



January 23, 2018

To: Senator Michael D. Brady, Chair
Representative Jay R. Kaufman, Chair
Joint Committee on Revenue

From: Jim Klocke, CEO, Massachusetts Nonprofit Network

Re: Testimony - Federal Tax Changes Informational Hearing

Chairman Brady, Chairman Kaufman, and members of the Joint Committee on Revenue, thank you for the opportunity to testify on the newly passed federal tax legislation and its potential impact on the Massachusetts nonprofit sector.

My name is Jim Klocke and I am the CEO of the Massachusetts Nonprofit Network (MNN). MNN is the voice of the nonprofit sector and a statewide organization that brings together all parts of the nonprofit ecosystem—nonprofits, funders, community and business leaders, and elected officials—to strengthen nonprofits and represent them on critical issues. MNN has over 800 members, representing nonprofits in every region of the state and from all subsectors of the nonprofit world.

Simply put, the federal tax bill will make it harder for all types of Massachusetts nonprofits to operate - small, medium, and large alike. As detailed below, the federal tax bill will reduce charitable giving, impose new taxes on the sector, and will negatively impact the Commonwealth's nonprofit community and the people and causes they serve.

With this testimony, I aim to provide context on the Commonwealth's nonprofit sector, highlight particular pieces of the federal tax bill which will be harmful to the sector, and to share ideas and identify potential ways in which the state and nonprofit sector can continue to be partners.

Background on Massachusetts Nonprofit Sector:

The Massachusetts nonprofit sector enriches communities and provides vital services. From scholarships for local students, to free and subsidized health care, to a wide array of environmental, artistic, historic, and cultural programs, nonprofits make immense contributions that benefit residents and government alike.

In addition, the Commonwealth's nonprofit sector has an economic reach that can be felt across the state. With over 540,000 jobs, the nonprofit sector employs more than 17% of the state's workforce, making Massachusetts the 6th largest nonprofit employer in the nation. With over \$30 billion in wages generated by nonprofits, the economic impact of the sector produces billions of dollars of income, sales, and tax revenues annually for the Commonwealth.

As for financial support of the nonprofit sector, while private and government support is critical, individual donations are the most common type of funding among Massachusetts nonprofits. In our last MNN member survey, 82% of our members reported relying upon individual donations, a percentage higher than those for foundation, corporate or government support.

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Federal Tax Reform and the Massachusetts Nonprofit Sector:

The federal tax reform bill presents many challenges for the nonprofit sector, most notably:

1. **Doubling of the Standard Deduction:** While the federal tax bill kept the charitable tax deduction intact, it dramatically increased the standard deduction, to \$12,000 for individuals and \$24,000 for couples. Doubling the standard deduction will significantly reduce the percentage of taxpayers who itemize. In terms of impact in Massachusetts, prior to the tax reform bill, roughly 1 million filers in Massachusetts itemized their charitable deductions, accounting for \$5.7 billion in charitable contributions. Recent estimates conclude that now only 5% of filers will itemize, resulting in \$275 million fewer dollars to fund communities and people in need.

National studies have estimated that these changes will reduce giving by \$13 to \$20 billion annually, with our own study predicting it will reduce giving in Massachusetts by over \$500 million per year. In essence, the doubling of the standard deduction, combined with the \$10,000 cap on any itemized deductions for state and local taxes, will make charitable giving more expensive for large numbers of middle- and upper-middle income households earning less than \$200,000 a year. As a result, an unintended consequence of doubling the standard deduction is to turn the charitable tax deduction into a tax benefit for only the wealthiest households.

2. **Estate Tax:** The federal tax bill maintained the estate tax, but doubled the exemption to about \$11 million for individuals and about \$22 million for couples, expiring after 2025. The estate tax is an important source of funding for nonprofits and foundations; it encourages donors to address future needs in their communities through estate planning. It is estimated that doubling the exemption for the estate tax will reduce federal revenues by nearly \$100 billion over 10 years and lower charitable giving by \$4 billion annually.
3. **Nonprofit Specific Taxes:** To pay for some of the tax cuts, the federal tax bill creates a new 1.4% excise tax on net investment income of nonprofit colleges and universities with assets of at least \$500,000 per full-time student and more than 500 full-time students. This provision will impact many of the Commonwealth's universities. The bill also institutes a new 21% excise tax on compensation above \$1 million or more paid to a nonprofit's five highest-paid employees. Finally, it changes the unrelated business income taxes (UBIT) by requiring that nonprofits calculate their taxes on each trade or business separately, rather than on aggregate profits and losses of all entities as under current law. As a result, some nonprofits will face significant new costs that take resources away from mission-related services and programs.
4. **Impact to the Federal and State Budget:** It is estimated that the tax bill will increase the federal deficit by more than \$100 billion per year for the next 10 years. Congressional leaders have already signaled a desire to curb funding for key programs such as Medicaid, Medicare, Social Security, and the Children's Health Insurance Program. This will put pressure on states, including the Commonwealth which depends greatly on federal revenues. If constrained federal revenues results in spending cuts at the state and local level, the revenue and resources that nonprofits depend on to provide services could be reduced at the very same time human needs are increasing.

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Opportunities Moving Forward:

1. **Federal Universal Charitable Tax Deduction:** In our work on federal tax issues MNN, along with a national coalition of partners, has advocated for a universal charitable tax deduction. We do so because while effective and important, the current federal charitable tax deduction is not available to a majority of the 103 million federal tax paying Americans who do not itemize their taxes. This makes the incentive to give dependent on income levels.

A recent study looking at the doubling of the standard deduction and its impact on charitable contributions also researched what, if any, new giving would result from a universal charitable deduction. This study found that giving would increase at all income levels – in low- and middle income households by as much as 8.4%, and in high income households by as much as 1.6%. In addition, a universal charitable tax deduction would only reduce federal tax revenues by 0.5%. MNN will continue to work with our federal delegation to push for a universal charitable tax deduction.

2. **State Charitable Tax Deduction:** In 2000, Massachusetts voters approved a ballot petition creating a state income tax deduction for charitable contributions. Unlike the federal deduction, a Massachusetts taxpayer could take advantage of the deduction even if he or she did not itemize their deduction on their federal income tax return (similar to the universal charitable tax deduction). This deduction was in effect for one year before it was suspended by the Legislature. Under current law, the states' charitable deduction is not slated to return until a fiscal year after the state's income tax rate drops to 5%. While this is years down the road, it is important to note in the current debate.
3. **Continued collaboration:** MNN is aware that many of the fiscal challenges the federal tax legislation presents to nonprofits are similar to fiscal challenges the state may face. Nonprofits work collaboratively with governments at all levels each day. We hope to continue to work together to ensure that the federal tax bill does not dramatically and unfairly impact local communities and the people that rely on the programs and services provided by our government and nonprofit sectors.

Mr. Chairmen and Committee members, on behalf of the members of the Massachusetts Nonprofit Network and nonprofits throughout the Commonwealth, thank you for the opportunity to testify today. I'm happy to answer any questions committee members might have. As always, we appreciate your continued support of the nonprofit sector.