



WINTER 2020

# PERCSPECTIVES ON RESEARCH

## TAX PRICES AND CHARITABLE GIVING: PROJECTED CHANGES IN DONATIONS UNDER THE 2017 TAX CUTS AND JOBS ACT

The Tax Cut and Jobs Act of 2017 made significant changes to the rate structure of the Internal Revenue Code of the United States. One of the many activities potentially affected by this change in marginal tax rates – and specifically, the near-doubling of the standard deduction – is charitable giving. Since the Act increases the standard deduction, some taxpayers who normally itemize their tax returns – and receive the benefit of deducting the amount given to charitable institutions – are expected to switch to the now-raised standard deduction.

Without the added tax deduction from those taxpayers who switch to the standard deduction, many have asserted that charitable giving would be diminished. Indeed, recently-released aggregate data does indicate a decline of 3.4 percent in giving by individuals in 2018, although, it is difficult to attribute this decline directly on the changes made through the Tax Cuts and Jobs because of other economic conditions and incentives to shift giving into the 2017 tax year.

In PERC working paper 1917, PERC Professor Jonathan Meer and co-author Benjamin Priday provide updated estimates of the tax price elasticity of charitable giving using data from the Panel Study of Income Dynamics. The authors apply these estimates to the provisions of the Tax Cut and Jobs Act of 2017 and use the data to predict the Act's effects on charitable giving. The paper also examines the marginal likelihood to donate from income.

Prior to the Tax Cuts and Jobs Act, the deduction for charitable giving reduced federal income tax revenue by approximately \$57 billion, with about 70 percent of that benefit accruing to households earning over \$200,000 per year.

By reducing marginal tax rates by 1 to 4 percentage points, the Tax Cuts and Jobs Act increases the tax price of giving for those who itemize their deductions. For those households, each dollar donated to a qualifying charity reduces their taxable income by one dollar and lowering their tax liability by their marginal tax rate. The Act lowered tax liability for about 80 percent of households, with an average reduction of about \$1,600 for all tax units. The increase in disposable income is likely increase giving to some degree, offsetting some of the reduction due to an increase in the tax price.

Previous academic research has focused on the direct impact of a change in the tax price of giving, holding all else constant. But a full accounting of the impact of the Act on giving should include this increase in disposable income. More importantly, though, the increase in the standard deduction means that far fewer households are expected to itemize, thus eliminating the direct tax incentive to make a charitable donation.

Because of the large number of households that

“...The increase in the standard deduction means that far fewer households are expected to itemize, thus eliminating the direct tax incentive to make a charitable donation.”

make no donations, the authors separately estimate the likelihood of giving and the amount given conditional on making a donation using fixed effects models and combine these estimates for an overall effect on donations.

Since those who donate large amounts may lower their marginal tax rates, estimates are provided for what the household's price of giving would have been without any donations and used as a proxy for the actual price of giving. Although the survey data does not include many very high earners, who make a large proportion of charitable donations, the authors apply their estimates to data from the Internal Revenue Service Statistics of Income to indicate the expected effects on these high-earning households.

Findings show that charitable giving is responsive to tax incentives and predictions estimate significant reductions in charitable giving, primarily arising from the reduction in the number of households that itemize their deductions. A 10 percent increase in the price of giving is expected to reduce giving by

10.7 percent, though effects are smaller for those who continue to itemize their tax returns. The marginal tendency to donate is small and, for most households, the size of the increase in disposable income from the Tax Cuts and Jobs Act is sufficiently low that it only slightly affects the overall estimates.

Given that the Act is expected to significantly change itemizing behavior, the results are estimated separately for households that always itemize and those that switch between using the standard deducting and itemizing; findings show that those that switch tend to be more sensitive to the tax price. Results also show latent effects, which suggests that taxpayers take some time to adjust their giving to changes in the tax code.

Evidence also shows that taxpayers take at least several years to fully respond to changes in the tax price of giving. To the extent that charitable giving is habit-forming, and that changes to incentives to give through one form of philanthropy alter giving to others, the ripple effects of the law may take years to fully develop.

---

## THE EFFECTS OF MANDATORY ENERGY EFFICIENCY DISCLOSURE IN HOUSING MARKETS

---

Government-mandated information disclosure is increasingly used as a policy intended to improve the ability of consumers to make the best possible decisions in the face of imperfect information about the quality of a product. Policymakers view disclosure requirements as a low-cost and less-intrusive means of improving market efficiency compared to alternative forms of regulation. As a result, such requirements are a significant policy component in many economic sectors including health care, education, and finance.

One setting where mandated disclosure plays a crucial role is investment in energy efficiency in housing markets. With prominent research gilding energy efficiency plans as substantial forms of investment that would pay for themselves within a short period of time, many European countries, as well as many states and municipalities in the U.S., have enacted mandatory residential energy audit and disclosure requirements. The success of these

audits and disclosures depend on their ability to provide cost-effective opportunities to improve energy efficiency that are not being taken advantage of in the current market.

In PERC working paper 1916, Steven Puller, the PERC Professor of Free Enterprise, along with coauthors Erica Myers and Jeremy West investigate the market frictions that contribute to underinvestment in energy efficiency in the housing market in Austin, Texas. The authors also study whether these audit and disclosure policies have the intended effect of improving the energy efficiency quality of homes. To establish the market frictions at play, the authors study whether the cause is behavior/information-driven or due to a failure to realize energy savings from engineering projections.

With behavior/information-driven market frictions, mandatory audits and disclosures benefit home buyers by providing information on the quality of energy efficiency of a home that was previously

“...Homeowners’ ignorance about their own energy efficiency is a market failure that disclosure policies can help to ameliorate.”

undisclosed or lacking entirely. In this scenario, as homeowners invest in energy saving products in order to be competitive, overall product quality would also increase.

In contrast, the perceived under-investment in energy efficiency could be attributed to a lack of realized savings from the products themselves. In this case, mandatory audits and disclosures would be largely ineffective. In theory, mandatory disclosure should improve the quality of goods and services by correcting for information-related market failures. In practice, previous literature finds little evidence that supports the efficacy of disclosure programs at improving market outcomes.

The city of Austin enacted the Energy Conservation Audit and Disclosure ordinance in 2009. The ordinance stipulates the home sellers must provide a standardized report of a certified technical audit of their properties’ energy efficiency to prospective buyers. This paper tracks the effects of Austin’s disclosure program by comparing homes sold in Austin to similar homes located just outside the city limits but are sold on the same real estate market and serviced by the same energy utility company.

The authors estimate the effects of the disclosure program on the capitalization of energy efficiency on home prices and on homeowner’s decisions to invest in energy efficiency using a panel fixed effect model that controls for local housing market shocks. Property-level data on housing transaction prices, electricity bills, energy efficiency program participation, and technical data from ordinance reports are compiled, then homes are selected for comparison that are similar in relevant attributes and that show similar trends for outcomes of interest before the ordinance was passed.

Findings show that encouraging home sellers to provide potential buyers with certified energy audits increases price capitalization of energy efficiency and leads to quality-improving residential investments in energy-saving technologies.

Although mandatory, the authors found that only 60 percent of targeted homes comply with the disclosure ordinance. Despite substantially larger expected price premiums from the disclosure from more efficient homes, the evidence shows that properties’ relative energy efficiency only weakly predicts whether or not sellers choose to disclose this information. This weak relationship is not due to buyers or realtors dictating compliance by asking sellers to provide audits, rather than by home sellers making the decision.

Given the estimated capitalization effects, the authors attribute this relationship to a significant share of homeowners being ignorant about the relative energy efficiency of their own homes. The homeowners’ ignorance appears to be a significant factor for why the voluntary disclosure of information that would improve the market does not occur where there is not a mandated policy in place.

These findings have important policy implications. This paper suggests that homeowners’ ignorance about their own energy efficiency is a market failure that can be mitigated by enacting disclosure policies. The capitalization findings indicate that home purchasers do understand and care about residential energy efficiency information when it is made available. Therefore, mandatory disclosure may improve overall quality by creating stronger incentives to invest in energy efficiency. Also, disclosure policies encourage homeowners to get energy audits that can then increase participation in energy efficiency incentive programs.

This study is one of the first of its kind to provide empirical evidence of the quality-improving effects of a mandatory disclosure policy in a peer-to-peer market. Market outcomes were improved by government intervention via mandated disclosures because both home buyers and sellers were uninformed about energy efficiency. This is likely to be found to be true in other peer-to-peer markets where strong assumptions, like that home sellers are informed and that information on quality is publicly available, do not hold and a mandatory disclosure policy would improve overall market quality.



**PRIVATE ENTERPRISE  
RESEARCH CENTER**  
TEXAS A&M UNIVERSITY

Texas A&M University  
4231 TAMU  
College Station, TX 77843-4231

NONPROFIT ORG.  
U.S. POSTAGE  
**PAID**  
COLLEGE STATION,  
TEXAS 77843  
PERMIT NO. 215

# PERCSPECTIVES ON RESEARCH

WINTER 2020

Founded in 1977 through the generosity of former students, corporations and foundations, the Private Enterprise Research Center pursues a dual mission of supporting academic research at Texas A&M University and developing market-oriented solutions to public policy problems.

PERCspectives on Research newsletters are not copyrighted and may be reproduced freely with appropriate attribution of source.

The opinions expressed in PERCspectives on Research are those of the authors and not necessarily those of Texas A&M University.

## CONTACT

Private Enterprise Research Center  
Texas A&M University  
4231 TAMU  
College Station, TX 77843-4231  
(979) 845-7559  
[perc@tamu.edu](mailto:perc@tamu.edu)



**PRIVATE ENTERPRISE  
RESEARCH CENTER**  
TEXAS A&M UNIVERSITY

For archived newsletters, visit  
[perc.tamu.edu](http://perc.tamu.edu)