Taxpayers are, for the most part, philanthropic. Americans contributed more than $200 billion to nonprofit groups in 2005 (Feuerherd, 2006). While only about one-third of taxpayers itemize deductions on their annual federal tax returns, approximately 90 percent of taxpayers with incomes of $100,000 itemize (Herman, 2006).

Most taxpayers agree that, for many tax issues, the Internal Revenue Code (Code) is incomprehensible and complex. Taxpayers often do not understand whether a Code provision applies to their situation, how or when to report an item, or what amount to report. Unfortunately, provisions relating to charitable contributions are some of the most complex in the Code. Even for simple cash gifts, taxpayers must maintain adequate records, including a cancelled check, bank record or receipt from the donee organization showing the name of the charity along with the date and amount of the contribution. In addition, taxpayers must determine when and for how much the contribution is deductible. For example, a check written to a charity on December 31 2008, but not mailed until January 2, 2009 is not deductible until 2009. If the check is, for example, a contribution to a fund-raising event that includes a dinner, the fair market value of the dinner is not deductible.

A charitable contribution to an educational institution would seem to be a fairly straightforward deduction since most educational institutions are qualified charitable
organizations. Generally, this deductibility is the case. However, taxpayers donating to colleges and universities often specify where and how their donation is to be used. The athletic department, sometimes via an athletic foundation, is a popular beneficiary of charitable gifts from university alumni and fans.

A 2005 study identified several motivations for supporting college athletics: (1) desire to improve and support the program, (2) desire to receive ticket benefits, (3) desire to help student athletes, (4) desire for enjoyment or entertainment and interest, and (5) desire to support or promote the university (Gladden, et al., 2005). Donations to athletic booster clubs or athletic foundations often come with various benefits offered at different levels of giving. In the above-mentioned study, some donors used the terms “extortion” and “coercion” to describe their feelings toward having to donate to athletics in order to receive ticket benefits (Gladden, et al. 2005).

Whether the motive for giving to a college athletic program is enjoyment, desire to help students, or strictly to be able to purchase tickets, lawmakers have not been so charitable when it comes to the amount a taxpayer can deduct on his or her tax return. When the donation provides the taxpayer with ticket rights, the Code contains a provision that may limit a taxpayer’s deductable amount.

The purpose of this article is to present the findings of a preliminary investigation into the compliance with provisions in Code Section (§) 170(l) regarding treatment of amounts paid to institutions of higher learning, specifically when the contribution allows for the right to purchase athletic tickets. The remainder of the paper is presented as follows. The next section discusses contributions to athletics with the right to purchase tickets. Next, the results of the preliminary study of universities’ disclosure policies regarding the limitation on the tax deductibility of
contributions containing the right to purchase tickets are presented. A discussion of the effects of overstated deductions is followed by concluding remarks.

**Contributions with the Right to Purchase Athletic Tickets**

Athletic events are something taxpayers can enjoy from the sidelines. Some fans feel a part of the team, even as spectators. Contributions to athletic departments or booster clubs often include benefits such as preferred parking, free or reduced-price tickets, clothing, or other advantages such as invitations to post-game or half-time events. These perks are designed to provide extra incentive for supporting the athletic program. Although universities are not-for-profit organizations, raising revenue is crucial to athletic departments (Dochterman, 2008). University athletic programs may disclose in their promotional materials that the value of the benefits received, based on a good faith estimate, is not tax deductible. However, anecdotal evidence suggests that they may not be prone to specify that only a portion of a contribution, after subtracting a good faith estimate of benefits received, is deductible if the taxpayer receives the right to purchase tickets for seating at an athletic event. Even if a taxpayer chooses not to purchase tickets, only a portion of the contribution is deductible. Unfortunately, this misrepresentation and easily overlooked exception to the rule leads to repeated tax noncompliance. This noncompliance adds to the increasing federal tax gap (the difference between what taxpayers actually pay and what they should pay.)

Under Code § 170 (a) (1), the general rule for charitable contributions is that a deduction is allowed for any charitable contribution where payment is made within the taxable year. In order to qualify as a charitable contribution, the donation must be made to a qualifying charitable organization (i.e., the organization has tax-exempt status). Code § 501 includes several characteristics that tax-exempt organizations share. First, the organization must serve some type
of common good. Second, the organization must not be a for-profit entity. Third, net earnings may not inure to the benefit of any private shareholder or individual. Fourth, the organization cannot attempt to exert political influence. When donating to a college or university, the donation is generally qualified under §501(c)(3) which lists “corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literacy, or educational purposes …” as all being qualifying for tax exempt status.

Two major exceptions to the deductibility of charitable contributions apply to universities. One exception deals with contributions where benefits or privileges are received. In this situation, the deductible amount is limited to the portion that exceeds the fair market value of the financial or economic benefit received as a result of making the contribution. Another exception is found in Code § 170 (l) which disallows deductions, in certain cases, paid to or for the benefit of institutions of higher education. If the taxpayer receives (directly or indirectly), as a result of making the contribution, the right to purchase tickets for seating at an athletic event, then the deductible portion of the contribution is limited to 80 percent. Code § 170(l)(2)(B) states “…if a payment is for the purchase of such tickets, such portion and the remaining portion (if any) of such payment shall be treated as separate amounts…” That is, if a taxpayer makes a payment to an institution of higher education, and a part of the payment is for tickets to an athletic event, the fair market value of the tickets is not deductible and only 80 percent of the remaining contribution is deductible. If the taxpayer’s payment includes only the right to purchase tickets, still only 80 percent of the contribution is deductible.

University fund-raisers walk a fine line in promoting that donations are deductible and disclosing that if benefits are provided, the fair market value of those benefits are not deductible.
In addition, fund-raisers should inform donors that, even if no benefits are received, if the contribution gives the taxpayer the right to purchase tickets, then only 80 percent of the payment is deductible. Unfortunately, one might assume that most university fund-raisers are more educated in marketing techniques than in tax accounting. Therefore, a preliminary study was conducted to ascertain the extent and accuracy of disclosure made by college athletic fund-raising promotional information. The motivation for this study was because the authors, having a certain level of tax expertise, noticed that printed promotional material from a university indicated that two free tickets would be provided with a donation of a certain amount. The material also indicated that contributions would be deductible with no mention of any reduction for the tickets or for the right to the tickets. As explained above, if a contributor itemizes deductions and deducts the entire amount of the payment, he or she is in clear violation of the Code § 170(l) rules.

**Preliminary Study Results**

Now the question arises, do college athletic programs mislead taxpayers about the amount they can legally deduct? In order to answer this question, this preliminary study investigated seventeen schools in one NCAA Division II conference. The conference was chosen because the researchers were familiar, in general, with the universities in the conference and information about giving to the athletic programs was easily obtained. Each of the universities had a website and a link to athletics. A Division II conference was assumed to be large enough to have experts available to insure the accuracy of promotional information (i.e., university legal counsel or athletic director with knowledge of rules for donations). The data gathered was obtained from university athletic program websites, printed promotional material and phone calls to athletic directors’ offices. Of the seventeen conference schools, ten offered
the right to purchase tickets with a donation. As stated earlier, donors are subject to an 80 percent limitation of the donation after any other benefits received have been subtracted. Based on information received via phone calls or websites, seven of the ten (70 percent) misstated the tax deduction rules.

One of the three schools that did not misstate the rules did state that donations were tax deductible and no percentage was taken off. However, information indicated that donors would receive a form to take to an accountant. Although not a misstatement, one would question if a taxpayer would conclude, before making a contribution, that a portion of the donation would not be deductible. This university was deemed to be correctly informing donors because ultimately, assuming the form includes accurate information and the taxpayer uses an accountant, the taxes should be reported properly. Unfortunately, the information could lead a donor to assume incorrect tax planning. Taxpayers who file their own taxes might easily ignore the form, not understanding its importance, and deduct the entire donation.

From this simple study, it is evident that a problem exists. An overwhelming majority of those universities attaching the right to purchase tickets with donations either misstated information or provided incomplete information. One might argue that universities are not required to provide tax advice to donors. However, if donors are not aware of the limitation, the over-deduction of charitable donations does have an effect on several stakeholders. One such stakeholder is the taxpayer when, upon an Internal Revenue Service (IRS) audit, 20 percent of his or her deduction is disallowed. In addition, the taxpayer would be subject to penalty and interest on the underpayment of taxes as a result of the overstated deduction. Another stakeholder is the university. If donors perceive that a university has misled them, donations for athletics and other needs may drop. Universities depend on the generosity of their alumni and
friends. If a donor has a negative IRS audit experience over a contribution with ticket benefits, the donor is likely to share his or her experience with other donors. Such bad publicity could result in significant decreases in donations not only to athletics, but to academics as well if the university is viewed as hiding information or misleading donors. Other taxpayers also are affected. As the tax gap widens, compliant taxpayers bear the burden of funding government needs.

**Effect of Overstated Deductions**

Even if a contribution statement is provided to a tax advisor, it is often not clear why the payment was made or what benefits were received. The following example illustrates the effects of improper treatment of donations. Many universities start their highest level of donation at $5,000. Assume a taxpayer donates $5,000 and will be taxed in the 35 percent bracket. With no benefits received other than a right to purchase tickets, only 80 percent of the payment is allowable as a charitable contribution, resulting in a $4,000 deduction and $1,400 in tax savings. If a taxpayer takes a deduction of the full $5,000 the tax savings would be $1,750. A tax gap of $350 is created. Considering that 70 percent of the universities in our sample that offered the right to purchase tickets with a donation incorrectly advised donors, one can see why the tax gap is widening.

Treasury Regulation 1.170A-13 provides guidance on record-keeping requirements. Taxpayers are required to maintain records for any charitable contribution of money or property. In general, for cash donations, taxpayers must maintain a cancelled check or a receipt from the donee organization showing the name of the organization, the date of the contribution and the amount of the contribution. If the donor does not have a cancelled check or receipt for contributions of $250 or less, a reliable written record stating the above information will suffice.
The taxpayer bears the burden of proving reliability. The regulation lists several factors indicating the reliability of a written record: (1) the contemporaneous nature of the written evidence, (2) the regularity of the recordkeeping procedures (i.e., taxpayer’s diary entries) and (3) for small amounts, the existence of any written or other evidence from the donee organization (i.e., emblem or other token). If a cash payment is made partly as a contribution and partly for goods or services, the charitable organization is required to provide a written disclosure statement for amounts over $75 (Publication 557, p 13). If property (rather than cash) is donated, the recordkeeping requirements become much more stringent. The acknowledgement or receipt must be written and should include the amount and any benefits given along with a good faith estimate of the value of those benefits (Publication 526, p 19). At any donation level, the taxpayer may be unaware of the 80 percent deductibility rule. However, with a deduction of less than $250, especially if the check is just made out to the university foundation, there is almost no reason for anyone to question a 100 percent deduction. Even on donations larger than $250, the organization is not responsible for reporting the 80 percent limitation to the taxpayer, and if no tickets are actually purchased, the fact that there was a right to tickets could be easily overlooked.

So, what is the effect of these overstated deductions other than a little less money for the government? All of these overstated deductions are a part of what the IRS refers to as the tax gap. The tax gap is the “difference between what taxpayers should pay and what they actually do pay voluntarily and timely” (Plumley, 1996).

The tax gap is created by non-compliance in three areas: filing, reporting and payment. Although the three components are interrelated, reporting non-compliance is likely the largest portion (Brown and Mazur, 2003). Reporting non-compliance results from overstated
deductions and understated income, resulting in underreported taxable income and thus underpaid taxes. In 2006, the IRS released updated estimates for the 2001 tax gap. The gap for individuals underreporting income was $197 billion (IR-2006-28, 2006). Of this number, an estimated $14 billion is attributed to over-reported deductions (IR-2006-28, 2006).

There are several theories on why the tax gap exists and is so large. Some believe that the complexity of tax laws and tax returns results in noncompliance. Rules relating to charitable giving are considered to be some of the most complex in the Code. Complex tax code rules lead to more tax revenue in some cases by causing taxpayers to forgo a little extra refund so they do not have to itemize. This complexity leads to less tax revenue in other cases. Many taxpayers who choose to itemize deductions would likely argue that complexity is a legitimate cause for taking an extra 20 percent deduction on charitable contributions made in exchange for athletic ticket rights at an educational institution.

Another theory also exists for why income is underreported: transaction visibility. Transaction visibility is achieved through third-party checks on income or deductions that would prevent a taxpayer from underreporting income. An example would be when a third-party reports payments to or from taxpayers, which the IRS can then match to individual returns. According to Kim Bloomquist (2003), much of tax noncompliance is due to a lack of third-party reporting. Transaction visibility is often lacking in contributions to educational institution athletics with ticket rights received. Even though the donation may be reported, it is often lumped together with all the other donations, and benefits received are likely not mentioned, especially if it is just for ticket rights or priority seating. In fact, in order to receive a 100 percent deduction, one university employee contacted during this study recommended a contribution for the booster club (hence allowing ticket rights) to be made out to the university fund with just a
notation for the booster club on the bottom of the check. This type of system makes the purpose of the deduction and the benefits received almost untraceable.

Who should be considered responsible for this reoccurring misstatement, the taxpayer or the educational institution? Booster clubs often advertise a tax deduction as a reason to donate. Even if the institution correctly states the 80 percent limitation in its promotional material, the notice may not be prominently displayed. Does the donee have the responsibility to provide the donor with all the tax information pertaining to donations? Any advice given by the donee organization is most likely taken by the taxpayer as accurate and from a legitimate and knowledgeable source. This situation leaves the impression that it is important for colleges and universities to not only know the tax law applicable to their donors, but to correctly inform them of the rules. At a minimum, donee organizations should make an effort to suggest that the taxpayer seek advice from a tax professional.

**Conclusion**

This preliminary investigation gives some insight into one source of tax non-compliance. This study has certain limitations. First, the sample chosen was one conference and not selected at random. Therefore, any conclusions made from this study should be interpreted with caution. Second, the information obtained was from limited sources. Third, if the investigation had provided for actual donations to be made, adequate and accurate information may have been provided by the universities. This study provides opportunities for future research. Investigation into donors’ actual compliance of the charitable contributions rules would provide additional evidence of whether this situation significantly adds to the tax gap. Expanding the research to other universities in larger and smaller divisions would also be of interest.
In conclusion, tax evasion is a huge issue. There are billions of unpaid dollars in the tax gap that could alleviate many financial troubles for the federal government. Although donations made to Division II schools’ athletic programs may seem insignificant, if 70 percent of donors are misinformed about the deductibility of their payments, then it is likely that a large percentage of those will fully deduct any donation made, and pay much less in taxes than they should. Although some tax noncompliance is not intentional on the part of the taxpayer, awareness would likely solve most of the type of noncompliance addressed in this study. University athletic programs should take responsibility by making sure the information provided to donors is, at the very least, accurate. After all, many educational institutions are funded through tax dollars so they are likely stifling some of their future funding by suggesting that donors take a deduction amount greater than what is legally allowed.
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