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The Art Market Adjusts: Charitable donation incentives under the CARES Act

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In the wake of COVID-19's spread, we have seen many museums temporarily closing their doors to the public and canceling long-planned fundraising events. As it is no secret that many museums in the U.S. already operate on tight budgets, the long-term impact of such closings on these institutions has been on the minds of many in the art world. On last week's edition of its podcast, Artnet referenced the National Center for Art Research's finding that the average museum in the US has thirteen months of cash reserves, meaning that the average museum in the United States can only operate for thirteen months without additional revenue; however, this number is heavily skewed by a few well-capitalized museums. According to the National Center for Art Research's findings, the median museum in the United States has approximately only two months of cash reserves on hand. As the current situation continues to unfold, it seems increasingly likely that museums will be closed for that long or longer. And, once re-opened, museums may be slow in ramping back up to their prior levels of revenue as people re-acclimate to gathering in large groups and in public spaces. In light of the uncertainty caused by the unfolding epidemic for the futures of many museums, it therefore may be reassuring for museum-goers to know that Congress has passed temporary measures to encourage cash donations to public charities, such as museums, for 2020. So please support your local museums!

In this conversation, my colleagues Paul Roy and Sarah Verano discuss the CARES Act and its impact on charitable giving in 2020.

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Sarah: It's been reported that cultural institutions in major cities are projecting shortfalls in revenue due to the shut-downs necessitated by the spread of COVID-19. Museum supporters in a position to provide monetary assistance to affected institutions should therefore take note that the CARES Act includes provisions which provide temporary tax benefits to those making charitable contributions. These benefits are also more accessible to donors than we have seen in the past several years. Paul, would you be able to explain why, practically speaking, most individual taxpayers making small charitable contributions typically do not receive a tax benefit when making a charitable contribution?

Paul: Because the charitable contribution deduction is a "below-the-line" deduction, a taxpayer can only receive the benefit of the deduction if the taxpayer chooses to itemize deductions rather than to take the standard deduction. Itemizing only makes sense if the value of the itemized deductions exceeds the value of the standard deduction, which is currently quite high ($12,200 for individuals or $24,400 for married couples). Before the Tax Cuts and Jobs Act of 2017, many people used to itemize their deductions, in large part because at that time there was no cap on the deduction of state income tax. Now, unless a taxpayer is making a particularly large charitable gift, it often will not make sense to itemize deductions, and, in such case, the taxpayer will receive no tax benefit from making the charitable contribution.

Sarah: How does the CARES Act change this for 2020?

Paul: Individuals who do not itemize deductions will be allowed an "above-the-line" charitable contribution deduction of up to $300 for gifts of cash to public charities made in 2020. Presumably, non-itemizing individuals filing a joint return will be allowed a $600 combined deduction. This change will permit taxpayers making relatively small charitable contributions to reap a tax benefit from such donations in 2020.

Sarah: Are there any benefits included in the CARES Act for individuals who do itemize their deductions?

Paul: Individuals who itemize deductions may elect to ignore the normal adjusted gross income ("AGI") limits for gifts of cash made to public charities in 2020. This essentially means that a 100% of AGI limitation will apply instead of the usual 50% or 60% limitation for such cash contributions. Gifts of cash in excess of 100% would be eligible for the normal 5 year carryforward rule for 2021 and later years subject to the usual 50% or 60% AGI limit applicable for 2021 and future years . However, carryforwards of cash contributions from years prior to 2020 will not be eligible for the 100% of AGI limit in 2020. They will however be allowed in 2020 to the extent of the normal carryover rules, generally 50% or 60% of AGI.

Sarah: Are there any benefits for entities that may be considering making charitable contributions?

Paul: In the case of gifts from a pass-through entity such as a partnership or "S" Corporation, the election to disregard the normal AGI limits for cash contributions will be made at the individual shareholder or partner level. "C" Corporations will be able to deduct up to 25% (rather than the normal 10%) percent of their net income for cash distributions made to public charities within their taxable years beginning in 2020. The same carryforward restriction applicable to individuals will apply to corporations with carryover charitable contributions from 2019 and prior years and with respect to carryforwards into 2021 and future years. That is, the 10%, not the 25%, of net income limit will apply to such carryforwards.

Sarah: What is considered a public charity for purposes of the CARES Act?

Paul: This temporary change in charitable deduction rules for individuals and corporations only applies to cash gifts to public charities. For this purpose, donor-advised funds (DAFs) and supporting organizations do not qualify as public charities, but operating foundations and certain other foundations, including pass through foundations and pooled common funds, will qualify for this purpose. Non-cash contributions can still be made to public and non-public charities subject to the normal AGI limits.

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