



## COUNCIL ON FOUNDATIONS

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April 4, 2005

The Honorable Charles Grassley  
United States Senate  
Washington, DC 20510

Dear Chairman Grassley:

As you prepare for tomorrow's Senate Finance Committee hearing, the Council on Foundations would like to share its thoughts about several very important issues to be addressed during the hearing and in the coming months. We are committed to doing our part to put an end to the illegal and unethical behavior of the few who abuse the system and tarnish the reputation of the entire foundation community. Our goal is to improve the role of our private sector oversight and accountability standards, to advocate for the enforcement of existing laws and the expansion of regulations if necessary. We strongly believe that some legislative proposals being considered may inadvertently harm the ability of foundations to meet their missions to improve communities and to enhance the lives of individuals.

The Council represents more than 2,000 members, including community, family and corporate foundations that are the backbone of America's compassion. Their perspective on some of these proposals is a critical component of the legislative process and we are committed to engaging actively in it.

Attached is a brief summary of our current positions on some of the proposals you are considering at your hearing. We would be pleased to provide additional information and analyses should you desire it.

The Council on Foundations appreciates the work of the Senate Finance Committee in promoting a dialogue with foundations and public charities about reforms that will prevent abuses and continue to afford foundations the flexibility to pursue creative solutions to global problems. Many of the proposals in the staff discussion draft paper are far-reaching and will require continued thoughtful consideration. We stand ready to continue to work with you to ensure the appropriate balance between enhanced voluntary efforts and increased government oversight to enforce the laws and to encourage adherence to high ethical standards.

Sincerely,

Dorothy S. Ridings  
President and CEO

Enclosure

# **The Council on Foundations**

## **Overview of Selected Charitable Sector Reform Proposals**

### **Administrative Expenses**

Questions about administrative expenses have been at the forefront of discussion of problems affecting tax-exempt organizations. The issues range from what constitutes administrative expenses, to how they are reported, and finally to how much is too much. Improvements should be made that identify those foundations that have unusually high administrative expenses in comparison with other foundations that are like them.

#### ***We Support:***

- Uniform standards for reporting foundation administrative expenses with common definitions.
- Enhanced reporting of administrative expenses that exceed a threshold percentage of 20 to 25 percent of total expenses, based on the average of these costs over a five year period.
- A modest fee to the IRS for processing the additional information.
- Excluding administrative expenses that exceed 35 percent of total expenses from qualifying distributions in calculating a foundation's payout.

#### ***We Oppose:***

- Limitations on administrative expenses that discourage direct service to the community.
- IRS filing fees that are punitive or intended to generate a significant amount of revenue to pay for other activities in the legislation.
- Reporting requirements that fail to recognize differences among foundations including their size, whether they have paid staff, the scope and scale of their grant-making, the kinds of grantees they fund, and the extent to which they directly carry on charitable programs in comparison to the scope of their grant-making.
- Reporting requirements that are triggered by expenditures in a single year given that the ratio may vary from year to year due to circumstances beyond the foundation's control.

### **Compensation**

The law limits compensation to that which is reasonable in amount and necessary to accomplish the foundation's charitable purposes. Private foundations may not pay compensation that is excessive and must disclose compensation paid to board members and officers on Form 990-PF. Compensation is judged by what similar organizations pay for similar services in the same geographic area.

#### ***We Support:***

- Strict enforcement of current legal requirements that compensation be both reasonable **and** necessary.
- Increased penalties on both the recipient and foundation managers who approve excessive compensation.
- Improvements to laws that govern how trustee compensation is determined and disclosed.

- Improvements to the 990-PF that provide more consistent reporting of compensation and better identification of outliers.
- Targeted follow-up, including audits and the imposition of penalties as appropriate, that discourages the kind of outrageous compensation reported recently in the media.

***We Oppose:***

- Any prohibition against paying trustees or limiting compensation to an artificial amount that has been judged to be “*de minimis*.”
- The use of a specific dollar amount to trigger additional reporting.
- Treating family members who are disqualified persons differently from non-family members who are disqualified persons.
- Using federal rates as benchmarks for compensation.

**Increased Philanthropy**

Foundations have a rich history of funding some of our country’s greatest achievements: the discovery of the polio vaccine, protease inhibitors, the 911 emergency response system and Sesame Street. Foundations’ entrepreneurial, independent and visionary strategies are ones that should be supported and encouraged by Congress. Foundations are an American success story – they do vital work in the communities you represent.

***We Support:***

- The President’s plan to reduce the excise tax on the net investment income of private non-operating foundations from 2 percent to 1 percent that will encourage additional funding for grants while reducing major administrative burdens.
- Reforms that prevent donors from claiming deductions that greatly exceed the actual value of non-cash and non-stock assets.

***We Oppose:***

- Changing the valuation standard for non-cash charitable gifts. Much of America’s wealth - as much as 60% - is in property other than cash and publicly-traded securities. Since non-cash charitable gifts are so vital, valuation reforms must be carefully drafted to avoid discouraging donors from contributing to charity.

**Donor-Advised Funds**

Nearly all community foundations offer donor-advised funds as a giving option, amounting to approximately 25 percent of total assets held by community foundations.

***We Support:***

- Prohibition of grants from donor-advised funds to private non-operating foundations.
- Prohibition of grants to or for the benefit of donors or advisors, their family members and businesses they control.
- Standards to ensure that donor-advised funds can continue to be a building block for philanthropy and do not become a focus of abuse.

***We Oppose:***

- Prohibitions on all grants to individuals, including scholarships, disaster relief and emergency hardship grants.
- Prohibitions on private foundation grants to donor-advised funds.
- Banning grants to nondomestic organizations since donor-advised funds provide a simple, low-cost mechanism through which donors can safely support a far wider range of foreign charitable organizations.

**Supporting Organizations:**

Supporting organizations are among the many charitable vehicles that donors can utilize to achieve their specific philanthropic goals. As with all charitable vehicles, supporting organizations have unique characteristics that make them more effective and efficient than other options in certain circumstances.

***We Support:***

- Continued availability of Types I, II and III for community foundations, universities, non-profit healthcare organizations and numerous other charities that rely on gifts made possible by supporting organizations.
- Specific IRS technical requirements to ensure that supporting organizations are properly organized and operated and that the charities they support have sufficient oversight of and involvement with the affairs of the supporting organization.
- Additional oversight and procedures to address concerns about Type III abuse.

***We Oppose:***

- Elimination of Type III supporting organizations.

**Improved Financial Reporting**

***We Support:***

- Modifications and simplification of Forms 990 and 990-PF, and of financial statements that will improve public disclosure and transparency.
- E-filing of these forms as soon as can reasonably be done.
- Amendments to the Internal Revenue Code to permit the IRS to share audit and investigation information with state charity regulators.