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THEORY AND EVIDENCE FOR A TAX-DAY DEDUCTION

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Under certain circumstances the US tax system subsidizes charitable contributions for taxpayers by allowing them to deduct qualified contributions from their taxable income. Decades of research demonstrate that this subsidy encourages charitable contributions. But people often underestimate the value of their subsidy because they often underestimate their tax rate. This suggests that improving public understanding of the subsidy could lead to an increase in charitable contributions.

The incentive for charitable giving is related to the marginal tax rate—that is, the higher the rate, the greater the incentive to give. But many people do not know their marginal tax rate and often use their average tax rate as a proxy.[1] In a progressive income tax system—such as the one used by the US, where tax burdens generally rise with income—the average tax rate is never higher than the marginal tax rate.[2] As a result, taxpayers who use the average tax rate to determine their charitable contributions tend to underestimate their incentive and contribute less.

These findings suggest that increasing public awareness of the existing tax subsidy could raise charitable contributions. In this brief, I review an idea that has been discussed as early as 1990: a tax-day deduction, which allows a deduction up to the day people file their taxes (see Steuerle 1990).

THEORIES ABOUT A TAX-DAY DEDUCTION

Most people were aware of the Indonesia tsunami and the Haiti earthquake when they happened; in fact, about 60 percent followed the story “very closely” (Pew Research Center 2010). But few people might have known that, specifically because of these disasters, they were allowed to itemize eligible donations on their prior year’s taxes. It is easy to imagine that this information could get lost in the intensive coverage of the tragedies. Generally, the larger the disaster or crisis, the more the government may have to spend advertising the additional tax allowance within the brief window when it applies.

There are a number of advantages to permanently allowing a tax-day deduction rather than allowing it only during a crisis (Steuerle 2013). If the extension were permanent, taxpayers could learn over time how their donations can lower their taxes. Tax preparers or tax software could show taxpayers how their taxes owed or refunds would change with additional donations.[3] Taxpayers would have a much better understanding of how their contributions are being subsidized if they could conduct "what if" experiments and observe how increasing their contributions affect their taxes. For example, taxpayers could immediately see that an additional $100 donation to charity would reduce their taxes by $25 (for itemizers in the 25 percent tax bracket).

That is particularly useful because the recently passed One Big Beautiful Bill Act (OBBBA) complicated the incentives to contribute. For many years, the rule has been that taxpayers who itemize their deductions can subtract contributions from their taxable income. Under the OBBBA, those who itemize their deductions can only subtract contributions in excess of 0.5 percent of their adjusted gross income (AGI). Those who use the standard deduction can subtract their contributions (up to $1,000 for single filers or $2,000 for married taxpayers filing jointly) from their taxable income. Along with other changes in the OBBBA,[4] it can be difficult for taxpayers to know if they should itemize or take the standard deduction—that is, whether their incentive ends when their contributions exceed $1,000 or $2,000 or begins when their contributions exceed 0.5 percent of their AGI. A tax-day deduction solves this dilemma because the taxpayer will have all the Information they need to make these determinations.

Furthermore, a tax-day deduction is unusually tax efficient. Typically, using the tax system to encourage more contributions involves increasing the incentive. For example, moving to a universal deduction with no minimum amount (or floor) would allow more people to receive subsidies for their giving, but much of that giving would have occurred without the subsidy. So it could cost the treasury a lot of money without much increase in charitable giving. A tax-day deduction, on the other hand, subsidizes contributions that would have occurred if people understood the subsidy, but not otherwise—therefore, it only subsidizes giving induced by the subsidy.

Rees-Jones and Taubinsky (2016) discuss the tax-day deduction, making three points. First, if people tend to focus on the present, they will be more motivated to give if the reward is available soon after the donation. Currently, a donation made in January 2025 can only be deducted when a taxpayer files their return in 2026, possibly as late as April, and any potential refund would come even later. So, for present-focused people (who heavily discount the future), the benefit of the deduction may come so far in the future that it plays little or no part in their decision about whether and how much to give. In contrast, a tax-day deduction would let people donate in April 2026 and immediately reduce their taxes owed. And if they are receiving a refund, they would usually see the benefit in less than three weeks.[5] This would make it much easier for present-minded people to be aware of the benefits of the deduction.

Second, incentives in the tax system can be confusing and "not fully salient" (Rees-Jones and Taubinsky 2016, 2). If taxpayers underestimate their tax incentives, they will contribute less. Under previous law, the subsidy rate for itemizers is just their tax rate: for every $100 they contribute, they reduce their taxes by $25. But taxpayers can accurately understand the subsidy rate only if they understand two pieces of information: whether they usually itemize their deductions and the level of their marginal tax rate.

Third, although there are only seven tax brackets in the US individual tax system, and three for married couples filing jointly with less than $200,000 of taxable income, people have a hard time learning or understanding their tax bracket. This is especially true for people with income that varies substantially from year to year, and also for people with steady incomes but who in a year experience a sharply lower income (possibly because of unemployment) or a sharply higher income (possibly because of a large bonus). The average tax rate is easier to understand than the marginal tax rate, because it can be calculated by dividing total individual taxes by taxable income—that is, people can get a sense of their average rate by looking at their pay stubs and comparing their taxes withheld and their income. But the progressive structure of the US individual income tax system means that taxpayers who use the average rate will underestimate their marginal tax rate,[6] which in turn means that they will underestimate their subsidy.

Rees-Jones and Taubinsky (2016) believe that allowing tax-day deductions could lead to substantial increases in contributions because of tax aversion and its interaction with tax salience. They cite research demonstrating the presence of tax aversion among some taxpayers and that show some people prefer reducing taxes to increasing refunds by the same amount. They point out that allowing taxpayers to make donations and receive rapid rewards in the form of tax cuts when filing will be particularly powerful because the tax rates are “unusually salient” (Rees-Jones and Taubinsky 2016, 5). They believe that it would empower tax preparers to more actively promote charitable giving.

There are, however, several potential problems with a tax-day deduction. Rees-Jones and Taubinsky (2016) indicate that a large share of high-income taxpayers (who make most of the contributions) regularly interact with a tax professional. To the extent that this is true, they may already know their marginal tax rate. Furthermore, the Tax Cuts and Jobs Act of 2017 substantially increased the standard deduction, and thereby reduced the share of taxpayers who itemize to those mainly in the higher-income bracket.[7] On the other hand, the OBBBA has complicated the subsidy for both itemizers and non-itemizers.

Rees-Jones and Taubinsky (2016) also mention that a strong interaction between end-of-year giving and the holiday season could cause an overall reduction in giving. They cite a 2014 study, which found that nearly 33 percent of contributions are made in December and 12 percent are made in the final three days of the year.[8] But people give at the end of the year for many reasons. For example, the sharp increase in religious giving on the last day of the year may be due to families fullfilling their donation commitments for the year.[9] People may also give away some of their end-of-year bonuses or simply complete any planned donations for the year. While this is an important question for future research to address, the above considerations suggest it may be of limited concern.

If research shows that there is a trade-off between end-of-year giving and giving when filing taxes, the problem could be resolved by only allowing a share of tax-day contributions to be deducted. For example, donations made during the year would be fully deductible while only half of tax-day donations would be deductible. This would provide the most benefit to end-of-year giving, but still provide an incentive, albeit weaker, to contribute on tax day.

Finally, Steuerle (2013) suggests that with a tax-day deduction, some people may mistakenly deduct their contributions twice for the filing year: once before the contribution is made and again when the contribution is made. Charities may need to add a checkbox to receipts, and tax software and tax accountants may need to remind or warn taxpayers that they can deduct their contributions only once. Regardless of the method, it would introduce an additional complication to the tax system. This burden might be reduced with tax software requiring a bit more information on tax-day deductions, with improved information reporting to the IRS.

EVIDENCE OF THE EFFECT OF A TAX-DAY DEDUCTION

Recent research has shown that allowing a tax-day deduction increases donations. Hickey, Minaker, and Payne (2019) analyzed Canadian donations to relief organizations in the aftermath of the 2010 earthquake in Haiti. In January 2010, the federal government offered a matching grant in response to the devastating earthquake. But the province of Quebec went a step further and allowed taxpayers to deduct relief contributions from their 2009 tax filings. Comparing donations made by neighborhoods of Quebec with donations made by neighborhoods of other provinces with similar characteristics (e.g., average incomes, the share of residents that are Haitian, and the share of residents that speak French at home), the authors found that the frequency of claimed donations increased by 2 percentage points and average donations increased by 9 percentage points in Quebec.

There is reason to believe that this change in donations occurred because the tax-day deduction increased the salience of the subsidy. The Canada Survey of Giving, Volunteering and Participating shows that in 2010, 84 percent of Canadians, ages 15 and older, contributed to charity.[10] Yet, for tax year 2010, only 23 percent of all returns used the available tax credit for donations.[11] Although there are plausible reasons for this difference besides a lack of salience, they are unlikely to explain it entirely.[12] Research suggests that there are similar responses in the US. Chetty, Looney, and Kroft (2009), among others, demonstrate that saliently including sales tax in the price of goods, rather than hiding it in the total price, will decrease demand.

Goldin and Listokin (2014) conducted an online survey, which showed that Americans with more than $30,000 of income generally know whether they itemize their deductions or take the standard deduction. But the authors found that nearly half of itemizers did not know that charitable contributions reduced their taxable income. Even among those in the 33 and 35 percent tax brackets—the highest brackets applicable to survey respondents and those who received the greatest subsidy—22 percent of itemizers did not correctly report that their contributions were subsidized.

Blaufaus and colleagues (2022) reviewed the literature on tax misperception. They show that marginal tax rates are widely misunderstood, with overestimates being more common than underestimates. But importantly, they point out that overestimates tend to occur among lower-income taxpayers while underestimates tend to occur among higher-income taxpayers (Blaufus et al. 2015; Gideon 2014, 2017). Because a large share of donations come from high-income taxpayers, contributions may be much lower than they would be if people correctly understood their marginal tax rate.

Blaufaus and colleagues (2022) also cite three studies on this misunderstanding of the marginal tax rate: Blaufaus and colleagues (2015) report that one-sixth of survey respondents confused the average tax rate with the marginal tax rate, and de Bartolome (1995) and Rees-Jones and Taubinsky (2019) both report that people tend to use the average tax rate in place of the marginal tax rate.

McClelland and colleagues (2019) and Steuerle and colleagues (2021) consider a universal deduction with various floors on the amount of giving. They find that a deduction for all contributions would have raised contributions by $8.7 billion and cost the federal government $27.1 billion in 2019. However, only allowing contributions in excess of 1 percent of AGI would have increased contributions by $6.5 billion and cost the government $9.7 billion in 2019. Here, a tax-day deduction would allow taxpayers to understand if their contributions are subsidized because their AGI will have been established.

It is unclear whether donors substitute giving to one charity for another over time. Scharf, Smith, and Ottoni-Wilhelm (2022) find that disaster appeals raise overall donations rather than replace donations to other causes. They also find that other charities receive temporary bumps during disaster appeals. If there is a similar interaction between tax-day giving and end-of-year giving, charities receiving end-of-year donations may not see much, if any, decline, and may even see increased donations.

CONCLUSION

Research suggests that while people generally know whether they itemize, they tend to not know their marginal tax rate. People are likely to be more aware of their marginal tax rate—and hence the subsidy to their contributions—when they are filing their taxes. Therefore, a tax-day deduction will likely increase donations, and research has shown that extending the deadline for donations to the tax day increases contributions.

NOTES

[1] For more information on marginal and average rates, see "What Is the Difference between Marginal and Average Tax Rates?" T*ax Policy Center Briefing Book*, accessed October 14, 2025, https://taxpolicycenter.org/briefing-book/what-difference-between-marginal-and-average-tax-rates.

[2] For more information on the US individual income tax system, see "Are Federal Taxes Progressive?" T*ax Policy Center Briefing Book*, accessed October 14, 2025, https://taxpolicycenter.org/briefing-book/are-federal-taxes-progressive.

[3] In 2024, about 60 percent of filers received a refund. Internal Revenue Service, "Filing Season Statistics for Week Ending April 18, 2025," updated May 29, 2025, https://www.irs.gov/newsroom/filing-season-statistics-for-week-ending-april-18-2025.

[4] Other changes in the OBBBA include increasing the cap on the state and local tax deduction from $10,000 to $40,000 making less than $500,000 from 2026 through 2029. The cap is not indexed for inflation and future congresses may choose to keep or change the higher amount or let it expire.

[5] Intuit, "Where's My Tax Refund? The IRS Refund Timetable Explained," updated July 31, 2025, https://turbotax.intuit.com/tax-tips/tax-refund/wheres-my-tax-refund-the-irs-refund-timetable-explained/L9ZoW82cT.

[6] One type of "schmeduling" (known as "ironing") occurs when taxpayers use the average tax rate and underestimate their marginal tax rate; "spotlighting" occurs when taxpayers do not recognize that there are marginal tax rates different from their own. See Blaufaus and colleagues (2022) and Rees-Jones and Taubinsky (2019) for more information.

[7] In 2017, 31 percent of filers itemized their deductions, but only 11 percent did in 2018, the first year of the Tax Cuts and Jobs Act. Internal Revenue Service, "SOI Tax Stats—Individual Statistical Tables by Size of Adjusted Gross Income," updated November 8, 2024, https://www.irs.gov/statistics/soi-tax-stats-individual-statistical-tables-by-size-of-adjusted-gross-income.

[8] Network for Good Digital Giving Index accessed by Rees-Jones and Taubinsky on March 24, 2016, http://www.networkforgood.com/digitalgivingindex/.

[9] Giving USA reports that there is a sharp increase in religious giving every December 31. Tim Sarrantonio, "What New Research Tells Us about How Donors Give in December (and Year-Round!)," Giving USA, December 2, 2021, https://givingusa.org/what-new-research-tells-us-about-how-donors-give-in-december-and-year-round/.

[10] Sector Source, "Research about Giving in Canada," accessed October 15, 2025, https://www.sectorsource.ca/research-and-impact/giving-research.

[11] Government of Canada, "Final Statistics 2012 Edition (2010 Tax Year)," modified August 12, 2019, https://www.canada.ca/en/revenue-agency/programs/about-canada-revenue-agency-cra/income-statistics-gst-hst-statistics/t1-final-statistics/t1-final-statistics-2012-edition-2010-tax-year.html.

[12] Some people may be contributing to a nonqualifying organization, and some survey respondents may be falsely stating that they have made a contribution. Additionally, only about two-thirds of returns are taxable, and therefore some filers may not bother with the credit because they are filing a nontaxable return.

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