October 15, 2024

Honorable Jason Smith
Committee on Ways and Means
U.S. House of Representatives
Washington, DC 20515

Honorable Ron Wyden
Committee on Finance
U.S. Senate
Washington, DC 20510

Honorable Richard Neal
Committee on Ways and Means
U.S. House of Representatives
Washington, DC 20515

Honorable Mike Crapo
Committee on Finance
U.S. Senate
Washington, DC 20510

Dear Chairman Smith, Chairman Wyden, Ranking Member Neal, and Ranking Member Crapo,

As you and your colleagues prepare for the 119th Congress, you will face consequential choices about our tax code. The expiration of various provisions from the 2017 *Tax Cuts and Jobs Act* at the end of 2025 will cause significant policy changes even if Congress does nothing. Those changes have the potential to impact every segment of the economy and society.

With so much at stake, we applaud you for gathering public input in a variety of ways. This letter will state many of the priorities of Independent Sector and its member organizations for tax legislation in 2025. We believe they are essential to unlocking the full potential of America's most powerful force for good: the nonprofit sector. While we strongly support these policies and will advocate for them vigorously, we also welcome the opportunity to engage with any proposal that seeks to strengthen our sector. Ours are not the only ideas worth considering, nor are they the only ideas we could support.

About the Nonprofit Sector

The nonprofit sector — including charities and foundations — has been bringing people together to meet community needs since our nation's

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founding. Every day, nonprofits provide housing, health care, nutrition, workforce development, education, disaster relief, cultural inspiration, spiritual guidance, environmental conservation, and any number of other vital services.

Because they are run by boards of directors grounded in the community and driven only by service, nonprofit organizations are uniquely responsive to those they serve. Perhaps because of this, they are among the most trusted organizations in our society. The nonprofit sector fosters democracy and serves as an essential and trusted partner to government at all levels.

While these organizations exist to serve a charitable purpose under the tax code, the sheer magnitude of their work constitutes a vital part of our economy. Nearly 10% of the private workforce in the U.S. was employed by a nonprofit in 2022, totaling over 12.8 million paid workers.[1] When data were last compared by researchers, employment in these organizations outpaced manufacturing at the national level and in 27 states.[2] Finally, as detailed later in this letter, the nonprofit sector is a significant source of tax revenue for the federal government.

About Independent Sector

Independent Sector was founded in 1980 as the national membership organization for nonprofits, foundations, and corporate giving programs nationwide. Working together, our hundreds of member organizations and their networks reach every state and district and touch the life of every American. They range from some of the largest charities in the world to all-volunteer organizations, and from major philanthropic institutions to small foundations, academic centers, community-based organizations, and more. Independent Sector's core aim is to support these organizations and all of civil society, working toward a healthy and equitable nonprofit sector to ensure all people living in the U.S. thrive.

In addition to policy advocacy, setting standards and best practices, and community-building work, Independent Sector commissions and conducts relevant research. Since 2020, our *Health of the U.S. Nonprofit Sector* reports have presented data, analysis, and recommendations about key areas powering the nonprofit sector. These reports focus on four critical measures of health: 1) financial resources, 2) human capital, 3) governance and trust, and 4) advocacy and civic engagement. Because these measures are so central to

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[1] U.S. Bureau of Labor Statistics. Quarterly Census of Employment and Wages. 2022 data accessed at https://www.bls.gov/bdm/nonprofits/nonprofits.htm

[2] Salamon, L., & Newhouse, C. (2020). The 2020 Nonprofit Employment Report. *Nonprofit Economic Data Bulletin no. 48.* Johns Hopkins Center for Civil Society Studies. https://ccss.jhu.edu/publications-findings/?did=517

understanding and strengthening the nonprofit sector, our policy recommendations have been organized accordingly.

The Tax Code Should Strengthen Financial Resources for the Nonprofit Sector

Charitable giving is the lifeblood of the nonprofit sector. The dollars that nonprofit organizations receive sustain their ability to provide essential services in every community across the nation. Unfortunately, charitable donations have shown significant weaknesses in recent years, according to data from *Giving USA*, the authoritative annual report on giving.[3] After a historic decline in 2022 — the largest annual decrease in the report's six-decade history — charitable donations also failed to keep up with inflation in 2023. When viewed alongside strong GDP and stock market growth and declining inflation, alarm bells should be going off for policymakers, as they are for nonprofit sector leaders.[4]

While there are certainly a wide range of influences on charitable giving, one consideration is particularly relevant to any discussion of tax policy in 2025: the impact of the Tax Cuts and Jobs Act of 2017 (TCJA). Although that legislation preserved the existing itemized deduction for charitable contributions, it made many other changes to the tax code that dramatically reduced the number of American taxpayers eligible to claim this deduction. At the time, Independent Sector joined with academic experts to estimate the impact of similar proposed changes. This study found that such changes would decrease charitable giving, including giving to religious institutions, by as much as $13.1 billion per year.[5] Unfortunately, recently released retrospective research indicates that the impact was even greater than anticipated. Using a data set uniquely designed to understand the impact of various societal, economic, and policy changes on giving, researchers recently demonstrated that the TCJA caused a permanent reduction in charitable donations of approximately $16 billion per year.[6]

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[3] The Giving Institute (2024). *Giving USA 2024: The Annual Report on Philanthropy for the Year 2023.* Summary available at https://philanthropy.indianapolis.iu.edu/news-events/news/_news/2024/giving-usa-us-charitable-giving-totaled-557.16-billion-in-2023.html

[4] Charitable Giving Coalition (2024, June 25). *Charitable Giving Coalition Concerned that Giving Failed to Keep Pace with Inflation in 2023*. https://charitablegivingcoalition.org/2024/06/950/

[5] Indiana University Lilly Family School of Philanthropy (2017). *Tax Policy and Charitable Giving Results*. Study commissioned by Independent Sector. https://independentsector.org/resource/tax-policy-and-charitable-giving/.

[6] Han, X., Hungerman, D., & Ottoni-Wilhelm, M. (2024). *Tax Incentives for Charitable Giving: New Findings from the TCJA.* National Bureau of Economic Research. https://www.nber.org/papers/w32737.

Beyond recent decreases in dollars donated, we are equally concerned by a longer-term trend that predates TCJA: fewer Americans are giving to charity at all. Twenty million fewer American households gave to charity from 2000 to 2016, a decline of 13%.[7]

Recommendation: Give every taxpayer access to the charitable deduction by making it available to those who do not itemize their tax returns

Giving every taxpayer access to the charitable deduction would more than mitigate the negative impacts of TCJA on giving and create millions of new donors in the short term.[8] In the long term, those new donors would build and reinforce the pipeline of American generosity. Regardless of total funding levels, it is critical that our civil society be funded by the broadest possible segment of the population. A nonprofit sector that is funded only by the wealthy will be less grounded in the communities it intends to serve.

When considering these policy options, it is essential to remember the uniqueness of the charitable deduction in our tax code. The true "beneficiary" of the deduction is not the individual who gives away their own income; it is the person or the community that receives charitable services as a result. As an active member of the Charitable Giving Coalition, Independent Sector strongly supports legislation that would expand access to the charitable deduction, including the Charitable Act.[9]

Recommendation: Increase the Charitable Mileage Rate for nonprofit volunteer drivers

Volunteers play a vital role in the work of nonprofit organizations and the communities they serve, providing proactive leadership, delivering essential services, and expanding the impact of nonprofit missions. We also know that those who engage with nonprofits as volunteers are more likely to donate to charities.[10] Federal law hurts nonprofit organizations' ability to attract this valuable resource by severely limiting how much they can reimburse volunteer drivers. While businesses can reimburse their employees up to 67 cents per mile driven,

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[7] Clark, C., Han, X., & Osili, U. (2019). *Changes to the Giving Landscape*. Indiana University Lilly Family School of Philanthropy. https://blog.philanthropy.indianapolis.iu.edu/2019/10/24/changes-to-the-giving-landscape-giving-before-and-after-the-great-recession/.

[8] Indiana University Lilly Family School of Philanthropy (2019). *Charitable Giving and Tax Incentives: Estimating changes in charitable dollars and number of donors resulting from five policy proposals.* Study commissioned by Independent Sector. https://independentsector.org/resource/impact-of-five-charitable-giving-policy-proposals/

[9] Charitable Act, S. 566 and H.R. 3435, 118th Cong. (2023).

[10] Bergdoll, J. (2021). Unpublished analysis of 2019 data from the Panel Study of Income Dynamics, public use dataset. Indiana University Lilly Family School of Philanthropy. Produced and distributed by the Institute for Social Research, University of Michigan. Dietz, N. (2015). Unpublished analysis of U.S. Census Current Population Survey Volunteer Supplement. University of Maryland Do Good Institute.

the charitable mileage rate is fixed at a mere 14 cents per mile, where it has been for over two decades. We support the Volunteer Driver Tax Appreciation Act — legislation that would correct this harmful discrepancy.[11]

The Tax Code Should Strengthen Human Capital and the Nonprofit Sector Workforce

As detailed previously, the nonprofit sector is a significant employer — collectively the third-largest segment of the nation's workforce. As part of this presence, nonprofit organizations generate major revenue for the U.S. Treasury: Their employees pay income and payroll taxes on over $873 billion in annual wages[12] and — despite their "tax-exempt" moniker — nonprofits pay an estimated $65 billion each year in federal payroll taxes.[13] These organizations face significant hiring, employee benefits, and worker training and retention issues and bear substantial costs as employers. But these major employers and taxpayers are excluded from a wide range of employer incentives delivered as tax credits that are made available to for-profit employers — simply because they are tied to the federal income tax.

<u>Recommendation: Give nonprofit organizations access to existing tax incentives available to for-profit businesses</u>

Nonprofit employers who take the same beneficial actions envisioned by Congress to hire and invest in workers should have access to the same tax incentives as their for-profit counterparts. In addition to correcting a fundamental unfairness, giving nonprofits access to these tax credits would boost the policies' underlying goals by reaching a new and significant portion of the workforce.

While not an exclusive list, these existing federal tax incentives[14] should be made available to eligible nonprofit organizations:

- Employer-Provided Childcare Credit (Section 45F): Access to affordable childcare is one of the major issues confronting the nonprofit sector's workforce, of which 65% are women, compared to 47% in the overall workforce.[15] Studies continue to show that the lack of adequate childcare for employees,

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[11] S. 3020 and H.R. 3032, 118th Cong. (2023).
[12] U.S. Bureau of Labor Statistics. Quarterly Census of Employment and Wages. 2022 data accessed at https://www.bls.gov/bdm/nonprofits/nonprofits.htm
[13] Calculation provided by the National Center for Charitable Statistics at the Urban Institute.
[14] For more detail, see *Tax Credit Fairness for Nonprofit Employers*, Independent Sector (2024). https://independentsector.org/wp-content/uploads/2024/08/Nonprofit-Tax-Credit-Fairness-paper-2024-1.pdf
[15] Independent Sector (2024). *Health of the U.S. Nonprofit Sector*. https://independentsector.org/resource/health-of-the-u-s-nonprofit-sector/.

particularly women of color, has been an impediment to the recovery of the workforce after the pandemic.

- Work Opportunity Tax Credit (WOTC) (expanded to all hiring categories, Section 51): WOTC is available to employers for hiring individuals from targeted groups who have traditionally faced barriers to employment, including TANF and SNAP recipients, long-term unemployed, and more. Currently, nonprofit organizations are only eligible to claim WOTC for hiring qualified veterans — one of the 10 targeted groups. Given their existing services to a wide range of targeted populations, incentives for employment of such individuals could provide yet another powerful way for nonprofits to make a difference.

- Employer Credit for Paid Family and Medical Leave (Section 45S): Attracting and retaining employees is a longstanding challenge for nonprofit employers, and it is made more challenging when only the leave policies of for-profit counterparts are subsidized through the tax code. In a workforce that is over two-thirds female, paid leave has even greater importance.

- Indian Employment Credit (Section 45A, expired): This credit provides up to $4,000 annually to employers who hire enrolled members of an Indian tribe or their spouses who work on an Indian reservation and live on or near a reservation. It expired at the end of 2021, but when restored should include nonprofit employers.

- Small Employer Pension Plan Start-Up Cost and Automatic Enrollment Credits (Sections 45E, 45T): Nonprofit workers shouldn't have to choose between serving a mission-oriented organization and securing their own retirement. Unfortunately, small employers cite high start-up costs as a deterrent to establishing retirement plans.[16] We applaud Senator James Lankford (R-OK) and Senator Catherine Cortez Masto (D-NV) for introducing targeted legislation[17] to correct this issue for small nonprofit organizations, and urge you to include it in any broad tax or retirement package you develop.

- Disabled Access Credit (Section 44): As organizations whose missions depend on serving the public, nonprofits have a special responsibility to be accessible to all. For organizations that occupy older

[16] U.S. Government Accountability Office (2015). *Retirement Security: Federal Action Could Help State Efforts to Expand Private Sector Coverage*. https://www.gao.gov/products/gao-15-556

[17] Small Nonprofit Retirement Security Act of 2024, S. 4965, 118th Cong. (2024).

buildings, or for those with ongoing accessibility costs for their audiences, the cost of ADA compliance can be significant.

While there are various ways to accomplish this work legislatively, policymakers would do well to build on the bipartisan model of current incentives by allowing these credits to be applied against payroll tax liability for nonprofit employers. Alternatively, nonprofit employers could be given the option to receive direct payment for the value of the credit.

The Tax Code Should Strengthen Nonpartisan Advocacy and Civic Engagement for the Nonprofit Sector

<u>Recommendation: Maintain the absolute prohibition on political campaign activity for 501(c)(3) nonprofit organizations</u>

A healthy nonprofit sector requires a healthy democracy. Because of their charitable mission and deep connection to those they serve, nonprofit organizations are uniquely positioned to help communities lift their voices and advocate for what they need most. In fact, voters who are contacted through nonpartisan civic engagement by nonprofit organizations are 10% more likely to vote than comparable voters who are not contacted.[18]

While there are many factors that contribute to this response, perhaps foremost among them is the nonpartisan nature of the outreach and the organization conducting it. In fact, since 1954, the definition of a charitable nonprofit organization has explicitly excluded any organization that would "participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office."[19] This prohibition is often referred to as the "Johnson Amendment" for its sponsor, then-Senator Lyndon Johnson (D-TX), although it cleared Congress without objection and was signed into law by President Dwight D. Eisenhower.

The prohibition on political campaign activity serves as a critical firewall, protecting the nonprofit sector from an often bitter and divided political landscape. Nonprofit organizations have an important role to play in bridging differences and bringing Americans together, but they cannot play this role effectively if they themselves are captured by political partisanship. Additionally, nonprofits would face major operational challenges if they were forced to choose between endorsing a candidate they believed would support their mission and a sitting elected official with sway over their budget. Regardless of their actions, perceptions of

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[18] Nonprofit VOTE (2024). *Nonprofit Power: Building an Inclusive Democracy*. https://www.nonprofitvote.org/wp-content/uploads/2024/03/2024-Nonprofit-Power-digital-edition.pdf

[19] Chapter 26, U.S. Code § 501(c)(3)

political partisanship would undercut nonprofits' trusted status and render much of their work more difficult or impossible. Simply put, eliminating or weakening the prohibition on political campaign intervention would represent an existential threat to the nation's nonprofit sector.

In addition to damaging the nonprofit sector, eliminating the prohibition on political campaign activity would further corrupt the American political system. Because contributions to charities are tax-deductible, this would effectively require the U.S. Treasury to subsidize political donations. This cost is not mere conjecture: In 2017, the Joint Committee on Taxation estimated that a proposed weakening of the "Johnson Amendment" would cost taxpayers $2.1 billion over the following decade.[20] This implies that at least $6 billion in otherwise taxable political campaign contributions would be converted into de facto tax-deductible campaign contributions. The right to free speech is enshrined in the U.S. Constitution, but there is no such right to tax-free speech.

<u>Recommendation: Consider opportunities to clarify or provide further guidance on what constitutes prohibited "political campaign intervention"</u>

In addition to preserving the firewall between charitable nonprofits and political campaigns, it is equally important that nonprofit organizations be engaged in the public policy process through permitted activities such as advocacy, lobbying, and nonpartisan civic engagement. Public policies designed without the input of nonprofits and the people they serve are less effective, and our democracy is less representative when nonpartisan civic engagement is curtailed.

As we noted in greater detail responding to a Ways and Means Committee request for information last year, [21] recently released research demonstrates an alarming decline in nonprofit organizations' engagement with public policy. In 2022, only 25% of organizations reported that they had ever communicated a position on legislation to policymakers, as compared to 74% that reported ever having done so in 2000. Regardless of whether they engaged with public policy or not, nonprofit organizations self-reported that "tax laws or IRS rules" were the single most discouraging factor influencing their decision about whether to engage.[22] This

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[20] Joint Committee on Taxation (2017). *Estimated Revenue Effects Of H.R. 1, The Tax Cuts and Jobs Act, As Ordered Reported By The Committee On Ways And Means On November 9, 2017*. https://www.jct.gov/publications/2017/jcx-54-17/

[21] Independent Sector (2023). *Response to August 14, 2023 Request for Information: Nonprofit Organizations and "Political Campaign Intervention."* https://independentsector.org/wp-content/uploads/2023/09/RFI-Response-Political-Campaign-Intervention.pdf

[22] Faulk, L. Kim, M., & MacIndoe, H. (2023). *The Retreat of Influence: Exploring the Decline of Nonprofit Advocacy and Public Engagement*. Independent Sector. https://independentsector.org/wp-content/uploads/2023/07/PENS-Advocacy-Report.pdf.

research is borne out by the experiences of Independent Sector, its members, and even IRS officials themselves in a recent Government Accountability Office (GAO) report.[23]

Independent Sector is proud to support the Nonprofit Stakeholders Engaging and Advancing Together (Nonprofit SEAT) Act (H.R. 3245), introduced by Rep. Nancy Mace (R-SC) and Rep. Betty McCollum (D-MN), and currently endorsed by nearly 700 nonprofit organizations across almost every state.[24] Section 10 of that legislation directs the GAO to issue a report to Congress on opportunities to clarify the difference between prohibited political campaign intervention and nonpartisan civic engagement for 501(c)(3) nonprofit organizations. We also encourage you to examine the Bright Lines Project — a nonpartisan initiative undertaken by a drafting committee of technical and legal experts — aimed at developing a framework of clear analytical steps that could be used by regulators and nonprofits alike.

The Tax Code Should Strengthen Governance and Trust in the Nonprofit Sector

Public trust is the currency of the nonprofit sector. Trust is essential for nonprofits to work with local communities, understand their needs, partner with government, recruit volunteers and donors, and so much more. For each of the past five years, Independent Sector has partnered with Edelman Data and Intelligence to survey the American public about their trust in nonprofit organizations — the largest nationally representative survey of its kind. The latest findings point to a divided nation and a nonprofit sector that is trusted above all others.[25]

While it may not be surprising to learn that people in the United States feel divided, the scale of that division is noteworthy: Fully 94% of respondents are worried about growing divisions and a lack of national unity. Yet, across 16 different industries and segments of society, there is one set clearly trusted above all others: nonprofit organizations. At +45, the net percentage of Americans who have high trust in nonprofit organizations to do the right thing far outpaces small businesses in second place at +21, to say nothing of corporations (-32), the news media (-37), or the federal government (-38).[26]

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[23] U.S. Government Accountability Office (February 2020). *Campaign Finance: Federal Framework, Agency Roles and Responsibilities, and Perspectives*, p. 42-43. https://www.gao.gov/products/gao-20-66r.

[24] Independent Sector (March 2023). *National and State Organizations Endorse the Nonprofit SEAT Act.* https://independentsector.org/resource/the-nonprofit-seat-act/.

[25] Independent Sector (June 2024). *Trust in Nonprofits and Philanthropy: Strengths and Challenges in a Time of Division*. https://independentsector.org/resource/trust-in-civil-society/

[26] *Trust in Nonprofits and Philanthropy*, page 17. Calculation of percentage of Americans rating low trust in organizations "to do what is right" subtracted from percentage rating high trust.

In addition to upholding the prohibition on political campaign intervention, policymakers have other key opportunities to strengthen governance and trust in the nonprofit sector.

Recommendation: Support IRS enforcement funding and tools to prevent abuse of the nonprofit sector

The nonprofit sector has grown in its importance to our society and our economy in recent years, but funding for the IRS Exempt Organizations (EO) Division has not kept up with this growth. From 2000 to 2013, the number of 501(c)(3) charitable organizations increased by more than 28%, while the number of full-time equivalent staff in the IRS EO Division increased by less than 6%. A 2020 Congressional Budget Office report found IRS appropriations had fallen by 20% in inflation-adjusted dollars since 2010, resulting in the elimination of 22% of its staff. The amount of funding allocated to oversight had declined by about 30% since 2010.[27] The American public in general — and donors and volunteers in particular — have a reasonable expectation that someone is on the watch for bad actors, and that those who exploit the nonprofit sector for their own personal gain will face consequences. Adequate resources and tools for regulators are essential to meeting this expectation.

Recommendation: Immediately rescind Form 1023-EZ and work with stakeholders to replace it

Amidst congressional scrutiny and budgetary pressures, the IRS released a dramatically simplified application for 501(c)(3) status in 2014, Form 1023-EZ. Numerous analyses and reports from the IRS's own internal watchdogs have demonstrated that this form simply does not collect enough information to allow for adequate determination of eligibility. For example, the Taxpayer Advocate Service studied a representative sample of approved Form 1023-EZ applicants in 2017, finding that an astonishing 42–46% of approved applicants did not meet one of the tests for qualification.[28] When the Treasury Inspector General for Tax Administration submitted 1023-EZ applications for five entirely fictitious organizations as part of a 2022 audit, four were approved.[29]

[27] Congressional Budget Office (July 2020). *Trends in the Internal Revenue Service's Funding and Enforcement*. https://www.cbo.gov/system/files/2020-07/56422-CBO-IRS-enforcement.pdf

[28] National Taxpayer Advocate (2017). *Annual Report to Congress, 2017*. Most Serious Problems Encountered by Taxpayers, item 5. https://www.taxpayeradvocate.irs.gov/reports/2017-annual-report-to-congress/full-report/.

[29] Treasury Inspector General for Tax Administration (2022). *More Information is Needed to Make Informed Decisions on Streamlined Applications for Tax Exemption*, Report Number 2023-10-001. https://www.oversight.gov/sites/default/files/upload-reports/202310001fr.pdf.

The continued existence of this blatant mechanism for fraud is deeply concerning and hurts public trust in the nonprofit sector. As in Section 9 of the Nonprofit SEAT Act (H.R. 3245), we urge Congress to immediately rescind Form 1023-EZ and to work with the nonprofit sector and state charities regulators to replace it.

<u>Recommendation: Craft any policies intended to “reform” the nonprofit sector with those who will be impacted by them</u>

We are well aware that there are various proposals from policymakers, academics, and others to change laws or regulations governing nonprofit organizations with the stated intention of preventing abuse, ensuring funds are put to best use, or any number of other laudable goals. Independent Sector believes that sensible reforms to appropriate laws and regulations could strengthen the nonprofit sector by bolstering the public’s trust. However, we are equally wary of those attempting to bend nonprofit organizations to their own perspective or purpose under the guise of “reform.” Independent Sector approaches 2025 as a good faith partner willing to work with anyone who seeks a healthier, more trusted nonprofit sector. It is essential that any reform policies be developed in consultation with a broad cross-section of nonprofit sector organizations.

Conclusion

Again, while every year is a critical one for the work of the nonprofit sector, we know that 2025 will be particularly important for the tax code and its impact on these vital organizations’ ability to serve communities across the nation. We appreciate the opportunity to provide this input and look forward to working with you toward a stronger nonprofit sector and a thriving nation.

Akilah Watkins

Dr. Akilah Watkins
President & CEO