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Revenue and Transportation Interim Committee

62nd Montana Legislature

TO: Revenue and Transportation Interim Committee

FROM: Megan Moore, Legislative Services

RE: SJR 23: Analysis of Limiting Exemptions to Ratio of Donations to Gross Receipts

DATE: April 17, 2012

The Senate Joint Resolution 23 (SJR 23) study of tax exemptions for nonprofit organizations requests an analysis of the impact of limiting income and property tax exemptions for nonprofits to reflect charitable donations compared with other sources of revenue. The ratio of donations to total revenue varies by the type of nonprofit organization. The following table provides data on contributions, gifts, and grants by type of organization and compares those amounts to total revenue for Montana organizations.[1]

Contributions and Total Revenue for Montana Nonprofits, FY 2009

Organization Type	Number	Contributions, Gifts and Grants	Total Revenue	Contributions as % of Total Revenue
Arts, culture and humanities	188	$25,628,852	$48,303,887	53.1%
Education - higher	10	$66,624,316	$154,680,876	43.1%
Education - other	231	$62,588,568	$177,136,110	35.3%
Environment	164	$40,362,150	$63,836,589	63.2%
Health - hospitals	43	$31,754,208	$2,127,090,753	1.5%
Health - other	171	$86,724,857	$331,110,354	26.2%
Human Services	698	$265,762,339	$568,307,164	46.8%
International	23	$20,004,464	$22,052,593	90.7%
Mutual Benefit	2	$32,340	$363,046	8.9%
Other public & societal benefit	224	$86,528,843	$147,864,092	58.5%
Religion	59	$17,204,021	$36,432,435	47.2%

Contributions, gifts, and grants as a percentage of total revenue varies considerably by type of organization from a low of 1.5 percent for hospitals to a high of nearly 91 percent for International organizations.

Limiting the Exemption

[1] Data gathered from the National Center for Charitable Statistics, available from http://nccsdataweb.urban.org/tablewiz/pc.php.

One way to model limiting tax exemptions for nonprofits is to use the percentage of contributions, gifts, and grants as a percent of the total revenue by category as the benchmark for a complete exemption from the income and property tax. A nonprofit with less than the percent for the category could qualify for a portion of the exemption based on the ratio of donations to total revenue for its category. An example using the Arts, culture, and humanities category follows. The "Revenue from Donations" column shows four different levels of donations that correspond with 25 percent, 50 percent, 75 percent, and 100 percent of the 53 percent donations as a portion of revenue for the whole category. The table shows the value of the full exemption and how much organizations with donations at different levels might pay in property and corporate taxes based on the model. Taxes are calculated using a 2.63 percent commercial property tax rate and 540.84 mills (the 2010 average) and the 6.75 percent corporate tax rate.

The full exemption values and payments based on donations for the other categories of organizations

Organization Type	Revenue from Donations	Percent of Exemption	Value of Commercial Property	Full Property Exemption	Property Payment Based on Donations	Revenue Less Expenses	Full Income Exemption	Income Payment Based on Donations
Arts, culture and humanities	13%	25%	$500,000	$7,112	$5,334	$100,000	$6,750	$5,063
Arts, culture and humanities	27%	50%	$500,000	$7,112	$3,556	$100,000	$6,750	$3,375
Arts, culture and humanities	40%	75%	$500,000	$7,112	$1,778	$100,000	$6,750	$1,688
Arts, culture and humanities	53%	100%	$500,000	$7,112	$0	$100,000	$6,750	$0

would be the same but the revenue from donation amounts would differ by category and are presented below.

Organization Type	Revenue from Donations	Percent of Exemption
Education - higher	11%	25%
Education - higher	22%	50%
Education - higher	32%	75%
Education - higher	43%	100%
Education - other	9%	25%
Education - other	18%	50%
Education - other	27%	75%
Education - other	35%	100%
Environment	16%	25%
Environment	32%	50%
Environment	47%	75%
Environment	63%	100%
Health-hospitals	0.37%	25%
Health-hospitals	0.75%	50%
Health-hospitals	1.12%	75%
Health-hospitals	1.49%	100%

Organization Type	Revenue from Donations	Percent of Exemption
Health - other	7%	25%
Health - other	13%	50%
Health - other	20%	75%
Health - other	26%	100%
Human Services	12%	25%
Human Services	23%	50%
Human Services	35%	75%
Human Services	47%	100%
International	23%	25%
International	45%	50%
International	68%	75%
International	91%	100%
Mutual Benefit	2%	25%
Mutual Benefit	4%	50%
Mutual Benefit	7%	75%
Mutual Benefit	9%	100%
Other public & societal benefit	15%	25%
Other public & societal benefit	29%	50%
Other public & societal benefit	44%	75%
Other public & societal benefit	59%	100%
Religion	12%	25%
Religion	24%	50%
Religion	35%	75%
Religion	47%	100%

Impacts

The impacts from limiting income and property tax exemptions to donations as a percentage of total revenue are difficult to quantify. Effects could include increased property and income tax revenue, decreased property tax and business equipment tax bills for taxpayers that are not nonprofits, added costs for nonprofit organizations, and/or decreased services for recipients of nonprofit services.

Section 15-10-420 limits governmental entities to imposing the number of mills required to generate the amount of property tax assessed in the prior year using the taxable value for the current year plus an inflation factor equal to one-half of the average rate of inflation over the previous 3 years. Newly taxable property is excluded from the taxable value in the current year. Section 15-10-420(3)(a)(v) describes newly taxable property to include the transfer of property from tax-exempt to taxable status. If property tax exemptions for nonprofits were limited based on the amount of donations, the property subject to taxation would be considered newly taxable property. A government entity could continue to levy the same level of taxes (with an increase for the inflation factor) and collect additional revenue from the property transferred from tax-exempt to taxable status. The government entity could also choose to reduce property taxes and keep the revenue constant, or do some combination of the two.

Limiting the income tax exemption for nonprofits could increase corporate tax collections and lead policymakers to consider lowering other taxes over time. While this impact is not easy to quantify, there is a more direct effect stemming from recent changes to the business equipment tax. Senate Bill No. 372 (2011) lowered the business equipment tax rate from 3 percent to 2 percent for the first $2 million of taxable market value. The bill also added a provision for lowering the rate further, to 1.5% for the first $3 million of taxable market value, if individual income tax and corporate income tax collections exceed the revenue collected in the previous year by more than 4 percent. Requiring nonprofit organizations to pay corporate tax based on their levels of donations could contribute to an increase in income tax collections. If the increase is more than 4 percent above the previous year, the business equipment tax rate would decrease.

Nonprofit organizations that see their income and property tax exemptions limited based on the amount of donations they receive will face increased operating costs. The increased costs could lead to cuts in programs and services or depletion of reserves. These organizations might seek additional funding from individual donations or grants from other charitable organizations or the government. (An increase in donations could make the organization eligible for a larger exemption in the future.)

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