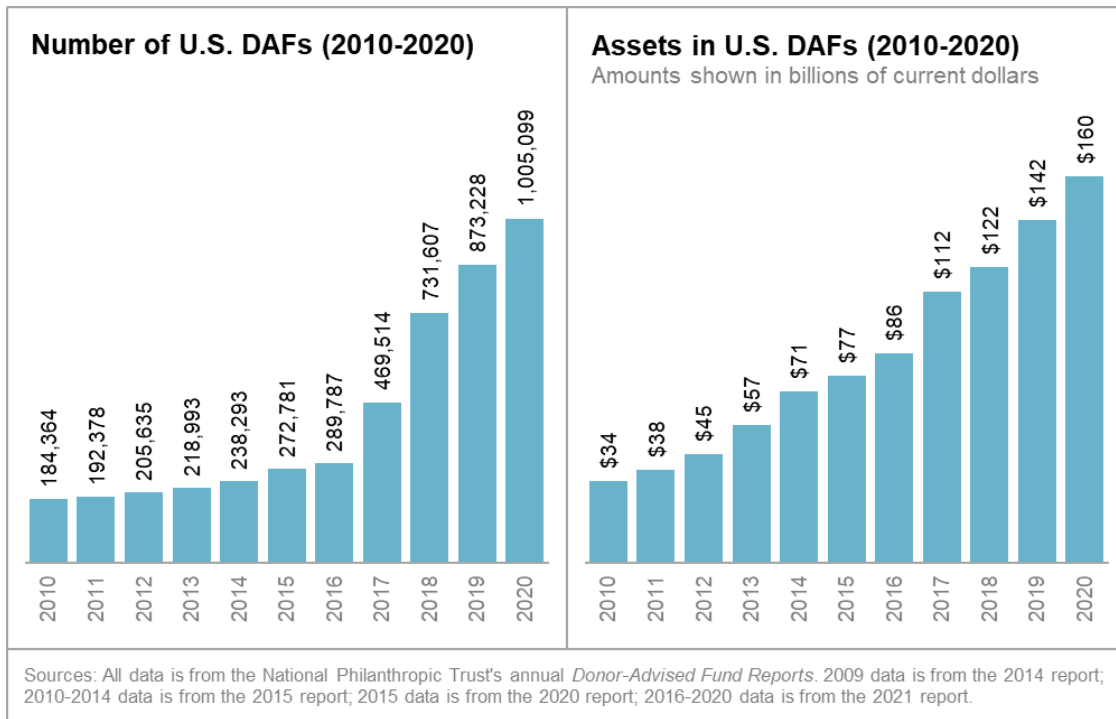
Private foundations fulfill the letter of the law in being legitimate recipients of charitable donations. But with most private foundations giving out grants at annual payout rates just barely above the minimum 5 percent of assets required, they do not always move money in a timely way to public charities, and can serve instead as warehouses for charitable funds.<sup>48</sup>

They can also prove financially advantageous to the investment advisers who manage their endowments and to the family members who sit on their boards, raising questions about the extent to which they are truly fulfilling their charitable missions.

### **Wealthy giving to donor-advised funds is growing even faster.**

As quickly as the wealthy have been creating private foundations, their embrace of donor-advised funds, or DAFs<sup>49</sup>, has been even more rapid. DAFs have been the fastest-growing recipient of charitable funds in the U.S. in recent decades. According to the National Philanthropic Trust, donations to DAFs rose from \$9 billion in 2010 to almost \$48 billion in 2020—growth of 412 percent over just ten years.<sup>50,51</sup> In contrast, giving by individual donors grew by just 56 percent over the same period.<sup>52</sup>

DAFs have seen such phenomenal growth that they now house more than \$160 billion in assets, and some DAF sponsors are now among the largest single charitable recipients in the country. A commercial DAF sponsor, the Fidelity Charitable Gift Fund, became the top recipient of giving for the first time in 2016, edging the United Way out of the top spot.<sup>53</sup> By the following year, six commercial DAF sponsors had broken into the top 10,<sup>54</sup> and they have never looked back. Fidelity Charitable alone held nearly \$50 billion in assets in 2021.<sup>55</sup>





DAFs offer wealthy donors a convenient way to offload appreciated complex assets such as appreciated real estate and artwork without incurring capital gains taxes and, at the same time, to get a tax deduction for their donation.<sup>56</sup> But there is no legal requirement for DAFs to pay out their funds to working charities—ever—so the civic benefit from these publicly-subsidized gifts can be delayed indefinitely.

Since DAFs have lax reporting requirements<sup>57</sup>, it is nearly impossible to determine how quickly individual DAF accounts are paying out, or whether their grants are going to qualified charities at all. But a couple recent reports indicate that the money flowing out to working charities from these giving vehicles is astonishingly slow. And that behind the bullish aggregate payout rates reported by donor-advised fund sponsors, the more generous funds are providing cover for many funds that give very, very little—and often nothing at all.

The first of these reports was a groundbreaking 2021 analysis of donor-advised funds at Michigan community foundations prepared by the Council on Michigan Foundations. This report was the first to examine the giving of a large sample of DAFs at the individual account level, and it revealed that the *median* payout rate of Michigan’s DAF accounts was just 3.1% in 2018.<sup>58</sup>

The second report was a 2022 study by the DAF Research Collaborative, or DAFRC. This study revealed that of the accounts the DAFRC was able to analyze—which included only community foundation DAFs—35 percent of the accounts paid out at less than 5 percent of assets, including 29 percent of accounts that gave no grants whatsoever in any single year. And 14 percent of DAF accounts paid out no grants in the entire four years covered by the DAFRC analysis.<sup>59</sup>

In both of these cases, if the researchers had not been able to see account level detail, the sponsors’ publicly-reported aggregate payout rates would have masked the fact that many accounts paid out abysmally little.

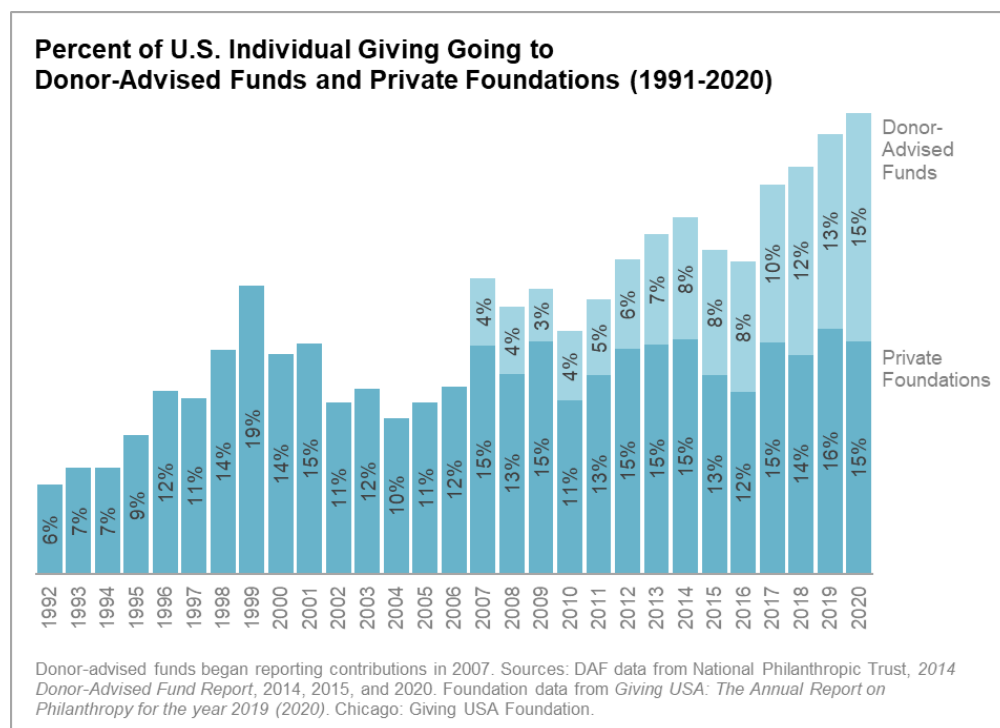
### **Private foundations and donor-advised funds are eating up ever larger slices of the charitable pie.**

Charitable giving in the U.S. has remained remarkably constant at roughly 2 percent of personal disposable income—the income that is left over for people to spend once taxes are taken out—for more than forty years.<sup>60</sup> But, over that same time, donations to private foundations and DAFs have grown many times faster than donations to working charities.

This means that not only have foundations and DAFs grown in sheer volume, but they have also grown significantly in the *share* of charitable dollars that they receive from America’s donors each year, while working charities receive less.

Data from *Giving USA* shows that giving to private foundations increased from 5 percent to 15 percent of all charitable giving since 1991.<sup>61</sup> And data from the National Philanthropic Trust

shows that giving to DAFs increased from 4 percent to 15 percent of all charitable giving since 2007.<sup>62</sup> Combined, these two intermediaries now soak up 30 percent of all U.S. donations—more than quintupling their share of the charitable pie in less than thirty years.



According to tax and philanthropy experts James Andreoni and Ray Madoff, this shift towards intermediaries has resulted in an estimated shortfall of \$300 billion to working charities over just the past five years.<sup>63</sup>

## Top-Heavy Philanthropy Means the Wealthy Can Evade Tax Obligations

**Affluent donors can opt out of paying millions in taxes.**

A 2021 *ProPublica* exposé revealed that many of the wealthiest people in our country have been able to use various tax-avoidance strategies that bring their effective tax rates down to just a “tiny fraction” of the millions of dollars that their assets grow each year.<sup>64</sup> One of the ways that they do this is through philanthropy—particularly through the use of private foundations and donor-advised funds.

When millionaires and billionaires donate unlimited amounts of money to charity, they are able to opt out of paying their fair share of taxes to support the public infrastructure we all depend on. But it is important to remember that philanthropy is not a substitute for democratically-governed public investments paid for by a fair and adequate tax system—both because of the

scale of the problems we face, and because there's no guarantee that billionaires will voluntarily choose to fund the things we need.

It is difficult, of course, to pin down exactly when a billionaire is using charitable giving primarily for tax avoidance, rather than sincere generosity. But some examples raise red flags.

Jeff Bezos and Elon Musk are currently the two richest people in the world and are also two of the billionaires exposed by *ProPublica* as having paid zero taxes in recent years.<sup>65</sup> Both of them made significant tax-deductible gifts to charity during the years when they paid no taxes—and both have made heavy use of intermediary giving vehicles to do it.

Bezos is currently worth \$137.5 billion, according to *Forbes*.<sup>66</sup> In the past, he gave a few gifts worth tens of millions of dollars to various direct causes, including his alma mater Princeton University and a museum in Washington state.<sup>67</sup> During the two years of the pandemic—and coincident with a huge increase in his assets—he stepped up his giving with gifts worth a total of \$400 million to Feeding America, the Obama Foundation, and the Smithsonian. But by far his greatest charitable commitment has been his 2020 pledge of \$10 billion to combat climate change through his Bezos Earth Fund.<sup>68</sup>

The structure of Bezos' Fund has been secretive, but indications are that he has set it up as a limited liability corporation (LLC).<sup>69</sup> Unlike a private foundation, an LLC would allow Bezos to have complete control over the management of the money, including reclaiming it if he so chooses. It would also allow him not only to give grants to charity but also to invest in for-profit ventures or to give to political causes and candidates. Of his \$10 billion pledge, he has so far fulfilled more than a tenth of it by giving away \$1.4 billion to various environmental groups.<sup>70</sup>

Musk, who is currently worth \$226 billion,<sup>71</sup> is a signer of the Gates-Buffett Giving Pledge to give away half of his money, either during his lifetime or in his estate.<sup>72</sup> He has occasionally given some relatively large gifts directly to working charities, including \$55 million to St. Jude Children's Research Hospital and \$5 million to an online learning organization. But the overwhelming majority of his giving has gone either to his own foundations or donor-advised funds. In 2021, Musk gave \$5.7 billion to charity—his greatest giving to date—but the recipients have been described only as “undisclosed”<sup>73</sup> and the gift was only exposed through a mandatory SEC filing<sup>74</sup>, leading many experts to think that it likely went into a donor-advised fund.<sup>75</sup>

It is worth noting that when Musk's foundation does give grants, the vast majority of those grants go to DAFs as well. In 2017, for example, the Musk Foundation gave out \$48 million in grants, but \$38 million of that went to a DAF controlled by Musk at Vanguard Charitable. The next year, \$12 million out of the foundation's \$14 million in grants went to a DAF at Fidelity Charitable.<sup>76</sup> Under current IRS rules, Musk's foundation has been able to count all of this DAF giving towards its annual payout requirement, reducing the amount it must give out to operating nonprofits to zero for years to come.

## Top-Heavy Philanthropy Means the Wealthy Can Use Public Charity for Self-Dealing and Personal Gain

Wealthy philanthropists can use charity for their own benefit in a number of ways—all without having to deliver a charitable benefit to the public. Besides gaining big tax deductions from their giving, they can use private foundations as sources of personal loans or compensation; they can use charities to push self-serving agendas; and they can use their giving to polish their reputations.

### **Charitable vehicles can be personal cash cows for donors.**

Unfortunately, some of the giving options available exclusively to affluent donors give them the ability to enrich themselves financially. This happens most directly in the case of private foundations.

When a donor sets up a foundation, they can appoint themselves, family members, friends, and associates as trustees. Trustees can then pay themselves compensation from the foundation's assets—and that compensation counts toward the foundation's charitable distribution requirement each year.

Non-family trustees are often compensated at larger foundations, especially when they serve in high-profile, full-time jobs such as executive directors or chief financial officers. Family members who are trustees of their own private foundations usually do not pay themselves for their trustee service. But it is permissible for them to do so, and a small portion do.

And some of these family trustees are indeed paid surprisingly high amounts for their trustee service. The du Pont family's Longwood Foundation pays its president, a du Pont descendant, more than \$350,000 in total compensation per year.<sup>77</sup> And the H.E. Butt Foundation pays more than \$300,000 each year to its president, the husband of a Butt family heir.<sup>78</sup>

Wealthy trustees can also take loans out from their foundations, and use that money for personal investments. This happens more frequently than we might suppose.

For example, Ken Malecha, the president of Best Brands Corporation, borrowed \$800,000 from his foundation—nearly all of its \$1 million in assets at the time.<sup>79</sup> Investor Raymond Perelman gave his son Ronald a loan of over \$120 million from their family foundation.<sup>80</sup> And corporate raider Carl Icahn borrowed \$100 million from his private foundation, invested the money in businesses that earned him tens of millions of dollars, and then was ten years late paying the loan back to the foundation—without interest.<sup>81</sup>

## **Wealthy donors can use philanthropy to push self-serving agendas.**

For any given issue, you are likely to find a millionaire philanthropist using charitable gifts to advance agendas that benefit them personally.

In 2019, for example, a number of wealthy parents participated in a criminal conspiracy to influence admissions at several top U.S. universities in favor of their children. The parents donated money to a charitable foundation called Key Worldwide Foundation (KWF). The foundation's founder, Rick Singer, then used foundation funds to bribe college officials, inflate exam scores, and pay himself.<sup>82</sup>

Foundation self-dealing in this conspiracy did not stop with Singer, however—and parents in the conspiracy got considerably more benefit from their donations than simply getting their child into a high-status school. Not only could they take a tax deduction for their gifts, since they were going to a charity, but they also often gave their gifts in the form of appreciated stock, and thus avoided capital gains tax on the sale of those assets.<sup>83</sup>

And some went even a step or two further in their malfeasance. In a letter to the IRS about the scandal, Senators Chuck Grassley and Ron Wyden of the Senate Finance Committee wrote that “several of the parents involved in the scandal may have misappropriated funds from private foundations over which they have financial control in order to make illicit payments to KWF.”<sup>84</sup> If this indeed happened, it would be in violation of the self-dealing prohibition regarding private foundations, since foundation assets cannot be used to pay for the personal interests of their primary donors. In addition, it is possible that the parents may have illegally claimed double the tax deduction for their donations—once when the funds went into their own private foundations, and again when the funds went into KWF.

As has already been well documented, billionaire oil executive Charles Koch and his late brother David have used their various foundations and DAFs to donate millions to nonprofits that, among other things, lobby hard against corporate taxes and spread disinformation about climate change that benefits their family business.<sup>85</sup> And the Walton Family Foundation, run by the children of Sam Walton, the founder of Walmart, has given hundreds of thousands of dollars to nonprofits that push for corporate and personal wealth protection policies including the Heritage Foundation, the Cato Institute, and Grover Norquist's Americans for Tax Reform, as well as the climate-change-denying Heartland Institute.<sup>86</sup>

But there are less well-known examples, as well. Willis Johnson, the founder of vehicle reseller Copart, donated money from his family foundation to pay for South Dakota to send its national guard troops to guard the border with Mexico.<sup>87</sup> And Dick Uihlein, the founder of business supply company Uline, has used his family foundation to contribute to nonprofits that have been challenging the validity of the 2020 presidential election, including some organizations designated as hate groups.<sup>88</sup>



## Other Factors Add Fuel to the Fire

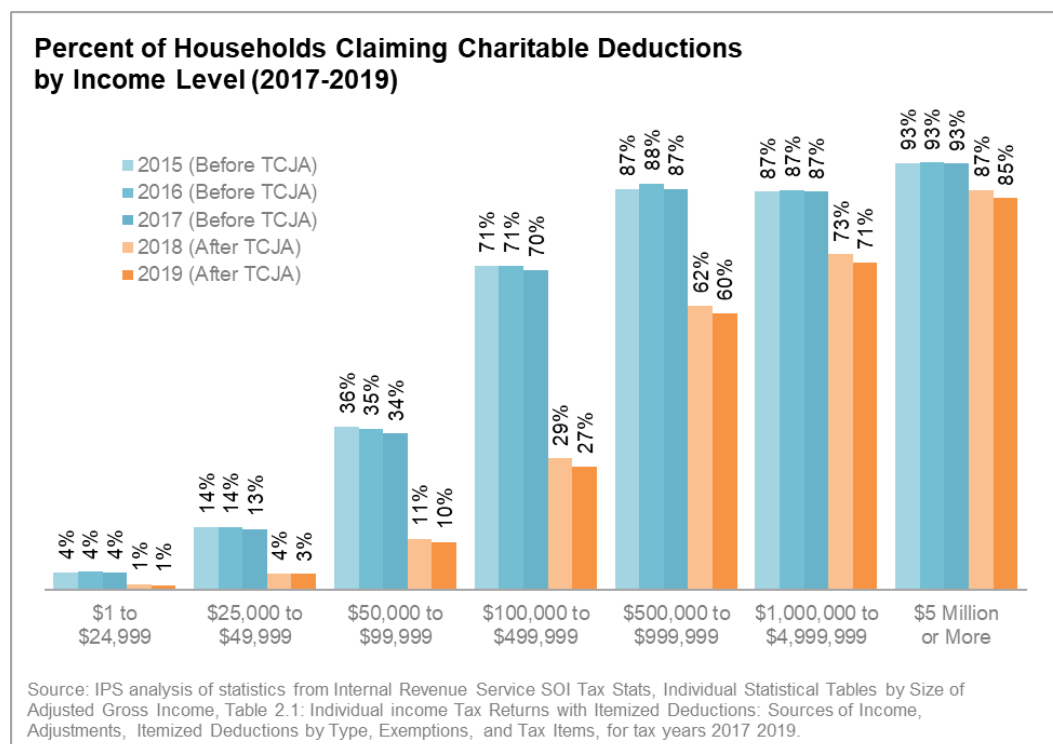
In 2017, Congress passed sweeping tax reform legislation that significantly reduced incentives for charitable giving. The nonprofit sector was still reeling from that change when it had to face COVID-19, perhaps its greatest test since the inception of national-scale philanthropy in the early 1900s. And, all the while, creative new tax shelters and tax-advantaged investment options have been gaining strength, further reducing the wealthy's need for charitable deductions.

### The Tax Cuts and Jobs Act of 2017

Charitable giving declined significantly and, so far, permanently following the passage of the Tax Cuts and Jobs Act, or TCJA, in 2017. The TCJA doubled the standard deduction and significantly decreased top income tax rates—changes which both reduce incentives for charitable giving—starting in 2018.

There is now strong evidence that the bill had a significant dampening effect on giving, particularly by upper-middle-class Americans. According to IRS data, in 2017, a full 25 percent of all households claimed charitable deductions on their tax returns. In 2018, when the tax changes took effect, that dropped to just 10 percent. And the change stuck—just 9 percent of all households claimed charitable deductions on their returns in 2019.<sup>89</sup>

The bill appears to have most affected people at upper-middle-income levels. While charitable deductions didn't change much for households at the top and bottom of the income scale, they



dropped a great deal for households in between. Roughly 70 percent of households making between \$100,000 and \$500,000, for example, claimed charitable deductions on their tax returns before the reform, but that dropped to just 29 percent after it.

This drop in charitable deductions jibes with declines in individual giving reported by *Giving USA*. The Giving USA Foundation wrote that giving by individuals fell from \$303 billion in 2017 to \$297 billion in 2018—a drop of 2 percent in current dollars, and a drop of more than 4 percent when adjusted for inflation.<sup>90</sup>

The *Chronicle of Philanthropy* was one of the first of the charitable sector news outlets to point out that the drop in contributions in 2018 was “due largely to average Americans donating less.” In previous years, they said, major giving had compensated for continued declines in giving by ordinary Americans—but this was no longer true.<sup>91</sup>

It is unfortunately likely that the effects of the TCJA will last far into the future. Since 2018, growth in individual giving has barely kept ahead of inflation, and has generally lagged behind growth in giving by other sources.<sup>92</sup> One study by Independent Sector and the Lilly Family School of Philanthropy has projected that the tax change could reduce charitable giving by as much as \$19.1 billion per year from 2018 through 2025.<sup>93</sup>

## Two Years of COVID-19

U.S. charities have now weathered two years under a global pandemic. Natural disasters, recessions, and changes in policy have all buffeted the philanthropic sector for better or for worse during its entire history. But the pandemic and its associated economic shock continue to pose an existential threat beyond any the sector has experienced before—and has exacerbated the shift toward top-heavy philanthropy.

In the first pandemic year, many donors across the income spectrum tried to help. Average Americans were hit hard financially during 2020, but still tried to assist others suffering in the crisis. According to Independent Sector, donor numbers grew by 1.3 percent during the first year of the pandemic, as more people drew from their shrinking paychecks to give to charity.<sup>94</sup>

Society also begged private foundations and donor-advised fund donors to dig deeper—and many did.<sup>95</sup> Foundation giving grew by more than 15 percent and DAF giving grew by 27 percent from 2019 to 2020, well outpacing their typical growth rates.<sup>96</sup>

And the result was that charitable revenue surged in 2020, growing by 9 percent over 2019, or 8 percent when adjusted for inflation.<sup>97</sup>

But giving during 2020 was not spread evenly. Many social service and health care charities saw record outpourings of support. Other organizations struggled, particularly if their missions were not directly related to pandemic aid. Social distancing and community lockdowns, while

necessary, severely hurt nonprofits that rely on the physical presence of visitors and those with fundraising programs based on events or street canvassing. And many food banks and homeless shelters were hit doubly hard, seeing the need for their programs rise even as they experienced revenue shortfalls.<sup>98</sup>

According to a study by the Urban Institute, small organizations suffered much more than big ones; 45 percent of organizations with budgets of less than \$100,000 had a decline in donations in 2020, while only 15 percent of organizations with budgets of over \$10 million saw declines.<sup>99</sup>

To make matters worse, the pandemic-related giving spike appears to have leveled off, even though many charities are still facing pandemic-related austerity. According to *Giving USA*, overall charitable giving did grow 4 percent from 2020 to 2021 in current dollars—but was actually down by 0.7 percent when adjusted for inflation.<sup>100</sup> With inflation still high and a potential recession looming, charities will likely continue to struggle in 2022 and beyond.

And most importantly for the long-term health of the sector, the pandemic has only accelerated charities' dependence on wealthy mega-donors, foundations, and donor-advised funds. The percent of overall giving coming from individuals continued to slide, from 69 percent in 2020 to 67 percent in 2021. The percent coming from foundations continued to increase, from 15 percent in 2020 to 19 percent in 2021.<sup>101</sup> And, as the *Chronicle of Philanthropy* reported, nearly all of the increase in giving in 2020 came almost entirely from major giving—not from broad-based support by everyday Americans, who were themselves coping with economic shock.<sup>102</sup>

Overall, the two-year effect of the pandemic on the charitable sector and the services it provides has been devastating. The U.S. nonprofit workforce is slowly recovering, but was still estimated to be down 495,000 jobs as of December 2021, as compared to pre-COVID levels. An estimated 44% of nonprofits have had to reduce services, 47% have served fewer people, and 64% had to pause services for at least some time during the height of the crisis.<sup>103</sup>

"In some ways, 2020 is a story of uneven impact and uneven recovery," said Amir Pasic, the dean of Indiana University's Lilly Family School of Philanthropy. "Many wealthier households were more insulated from the effects of COVID-19 and the ensuing economic shock," said Pasic, "and they may have had greater capacity to give charitably than households and communities that were disproportionately affected and struggled financially."<sup>104</sup>

## Competition from Impact Investing and Tax Shelters

### **More wealthy people are seeing impact investing as a substitute for direct giving.**

Affluent individuals, foundations, donor-advised fund sponsors, and working charities eager to have a positive effect on the world have been increasingly looking to impact investing as a way to do it. A significant portion of impact investments, however, are made through tax-advantaged vehicles, such as donor-advised funds.

Impact investment means choosing to invest in ventures that may earn lower returns than conventional ones, but where the social benefit from those ventures will theoretically outweigh the reduced revenue. Since the primary goal of impact investments is not profit but rather a positive result for society, they are often publicly subsidized through tax reductions or credits.

Today, at least \$715 billion has been put into impact investment projects worldwide.<sup>105</sup> And donor-advised fund sponsors in particular are jumping into the market with both feet, offering a variety of impact investing options to their account holders. The Fidelity Charitable Gift Fund, for example, manages five separate impact investment funds which together held more than \$3 billion in 2021.<sup>106</sup> Impact Assets, an impact investing firm, has received \$2 billion in investments through their donor-advised fund program.<sup>107</sup>

As the taxpayer subsidized impact investment market grows, so too are concerns that this sort of for-profit “philanthro-capitalism” is not yielding the positive public returns that it should.<sup>108</sup> And impact investing is increasingly being used as a substitute for direct philanthropic giving—particularly among the tech industry billionaires that are most drawn to it<sup>109</sup>, and at private foundations, which can use it to lower both their excise taxes and their payout requirements.<sup>110</sup>

### **Dynasty trusts could further reduce the amount of money going to charity.**

The release of the Pandora Papers in October 2021 raised the specter of a growing industry that is drawing revenue away from working charities: onshore tax havens such as dynasty trusts.<sup>111</sup>

When wealthy people put a portion of their assets into a dynasty trust, the money is held indefinitely by another entity—usually a bank—for the benefit of a designated beneficiary. The assets held in trust are not subject to taxation.

Most of the time the beneficiary is an heir who will receive the money when the original trust founder dies, allowing the heir to avoid estate, gift, and generation-skipping taxes.<sup>112</sup> But in some states, the original trust founder can name themselves as beneficiary, allowing them to escape even more taxes.

When wealthy people are able to shield assets from taxation this way, both for themselves and their heirs, they have less need for the deductions that come from charitable giving and bequests. As tax and philanthropy expert Ray Madoff said, “there’s every reason to think that the ultimate effect of this type of wealth being put into these vehicles will also be a long-term loss in revenue for charitable organizations.”<sup>113</sup>

# Fixing Philanthropy

The last time Congress overhauled the legal framework for the philanthropic sector was in 1969, when wealth was considerably less concentrated than it is now. This framework provided important tax-reduction incentives to encourage timely giving to charity—but it also created the loophole that allowed for the commercial exploitation of donor-advised funds.<sup>114</sup> It is time to modernize the rules governing philanthropy to:

- Promote a robust independent nonprofit sector outside of individual, political, and corporate influence.
- Prevent abuses of the tax system by philanthropy primarily used for aggressive tax avoidance or as a means to maintain control over donated dollars.
- Protect democracy and public society from the undue influence of private wealth and power.

To further these larger goals, the rules governing philanthropy should be overhauled to maximize the public good in these ways:

- Discourage the warehousing of charitable wealth by ensuring the timely flow of funds out of charitable giving vehicles for the public benefit.
- Implement governance mechanisms to align tax deductions with the public interest and to protect the integrity of our tax system.
- Encourage broad-based giving across all segments of society, particularly by the non-wealthy.

The public agrees that reform is needed. According to a July 2022 Ipsos poll, 81 percent of Americans do not believe that taxpayer money should subsidize the creation of perpetual private foundations. 69 percent want to double the minimum payout requirement for private foundations. And 72 percent want donor-advised funds to pay out their funds in five years or less.<sup>115</sup>

What follows is a menu of reforms, formed in consultation with policy experts in the philanthropic and civic space. We do not view our role as final arbiters of policy recommendations and, in some cases, offer multiple policy solutions.

## Reforms to Discourage the Warehousing of Charitable Wealth

The reforms below would increase the flow of charitable dollars, ensure greater accountability, and curb abuse by the indirect giving vehicles of foundations and donor-advised funds.

## A. Reforms to Donor-Advised Funds

The Tax Reform Act of 1969 largely established the rules governing public charities that we use today. But, as historian Lila Corwin Berman has written, the Act also opened giant loopholes that gave “unprecedented levels of public-subsidized power to private actors---specifically, to donor-advised funds.”<sup>116</sup> DAFs have taken advantage of these loopholes to set up private giving accounts with no payout requirement, few transparency and reporting provisions, and other abuses of the public trust.

The “donor-advised” descriptor is essentially a fictional notion, since the donor continues to control the destination of their gifts and, often, the investment practices of the fund. To protect the interests of the taxpaying public, Congress must address the fundamental design flaws in the DAF system with the reforms below.

**A1. Require a payout for donor-advised funds.** DAFs should be required to pay out the entirety of any donations within three years after donations have gone into the fund, including any income earned on these original donations during that time. DAF sponsors would set up sub-accounts under each fund for each calendar year to track the payout schedule of donations and income by year.

A faster DAF payout would have broad public support. According to a recent Ipsos poll, a full half of Americans believe DAFs should pay out within 2 years, and 72 percent believe DAFs should pay out within 5 years.<sup>117</sup>

**A2. Allow tax deductions to be taken only after the distribution of funds to an operating charity.** Currently, donors take their tax deductions when their donations go into the DAF, giving them no incentive to move funds out to working charities in a timely way. Distributions to another DAF or impact investment would not count as distributions to operating charities.

**A3. Limit tax deductions for donations of complex assets to their sale value.** This would base the deductions for donations of complex, non-cash appreciated property such as artwork, real estate, and cryptocurrency on their actual sale value, rather than their assessed value, and would delay that deduction until the year the property is sold. This would prevent donors from receiving charitable tax deductions based on overly-inflated assessments of the property’s value.

**A4. Exclude impact investments from counting toward DAF payout.** Impact investing should be encouraged, but not through tax-advantaged intermediaries. DAFs are meant to be used as short-term intermediaries for transferring funds to charities. To ensure that these tax-deductible donations serve the public interest, revenue should not be tied up in the DAF for more than a short time. There are existing DAFs that have assets currently tied up in multi-year impact

investments and are not able, in the short-term, to pay out funds. These DAFs could be temporarily exempted from the new rules.

**A5. Increase DAF transparency and reporting.** Donations to and from DAFs, as well as payout rates, should be publicly disclosed and reported on an account-by-account basis. To meet the IRS's public support test,<sup>118</sup> which ensures that charitable organizations are broadly-supported, grants from donor-advised funds should also be attributed to the individual donor and not to the sponsoring organization. This could be done in such a way as to protect anonymous givers.

We would also suggest mandating that DAF sponsors disclose to the IRS the names of all individual donors who have contributed over \$10,000 to each DAF account and the charities to which each individual DAF account has donated over \$10,000.

**A6. Prohibit perpetually-endowed donor-advised funds.** Endowed DAFs are accounts where the income from the fund can be granted out to charity each year but the bulk<sup>119</sup>—or sometimes all<sup>120</sup>—of the principal must remain untouched. These endowed DAFs can currently be set up in perpetuity, and some states even offer tax credits to donors who do so.<sup>121</sup>

But the deductibility of gifts to DAFs—which is entirely subsidized by the American public—is predicated on the use of those funds to serve the public interest in a timely way. Taxpayers should not be required to subsidize privately-controlled DAFs in perpetuity, since they receive no commensurate or timely benefit from perpetually-held funds.

**A7. Set firmer requirements for the nonprofit status of sponsoring organizations.** Some of those who know DAFs best have questioned whether sponsors should qualify as charities. For example, Marv Friedlander, who led the IRS division<sup>122</sup> that approved DAFs as public charities in the first place, has written that “all in all, I think it’s time to statutorily throw out the fiction that a DAF is a constituent part of a public charity.”<sup>123</sup>

This provision would make it so that DAF sponsors could not qualify as 501(c)(3) tax-exempt organizations if 25 percent or more of the sponsor’s governing board are (a) dealers in securities, (b) officers of for-profit organizations, and/or (c) employees of a financial corporation that can exercise control over the sponsor.

If a sponsor cannot meet these conditions, then the DAFs they manage should not qualify as charitable. This would force DAF sponsors to draw an explicit distinction between their staff and the staff of any closely-affiliated corporations. And it would help to ensure that the sponsors’ actions, recommendations, and reporting are driven solely by their charitable mission, rather than by for-profit interests.



## **B. Reforms to Private Foundations**

Over the past few decades, the assets of private foundations have been piling up quickly. By the end of 2021, U.S. foundations had an estimated \$1.3 trillion—money for which donors have already received tax deductions, but which is not making its way out to working charities.<sup>124</sup> Foundations also have great latitude in what they can count as charitable distributions—including gifts to donor-advised funds and compensation paid to staff and board members—which opens up the risk of abuse and self-dealing.

**B1. Increase the annual foundation payout requirement.** Foundations currently only have to distribute a minimum of 5 percent of their asset value to charity each year.<sup>125</sup> We propose increasing the requirement to 10 percent of assets.

An alternative to this would be to base the payout requirement on asset value, with the highest payout requirements for foundations with assets over \$100 million. As Candid's Issue Lab has reported, smaller foundations typically have higher payout rates than larger foundations, so requiring larger foundations to pay out more would target the reform to where it is most needed.<sup>126</sup>

Federal and state laws, including the Uniform Prudent Management of Institutional Funds Act, may need to be revised to allow for increased payout of charitable funds independent of economic conditions.<sup>127</sup>

**B2. Reform foundation payout exclusions.** Fixes should include:

- a) Eliminating administrative overhead from counting towards the minimum payout requirement. This would reduce incentives for exorbitant internal spending on salaries, travel, and accommodations for board members; internal programs; and other administrative costs—and would move more funds to active charities.
- b) Prohibiting grants to DAFs from qualifying toward the payout requirement unless the DAF funds are granted back out to working charities within one year. This mirrors a provision currently included in President Biden's 2023 budget proposal.<sup>128</sup>
- c) Closing loopholes that allow program-related and impact investments to be considered part of the payout allocation. Using tax-advantaged vehicles such as foundations for socially-oriented investing may have public benefits, but these activities undermine the principle of moving funds out of donor dominion in a timely way. In other words, no form of investment should be considered a charitable gift. Such activities can be continued, and even encouraged, but should not count toward the qualified payout distribution.

**B3. Require board independence.** If a private foundation is truly a public interest organization, it should not have a board composed entirely of family members and paid staff. Foundations should have independent boards with rules similar to those governing public corporation boards in many states.

**B4. Impose a ban on compensating family members.** To eliminate the potential for self-dealing, there should be an outright ban on compensation to founders and their family members for their services to the foundation.

**B5. Expand definitions of fiduciary duties to include mission alignment considerations.** Foundations should have latitude in their investment policies and practices to exclude investments in socially injurious companies and enterprises that are not aligned with their missions.

**B6. Eliminate the perpetual foundation.** This would require the charters of all future private foundations to include a limited lifespan provision.

The idea that foundations should exist in perpetuity is in fundamental conflict with their tax-deductible status. The deductibility of gifts to foundations—which is entirely subsidized by the American public—is predicated on the use of those funds to serve the public interest in a timely way. Taxpayers should not be required to subsidize privately-controlled foundations in perpetuity, since they receive no commensurate or timely benefit from perpetually-held funds.

Alternatives to this would be to establish a higher excise tax rate on legacy foundations, or to create a Limited Lifespan Foundation status that is subject to a lower excise tax rate. Limited Lifespan Foundations would be chartered to exist for less than 25 years.

## Reforms to Protect the Integrity of our Tax System

Our system of charitable giving is a creature of the tax code, so we can't implement meaningful charity reform unless we close the loopholes that allow philanthropy to be used for tax avoidance. And reform will have little effect without proper oversight to ensure that donors follow the rules.

### C. Creation of a New Oversight System for Foundations and Charities

The charitable nonprofit sector accounts for over 10 percent of America's private workforce and contributes 5 percent of the gross domestic product. But the offices of state attorneys general typically have small charity divisions with few resources devoted to oversight and are ill-equipped to oversee charities registered in their states. Concerns over the abuse of charities in the 1970s did spawn national watchdog entities like Independent Sector and the National

Committee for Responsive Philanthropy,<sup>129</sup> but broad-based public oversight of the sector is still severely lacking.

**C1. Create a new Office of Charity Oversight.** Use excise tax revenue from foundations to fund a new independent watchdog organization, removing that responsibility from the IRS. This new regulatory body would have broad authority not only to support the nonprofit sector and increase its effectiveness, but also to hold it accountable.

The U.S. Department of the Treasury and the Internal Revenue Service are currently charged with certifying tax exemption and overseeing charitable giving. But they are also constrained in the resources allocated to enforcement, especially with severe cutbacks to the IRS, so larger-scale wrongdoing is slipping through the cracks as it is. “The wealthy are stealing tens of billions from American taxpayers,” Senator Ron Wyden said recently about the inability of the IRS to enforce tax laws. “Paying taxes has become increasingly voluntary for those at the top.”<sup>130</sup> In the face of these large-scale challenges, investigating charitable abuses is a resource-intensive sideline with little revenue payoff.

This is particularly true when it comes to donor-advised funds. Marv Friedlander was the head of the IRS department that granted DAFs their charitable status in the first place.<sup>131</sup> But he has lost patience with how IRS inattention has allowed DAFs to skirt the rules, and suggests that the time has come for them to be managed some other way. “Why impose technically dense provisions on IRS agents,” he writes, “when DAFs...have failed to operate properly because they are not subject to the oversight of the funding public.”<sup>132</sup>

The good news is that the foundation sector provides substantial federal revenue itself with which to fund an oversight body. Revenue from the excise tax on the net investment income of foundations was \$960.9 million in 2018, the most recent data available.<sup>133</sup> At this stage, charities generate over \$1 billion to fund an oversight body.

**C2. Provide block grants to state oversight offices.** The new Office of Charity Oversight could allocate a portion of excise tax revenue to state-level oversight offices. Funds could be block-granted to states depending on the size of their philanthropic and charity sectors.

## **D. Reforms to Increase Transparency**

Legislators should take a number of actions to restore public trust in the charitable giving sector after decades of opaque activities. This would include reducing the politicization of charities and increasing transparency into the dark money world of anonymous political contributions and antidemocratic influence.

**D1. Prevent the politicization of charities.** Ensure that Congress doesn’t eliminate the Johnson Amendment,<sup>134</sup> which currently prohibits charities from supporting or opposing candidates for public office.

**D2. Shine a light on dark money.** Require the disclosure of donors to 501(c)4 corporations, which serve as a key mechanism for dark money donations from both the right and the left. While donors to 501(c)4 corporations don't claim a tax deduction, they can anonymously use them to give unlimited funds to influence issue work and campaigns.

## Reforms to Encourage Broad-Based Giving

Long-term declines in charitable giving by lower-dollar givers are less a result of tax policy and more a reflection of growing income inequality and declining economic security for many households. The only real way to broaden charitable support is to foster an economy that supports a stable and secure middle class, and to ensure that they have disposable income to donate to charity. For this reason, lawmakers should carefully structure policies to increase donor tax incentives so that they do not further subsidize households in the top 10 to 20 percent of income and assets. And they must balance private incentives for private charitable giving with the need for public revenues to support public services.

### E. Reform to Broaden Giving

Everyday Americans give generously when they can. When economic times are better for everyone, charitable giving increases as a percentage of disposable income—showing that most people give more when they have the money to do so.<sup>135</sup> We should encourage this natural generosity and give nonprofits a broader, more diverse base of support, by providing taxpayers at all income levels with an incentive to give.

We can encourage giving at all income levels by establishing a charitable tax deduction that applies to all taxpayers, not just those that itemize deductions on their returns. The trick is to establish a deduction that will not only provide real incentives for people to give more to charity, but also cost less to implement than it brings in.

**E1. Replace the itemized charitable deduction with a universal charitable tax deduction.** We recommend implementing a universal tax deduction for any households—not just those that itemize—that give more than 2 percent of their adjusted gross income to charity.

As part of the CARES pandemic relief Act of 2020, Congress implemented a temporary above-the-line charitable tax deduction for non-itemizing households. The measure allowed a maximum deduction of \$300 for individuals and \$600 for married couples, and was extended through 2021.<sup>136</sup> This provision cost a great deal and ended up doing very little to increase giving, mainly because most donors already give more than \$300 in any given year.<sup>137</sup>

A recent study by the Tax Policy Center shows that a universal deduction for giving at least 2 percent of adjusted gross income, on the other hand, is a “sweet spot” that would increase charitable contributions while simultaneously increasing tax revenue as well.<sup>138</sup> After analyzing

2019 tax revenues, they determined that such a deduction would have resulted in \$2.1 billion more revenue going to charities, and \$1.1 billion more revenue in taxes that year.

Any sort of universal tax deduction should exclude gifts to private foundations and donor-advised funds—as is the case with the temporary CARES Act tax deduction.<sup>139</sup>

## **F. Reforms to Reverse Top-Heavy Philanthropy**

Philanthropic reform alone is insufficient to remedy the antidemocratic effects of concentrated private wealth and power. For this, we need to tackle the broader ecosystem of wealth management practices of which strategic charitable giving is one aspect. The reforms below would directly address the problem of concentrated wealth and power in the charitable sector.

**F1. Establish a lifetime cap on charitable gift deductions.** Currently, we allow unlimited tax reductions to donors who have private foundations. This means that, as Bill Gates Sr. pointed out to report co-author Chuck Collins, Gates' son—Microsoft founder Bill Gates—will never pay taxes on the more than \$100 billion he will donate to his tax-exempt foundation. A lifetime cap of \$500 million would not discourage billionaires whose giving is genuinely motivated by generosity. But it would prevent donors from using charitable giving to reduce their taxes to zero indefinitely.

**F2. Establish a cap on the charitable estate tax deduction.** There is currently no limit on the amount of money that a person can pass tax-free to charity in their estate. This means that wealthy people can entirely remove themselves from the tax system by transferring their assets to their own private foundation. It is important that every person contribute to the costs of government—particularly the wealthiest among us. One way of accomplishing this would be by limiting the estate tax charitable deduction to a percentage of a donor's estate; we would recommend 50 percent.

**F3. Levy a wealth tax on DAFs and closely-held private foundations.** A wealth tax, such as Senator Elizabeth Warren's proposal to levy a 2 percent annual tax on wealth over \$50 million, should also apply both to donor-advised funds and to private foundations that are closely controlled by donors. As Emmanuel Saez and Gabriel Zucman wrote in a 2019 paper on wealth taxation, "To prevent abuse, donor advised funds or funds in private foundations controlled by funders should be subject to the wealth tax until the time that such funds have been spent or moved fully out of the control of the donor."<sup>140</sup>

For example, assets in the Musk Foundation should be counted as part of Elon Musk's personal wealth until it moves out to working charities. This would encourage the transfer of charitable funds to nonprofits, public foundations, and community foundations' general funds that wealthy donors do not control.

## Additional Revenue to Charity Resulting from Reform

Implementing just a couple of the most critical measures from the menu above would result in a significant amount of additional revenue flowing to working charities.

Requiring donor-advised funds to pay out incoming donations within three years, for example, would have resulted in at least an estimated \$26 billion in additional DAF grants to charity from 2018 to 2020. And if the minimum required payout requirement for private foundations had been 10 percent, rather than 5 percent, it would have resulted in at least an estimated \$166 billion in additional foundation grants to charity from 2018 to 2020.

These estimates are detailed in the Appendices at the end of this paper.

## What We Face Now

Philanthropy is an expression of our collective generosity and human solidarity. The nonprofits we support as a nation are both the lifeblood of a vibrant civil society and laboratories for experimentation with ways to solve our most pressing problems.

But the growing concentration of wealth and power is distorting philanthropy and imperiling our democratic institutions. Top-heavy philanthropy—small-dollar donor declines combined with increasing numbers of ultra-wealthy mega-donors—poses growing risks to the independence of nonprofits, the integrity of the tax system, and the health of our society.

We the people subsidize the charitable deductions of wealthy donors by up to 74 cents on every dollar. But we are seeing less and less of a return on our subsidy as the giving sector becomes more a province of the wealthy.

For over a decade, the Program on Inequality and the Common Good, based at the Institute for Policy Studies, has examined the impact of income and wealth inequality on civic life, opportunity, social mobility, democracy, and other aspects of U.S. society. We see that as inequalities of income, wealth, and opportunity grow in the United States, our society calls on the nonprofit sector to ameliorate the resulting damage and trauma. But the health and effectiveness of the charitable sector are deeply affected by these trends themselves.

While we celebrate the generous impulse behind so much of the philanthropic activity in the United States, we recognize that growing inequity in charitable giving holds risks not only for the nonprofit sector, but for the nation. And the public recognizes it, too; when taxpayers are aware of the ways wealthy donors can abuse charity, they show overwhelming support for oversight and reform. It's been more than fifty years since last time we significantly addressed the rules governing philanthropy, and it is high time to do it again.

# Appendices

## Appendix I: Estimate of Additional Revenue to Charity from Mandating a Three-Year DAF Payout

We have suggested implementing a three-year mandated payout for donor-advised funds. This would require each individual DAF account to pay out the entirety of any incoming contributions, plus any accumulated income earned on those contributions, within three years.

In this appendix, we estimate the amount of additional revenue that would have gone to charity if this mandate had already been in place six years ago—and if DAF accounts merely stuck strictly to the minimum required of them by the mandate, and waited the longest amount of time possible to grant out their funds.

According to the National Philanthropic Trust, U.S. DAFs received a total of \$77.53 billion in contributions from 2015 to 2017 (the orange cells in the table below). They paid out \$85.71 in grants from 2018 to 2020 (the blue cells in the table below).

If DAFs had a three-year mandated payout requirement, those incoming contributions would have been put into separate sub-accounts according to the year they came in, rather than going into a general DAF asset pot. The income they earned while they sat in the DAFs would have accumulated in those sub-accounts, along with the original contributions.

For example, the \$21.48 billion that DAFs took in in 2015 would have been put into its own 2015 sub-account, and it and any income it earned would have been tracked separately from contributions made in other years. If we assume that the original 2015 contribution was not spent out at all for three years, and earned similar returns to the S&P 500 during that time, it would have been worth \$27.96 billion by 2018, when it would have had to be completely paid out in grants to charity.

The \$25.20 billion and \$30.85 billion that DAFs received in contributions in 2016 and 2017 would have been similarly separately tracked.

In total, the contributions from 2015, 2016, and 2017 would have been worth an estimated total of \$112.22 by the time they had to be paid out in 2018, 2019, and 2020 (respectively). This total is \$26.51 billion greater than the \$85.71 that was actually granted to charity from over the three years from 2018 to 2020.

Again, this assumes that DAF donors gave out the minimum required of them, and delayed giving those grants as long as possible. DAF donors always have the option of being more generous, and giving those grants more quickly—both of which would better serve the interest of our public charities.



<b>Estimates of Additional Revenue to Charity from Mandating 3-Year DAF Payout</b>							
Assumes that all DAF accounts fulfill the bare minimum required, as follows: that they pay out the entirety of any contribution, plus any accumulated income earned on that contribution, on the third year following that contribution—and no earlier.							
Estimates also assume that DAF contributions earned income equivalent to returns on the S&P 500 while they remained in the DAF.							
Incoming contributions are highlighted in orange. Outgoing grants are highlighted in blue.							
All revenue amounts are in billions of dollars.							
	2015	2016	2017	2018	2019	2020	2018-2020 Total
<b>Actuals</b>							
Actual contributions to DAFs	\$21.48	\$25.20	\$30.85	\$36.22	\$39.69	\$47.85	
Actual grants from DAFs	\$14.15	\$15.97	\$19.71	\$23.75	\$27.29	\$34.67	\$85.71
<b>Estimates for a Mandated Three-Year Payout</b>							
Annual S&P 500 returns	1.4%	11.8%	21.6%	-4.2%	31.2%	18.0%	
2015 contributions + accumulated income	\$21.48	\$24.01	\$29.20	\$27.96			
2016 contributions + accumulated income		\$25.20	\$30.65	\$29.35	\$38.51		
2017 contributions + accumulated income			\$30.85	\$29.55	\$38.77	\$45.75	
Total grants from 2015-2017 contributions				\$27.96	\$38.51	\$45.75	\$112.22
Additional revenue to charity resulting from a mandated three-year payout				\$4.21	\$11.22	\$11.08	\$26.51
Sources: S&P 500 returns from The Balance ( <a href="https://www.thebalance.com/stock-market-returns-by-year-2388543">https://www.thebalance.com/stock-market-returns-by-year-2388543</a> ). DAF contributions and grants from National Philanthropic Trust, <i>Annual Donor-Advised Fund Report</i> , 2020 and 2021 editions ( <a href="https://www.nptrust.org/reports/daf-report/">https://www.nptrust.org/reports/daf-report/</a> ).							

## Appendix II: Estimate of Additional Revenue to Charity from Raising Private Foundation Payout Requirement

We have suggested raising the annual minimum required payout rate for private foundations to 10 percent. This would require all private foundations to give out 10 percent of their asset value in grants to charity each year, instead of the current 5 percent. To estimate the effect of this increase, we have assumed that it would only affect the granting behavior of foundations currently paying out at less than 10 percent, and that the granting behavior of foundations already paying out at 10 percent or more would remain the same.

*Giving USA*, the Giving Institute's annual publication on charitable giving, reported that foundations distributed an estimated \$238 billion to charity over the three years from 2018 to 2020.

The Charity Reform Initiative at the Institute for Policy Studies conducted an analysis of all publicly available IRS tax filings for private U.S. foundations that filed electronically in 2018-2020 as of May 2022. From that analysis, we determined that anywhere from 74 to 79 percent of foundations paid out at less than 10 percent of their asset value during those three years.

These below-10-percent foundations accounted for about 90 percent of the assets held in all U.S. foundations and about half of the grants from 2018 to 2020. Their gross payout rate—a

straightforward calculation of grants divided by assets—ranged from 5.2 percent to 7.0 percent, and they paid out an estimated total of \$132 billion in grants during that time.

If these foundations had given out grants at a gross payout rate of 10 percent instead, they would have given out a total of \$299 billion to charity from 2018 to 2020. This would have resulted in an additional \$166 billion in grants to charity during those three years.

<b>Estimates of Additional Revenue to Charity from Raising Foundation Payout</b>				
Payout rates are calculated as Adjusted Qualifying Distributions (Part XII, Line 6) divided by Net Value of Noncharitable Use Assets (Part X, Line 5) on the IRS 990-PF private foundation tax form.				
All revenue amounts are in billions of dollars.				
	2018	2019	2020	2018-2020 Total
<b>Actuals</b>				
Actual total U.S. foundation assets	\$995.3B	\$1,105.2B	\$1,214.6B	
Actual total U.S. foundation grants	\$73.9B	\$75.7B	\$88.6B	\$238.1B
Actual median payout rate	5.1%	5.1%	5.0%	
Actual gross payout rate (total assets/total grants)	7.4%	6.8%	7.3%	
<b>Estimates for Increasing Gross Payout Rate to 10% for Foundations Currently Paying Out Less than 10%</b>				
Proportion of foundations currently paying out less than 10%	74.9%	73.5%	79.2%	
Proportion of assets held in foundations currently paying out less than 10%	90.2%	90.5%	89.7%	
Proportion of grants from foundations currently paying out less than 10%	48.5%	54.8%	62.1%	
Median payout rate for foundations currently paying out less than 10%	4.6%	4.6%	4.8%	
Gross payout rate for foundations currently paying out less than 10%	5.2%	6.5%	7.0%	
Amount in grants paid out by foundations currently paying out less than 10%	\$35.8B	\$41.5B	\$55.0B	\$132.2B
Amount in grants paid out by foundations currently paying out less than 10% if their gross payout rate had been 10% instead	\$89.7B	\$100.1B	\$108.9B	\$298.7B
Additional grants to charity if foundations currently paying out less than 10% if their gross payout rate had been 10% instead	\$53.9B	\$58.6B	\$53.9B	\$166.5B
Total grants to charity if foundations currently paying out less than 10% if their gross payout rate had been 10% instead	\$127.8B	\$134.3B	\$142.4B	\$404.5B
Sources: assets, grants, and payout rates for foundations paying out less than 10% are from IPS Charity Data Lab analysis of publicly-available private foundation tax returns (990-PFs) for foundations filing electronically. Foundation assets are from St. Louis Federal Reserve, "Nonprofit Organizations: Total Financial Assets Held by Private Foundations, Level." Foundation grants are from <i>Giving USA: The Annual Report on Philanthropy for the year 2020</i> (2021). Chicago: Giving USA Foundation.				

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