

Public Hearing on Proposed Regulations: Taxes on Taxable Distributions from Donor Advised Funds Under Section 4966

IRS Auditorium/Teleconference | May 6 – 7, 2024

[Council Remarks as Prepared for Delivery]

Good afternoon. Thank you for convening today's public hearing.

I'm Jenn Holcomb, Vice President of Government Affairs and Legal Resources at the Council on Foundations.

The Council is a nonprofit membership association that serves as a guide for philanthropies as they advance the greater good. Building on our 75-year history, the Council supports more than 900 member organizations in the United States and around the world to build trust in philanthropy. The Council is proud to advocate on behalf of our members and philanthropy broadly for a regulatory environment that fosters a thriving and vibrant sector.

DAFs help individuals and organizations support the causes, charities, and communities they care most about today and long-term.

As we look at how these proposed regulations will impact community foundations and other sponsoring organizations, the Council is concerned that much of what is proposed will cause confusion and disruption.

We share many of the concerns you will hear from our members and partners during this hearing. And while there are parts of the regulations that we do support, given my limited time, I am going to focus on three areas of concern:

- (1) clarifying the definition of a DAF,
- (2) the personal investment advisor provision, and

(3) the applicability date.

Establishing a clear definition of a donor-advised fund.

First, community foundations administer a wide variety of funds. But **not** all those funds are DAFs. And these regulations should **not** treat such funds as DAFs. At the same time, we should all be able to agree that funds that operate like a DAF should be treated as one.

As defined in the Pension Protection Act, to be considered a DAF, the fund must have three characteristics:

- Separately identified with reference to the contribution of a donor or donors
- Owned and controlled by a sponsoring organization; and
- The donor or donor advisor must reasonably expect to have advisory privileges.

While those prongs seem fairly clear, our Legal Resources team routinely fields questions from community foundations asking for clarification regarding whether a fund is a DAF. And since the proposed regulations were released, we have received even more.

Though meant to provide clarity, they have instead caused even more uncertainty and confusion. Staff are confused about whether fiscal sponsorships, giving circles, and the field of interest funds they manage could now be treated as DAFs. Having these funds treated as DAFs limits their effectiveness as vehicles for collaborative giving.

And even if some of these funds are ultimately determined to fall outside the regulations, the process of having to analyze each fund is a sizeable undertaking. Many of our members manage hundreds, sometimes thousands, of various funds. Analyzing even a fraction of those to ensure each meets an exception is costly in terms of time, staff power, and financial resources. These worries are reflected throughout many of the comment letters you received from community foundations and other sponsoring organizations.

I want to share an example from a Council member about a fund that could be treated as a DAF under these proposed regulations:

- **The San Angelo Area Foundation** sponsors a giving circle named the Future Fund. It is composed of younger philanthropists who each give and collectively review grant requests

and recommend grants to 3-4 charitable organizations annually. On average, the group ranges between 40 and 50 donors. No one donor's input is greater than the others, but the Foundation is concerned the proposed regulations may treat this type of giving circle as a DAF. Today, this fund's endowment continues to support the group's charitable efforts, while continuing to add new members and donations.

I know there are many more examples – some you will hear about today and tomorrow. Each fund helps ensure charitable gifts support nonprofit organizations in communities across the country and sometimes around the world. Treating these funds as DAFs will not improve the charitable ecosystem, but instead add a new and unnecessary administrative roadblock.

Recent public comments by Treasury staff have suggested that the proposed regulations were not intended to capture many of these other fund types. We appreciate this clarification and hope it is reflected in the final regulations.

To that end, we urge you to opt for simplicity over complexity. This should include reiterating that all three prongs must be met to be considered a DAF; simplifying the facts and circumstances when considering if a fund is separately identified; and modeling an exception for participation in advisory committees that reflects the established rules for scholarship committees.

The definition of a DAF must be clear, simple, and consistently applied throughout the field, which is why getting these regulations right is important.

Treatment of a Personal Investment Advisor as a Donor Advisor

Next, the Council echoes many of the concerns you have already heard about considering a personal investment advisor a donor advisor.

We believe current state and federal laws, as well as standards of practice, already exist to help prevent and address any instances of abuse that may occur. For many of our community foundation members, outside investment advisors provide an important service. Foundation staff can work with these external consultants to ensure the DAF investments are appropriately managed so donors can achieve their charitable goals.

For many community foundations, using outside investment advisors is a part of their business model. For instance,

- The **Community Foundation of Western North Carolina** has 423 DAFs with assets of more than \$131 million. As of March, 19 percent of those DAF assets were managed by investment advisors recommended by donors and donor-advisors.
- The **Black Hills Area Community Foundation** is a relatively small organization with \$60 million in assets. They recently added DAFs managed by investment advisors recommended by donors to their work. In one instance, they were able to deepen a relationship with a donor who is now comfortable leaving a sizable estate gift to the foundation.
- Finally, almost 1,000 of the funds administered by the **Community Foundation of Greater Des Moines** are DAFs. It also runs the Charitable Investment Partners Program, which enables donors to benefit from both the services offered by their local community foundation and the existing relationship with their investment advisor. The CIP program includes 372 DAFs and 85 approved advisors.

Examining each of these arrangements and then making any necessary changes will take significant time and resources. It cannot happen overnight.

And it is important to note that the investment advisor arrangement can be revoked. A sponsoring organization can and should terminate the agreement if a problem or conflict arises, or the fund is underperforming. Over the past few months, I have talked with several members about this provision. Some have shared stories of having to do exactly that – end the relationship because problems arose.

Now we believe your goal here is to stop and prevent instances of abuse or conflicts of interest. The Council and our members share that broad goal. Our members take seriously the responsibility of being stewards of the charitable dollars they manage. That responsibility requires that foundations establish and maintain the public's trust. Without it, there's little the sector could accomplish.

At the Council, we believe that public trust in philanthropy expands when our field demonstrates high professional and ethical standards. This commitment shows up in all we do – from the ethical principles developed in 2022 to the pledge we launched with partners at the start of the COVID crisis to our continued commitment to Community Foundations National Standards.

Since 2009, we have been the supported organization for Community Foundations National Standards, a voluntary self-regulatory program. The National Standards accreditation seal represents a community foundation's commitment to rigorous, sector-driven best practices that exceed federal and state law requirements and demonstrate accountability and excellence to communities, policymakers, and the public.

To achieve accreditation, foundation policies and procedures are subjected to rigorous review by attorneys and peers. Today, over 440 community foundations are accredited by National Standards, and dozens more are in the process.

Proposed Applicability Date

Last, while we are assured by recent public comments that the final regulations will not be retroactive, we urge you to go further and ensure the field has adequate time to understand, pivot, and implement the final regulations.

Our members vary in asset size, number of DAFs, and staff capacity. We have heard concerns from the biggest community foundations to the smallest about what implementing this rule will mean for them.

The Council recommends a period of no sooner than two tax years starting after the tax year of publication in the Federal Register. That time will ensure our members can make the changes to their operations – minimizing any disruption to the sector and charitable giving broadly while also maintaining the public's trust in the sector.

Thank you for letting me share these remarks on behalf of the Council on Foundations and our members.

As you work to finalize these regulations, please look to us as a partner. We are committed to helping ensure our members and the sector have the information to understand how best to comply in the context of their organizations, the donors they engage, and the communities they serve. Together, we can ensure donor advised funds and the sector broadly continue to support nonprofit organizations and communities.