**Tax Cuts and Jobs Act of 2017:**
**Implications for Nonprofit Organizations**
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On December 20, 2017, Congress enacted sweeping tax reform legislation referred to as the Tax Cuts and Jobs Act (the "Act") which brought significant changes impacting nonprofits and donors. In addition, there were a few proposed changes that ultimately were not included in the Act but may suggest future legislation.

**Revised Income Tax Brackets and Rates.** Most individual income taxes are reduced until December 31, 2025. The number of income tax brackets remain at seven, but the income ranges in several brackets have been changed and each new bracket has lower rates. A different inflation measure (Chained CPI or C-CPI) will be applied to the brackets instead of the Consumer Price Index (CPI), so the brackets increase more slowly. This is effectively a tax increase over time, as people move more quickly into higher brackets as their income rises. This inflation adjustment element is permanent

| Tax Rate | Income Range Individuals | Income for Married Joint Filers |
|---|---|---|
| 10% | $0 - $9,525 | $0 - $19,050 |
| 12% | $9,526 - $38,700 | $19,051 - $77,400 |
| 22% | $38,701 - $82,500 | $77,401 - $165,000 |
| 24% | $82,501 - $157,500 | $165,001 - $315,000 |
| 32% | $157,501 - $200,000 | $315,001 - $400,000 |
| 35% | $200,001 - $500,000 | $400,001 - $600,000 |
| 37% | $500,001 and Up | $600,001 and Up |

**Revised Long Term Capital Gains Tax Brackets.** Short-term capital gains are taxed at the taxpayer's ordinary income tax rate. The long-term capital gains (LTCG) tax rates of 0%, 15%, and 20% apply. Under the Tax Cuts and Jobs Act, the three capital gains income thresholds do not match up perfectly with the tax brackets. Instead, they are applied to maximum taxable income levels, as follows:

| LTCG Rate | Single Filers | Married File Jointly | Head of House | Married File Separately |
|---|---|---|---|---|
| 0% | Up to $38,600 | Up to $77,200 | Up to $51,700 | Up to $38,600 |
| 15% | $38,600-$425,800 | $77,200-$479,000 | $51,700-$452,400 | $38,600-$239,500 |
| 20% | Over $425,800 | Over $479,000 | Over $452,400 | Over $239,500 |

The 3.8% net investment income tax that applies to certain high earners will stay in place, with the exact same income thresholds.

**Increased Standard Deduction.** The Act nearly doubles the standard deduction for individual taxpayers. raising the standard deduction to $24,000 (from $12,700) for married couples, $12,000 (from $6,350) for unmarried individuals, and $18,000 (from $9,350) for head of household. The outcome for persons who do not pay mortgage interest or property tax is that in future years they will not get any tax savings from the first $24,000/$12,000 donated to charities each year. And there will be no tax savings from charitable gifts if less is donated. Taxpayers will instead take the $24,000/$12,000 standard deduction.

According to the Joint Committee on Taxation, the number of taxpayers who will itemize their deductions in 2018 and following years will fall from 40 million under former law to just 9 million under the new legislation. The Indiana University Lilly School of Philanthropy estimates that this reduced number of itemizers plus cutting the top marginal tax rate may decrease charitable giving by approximately $21 billion.

**Increased AGI Limit for Cash Gifts.** Before the Act, the deduction limit for cash gifts to publicly supported charities and operating private foundations was 50% of Adjusted Gross Income (AGI). Excess deduction may be claimed for up to five additional years, claiming as much deduction each year subject to the limit. The Act increases the limitation for cash contributions from 50% to 60% of AGI. This increase in the AGI limitation would normally incentivize cash contributions. However, due to the standard deduction increase, the impact on giving is less helpful.

AGI limitations on other types of charitable contributions are not affected by the Act. For example, contributions of long-term capital gain property, such as stock or real estate, continue to be subject to a deduction limit of 30% of AGI. "Long-term" means that the donor owned the capital asset for more than a year. This property is the best asset to donate to a charity since there are two advantages. First, one can claim a charitable tax deduction for the full value of the property. Second, there is no capital gains tax owed by the donor or charity. If the donor sold the asset instead, he or she would owe long-term capital gains tax.

**Repeal of Pease Limitation.** Under prior law, most itemized deductions such as for charitable gifts, mortgage interest and state/local income taxes, were reduced by the "Pease Limitation" to 3 percent of the amount that a taxpayer's AGI exceeded an annually inflation-adjusted AGI threshold. However, the reduction could not reduce total deductions by more than 80 percent overall. The thresholds for 2017 were $261,500 (single filers) and $313,800 (joint filers) of AGI. Elimination of the Pease Limitation should make the charitable deduction more useful for high income donors for whom the increased standard deduction has less impact.

**Charitable Giving Strategies Resulting from Act.** In anticipation of the Act, many persons who planned to itemize deductions for 2017, but not itemize in 2018 due to the higher standard deduction, accelerated their charitable gifts before December 31, 2017. For example, donors with multi-year pledges, pre-paid amounts scheduled for future years. Other donors maximized charitable deductions in 2017 by increased giving to a donor advised fund that will provide money for grants in future years.

On the other hand, some high-income persons who were subject to the Pease Limitation in 2017 chose to delay gifts to 2018 when the limitation expires. The increased standard deduction may not appeal to these high-income taxpayers who will take advantage of a charitable deduction that is no longer reduced by the Pease Limitation in 2018 and beyond.

One future charitable giving strategy that the Act may incentivize is the "bunching" of gifts. Donors may give every other year (or less frequent) to have a higher amount contributed in one year to get them over the standard deduction threshold. This will create the opportunity for claiming an income tax charitable deduction.

**IRA Charitable Rollover**. The IRA Charitable Rollover ("rollover") was made permanent as of December 18, 2015. However, many donors may inquire if this was changed by the Act given the unique history of the rollover as a temporary law from 2006 to 2015. The good news is that the Act did not change the charitable rollover which applies to persons age 70.5 years and older. The annual limit of $100,000 for rollovers per donor still applies. In fact, the rollover may be more attractive since it does not qualify for a charitable deduction and is not impacted by the standard deduction increase. Rather, the rollover escapes income tax liability on the withdrawal. And the rollover still cannot be made for a gift annuity or to a charitable remainder trust, private foundation or donor advised fund.

**Revised Estate Tax Exemption, Rate and Expiration.** The threshold to qualify for the estate tax is $11 million for individuals and $22 million for couples, which are currently set at $5.49 million for individuals, and $10.98 million for married couples. The exemption amounts are adjusted for inflation. Absent further congressional action, the exemptions will revert to their 2017 levels (adjusted for inflation) beginning January 1, 2026. The marginal tax rate for gift, estate and generation-skipping taxes remains at 40%.

**Increased Estate Tax Threshold May Reduce Bequests**. Even at today's levels, only 0.2% of all estates are subject to the estate tax. The unlimited (100%) charitable deduction for the estate tax remains an incentive for philanthropy from large taxable estates. However, since fewer estates will be subject to estate taxation, one potential result is a decline in the number of bequests to charitable organizations.

**Elimination of Alternative Gift Substantiation.** The Act eliminates alternative gift substantiation for charities. A donor who gives $250 or more to a charitable organization is required to obtain a contemporaneous written acknowledgement of the gift to substantiate the donation for tax purposes. Before the Act, the Internal Revenue Code permitted a charitable organization to file a document with the IRS containing detailed information about the donor and his or her gift. This change should have limited practical effect as most charities send acknowledgement letters or receipts thanking all donors for their contributions.

**Changes to Unrelated Business Income Tax Rules.** The Act changes the method by which charities must calculate income from their unrelated trade or business activities. Rather than having the flexibility to aggregate all sources of unrelated business income ("UBI"), a charity must calculate the amount of UBI it generates separately for each line of business. This new calculation eliminates charities' ability to offset gains in one line of business with losses in another, potentially increasing the total amount of UBI on which charities are taxed. However, due to the Act's reduction in the corporate tax rate, charities will now pay tax on UBI at a rate of 21 percent—down from the 35 percent rate previously imposed on net UBI.

**New Excise Taxes for Highly Compensated Nonprofit Employees.** The Act imposes a new 21 percent excise tax on compensation more than $1 million paid by tax-exempt organizations to their covered employees. An individual is a "covered employee" if he or she is one of the five most highly compensated employees of the tax-exempt organization for the tax year in question or was one of the five most highly compensated employees during any preceding tax year, beginning with 2017. The excise tax must be paid by the tax-exempt organization, not by the covered employee. This provision applies not only to charities but also private foundations and other organizations that are tax-exempt but not charitable.

**New Excise Taxes for Large University Endowments.** Private nonprofit colleges and universities that have at least 500 full-time or full-time equivalent (FTE) students and endowment assets exceeding $500,000 per student are now subject to a new 1.4 percent excise tax on the net investment income. For a university with 50,000 full-time or FTE students, the tax would be applied if the university's endowment exceeds $25 billion.

**Proposals Omitted from the Final Act.** The Act omits many proposals considered by Congress that represented potentially negative implications for nonprofits. For example, the Act did not include more burdensome procedures to establish the rebuttable presumption of reasonableness used to determine whether intermediate sanctions apply. In addition, a proposal to eliminate private activity bonds was omitted from the Act. And while President Trump threatened repeal of the Johnson Amendment that prohibits political campaign activity by tax exempt organizations, this Amendment was not repealed by the Act. Finally, while Congress considered imposing a payout requirement on donor advised funds, no such rate or requirement was included in the Act.

The Tax Cuts and Jobs Act included some good – as well as some potentially bad or ugly – for nonprofits. Time will tell how the Act's provisions will impact fundraising and other important aspects of nonprofit operations on behalf of important charitable missions.