COUNCIL on FOUNDATIONS

ISSUE PAPER

Donor Advised Funds

Position

The Council opposes any proposals that require a DAF to pay out a percentage of funds each year or exhaust funds within a specified time period.

The Council supports the clarification of certain issues related to donor advised funds. Thoughtfully drafted regulations are necessary to provide the nonprofit sector and the public with additional guidance about the donor advised fund provisions in the Pension Protection Act of 2006.

How You Can Support Philanthropy (Ask)

Send letters to the Treasury Department requesting clarification on the DAF provisions enacted in the Pension Protection Act of 2006.

For more information, contact the
Council's Public Policy and Legal Affairs Department
at
govt@cof.org

Background

A donor advised fund, or DAF, is a unique philanthropic tool. DAFs allow donors to establish a fund at an institution and remain involved in supporting the causes and issues they care about. The donor may name one or more persons as the "advisor(s)." DAFs are often established at a public foundation, such as a community foundation. Community foundations oversee and manage funds on behalf of families or individuals and, in many cases, have the discretion to direct some of the resources to priority causes the foundation identifies.

The Pension Protection Act of 2006 (PPA) recognized the importance of DAFs, with Congress acknowledging this charitable tool for the first time by defining it.

A donor-advised fund as defined by the PPA is any fund or account: 1) which is separately identified by reference to the contributions of a donor or donors; 2) which is owned and controlled by the sponsoring organization, like a community foundation; and 3) with respect to which a donor or person appointed by the donor has or reasonably expects to have advisory rights with respect to investments or distributions. Several exceptions exist to these rules, including exceptions for scholarship funds and funds that support only one charitable organization.

Some donor-advised funds will be fully expended during the donor's lifetime; others will be a permanent legacy, benefitting communities into the future. These innovative giving tools empower donors to support the needs of their communities over time, and to leverage their funds with other donors who share a common interest in a specific issue.

Despite the benefits DAFs bring to communities, proposals have been discussed in Congress that would challenge the fundamental and long-standing value of endowed philanthropy. One proposal, Chairman Camp's *Tax Reform Act of 2014*, would require a DAF to exhaust its funds within five years or pay an annual 20 percent excise tax on the remaining money.

Proposal

The Council's membership and donors who seek to use DAFs as a giving tool oppose any proposals that require a DAF to pay out a percentage of funds each year or exhaust the funds within a specified time period.

However, donors and foundations alike would benefit from IRS regulations clarifying the following about DAFs:

- Whether Section 4966(d)(2)(A)'s definition of a donor advised fund applies to funds that have multiple unrelated donors, and if so, how.
- The definition of "more than incidental benefit" for donor advised funds, derived from Internal Revenue Code section 4967.
- Whether there is a definition of a legally binding pledge.
- Whether donor advised funds can be used to satisfy a legally binding pledge.

Rationale

Through daily contact with its members, the Council is acutely aware that the issues outlined in the Proposal section above are important and affect the day-to-day operations of community foundations and other foundations that hold DAFs.

Council members, especially community foundations, are extremely concerned by proposals to require each donor advised fund to payout a percentage of funds each year or exhaust the funds within a specified time period. DAFs are a widely used giving tool that engage younger donors than other giving tools. In 2014, the Urban Institute surveyed community foundations to understand more about both DAFs and the donors who use this philanthropic tool. The results highlight three key facts about DAFs:

1) ***DAFs help community philanthropy endure.*** DAFs help increase the impact of charitable giving and build access to long-term philanthropic resources in our communities. DAFs ensure funds are available during hard times, much like a community savings account. During the Great Recession, DAFs allowed community foundations to sustain and even increase charitable giving at a time when individual giving and endowments plummeted and communities were in need.

2) ***DAFs encourage lasting civic engagement.*** More than 70 percent of foundations report the average age of a DAF donor is between 46 and 64 years old. This signals that DAFs are an important entry point for planned, strategic giving and long-term community involvement. For example, 81 percent of foundations report donors serve on foundation boards, or in another leadership role; 68 percent of foundations report donors help address pressing community needs; and 42 percent of foundations report donors help anticipate emerging community needs.

3) ***DAFs build stronger communities.*** DAFS are flexible, allowing community foundations to quickly respond to local needs. DAFs have been used to support everything from emergency response efforts to community economic development. Each community foundation utilizing DAFs has a story to share about connecting donors to the causes they care about using donor advised funds.

In addition to concerns about payout requirements, without additional regulatory guidance to supplement and clarify the current Internal Revenue Code provisions, community foundations and donors do not always have a clear understanding of how to comply with the law and may inadvertently risk violations with respect to grantmaking or other distributions.

Community foundations take seriously the obligation to protect donor investments. The majority of community foundations voluntarily self-regulate through the National Standards for U.S. Community Foundations™ program. This peer-driven voluntary process includes a review of community foundations' DAF policies and procedures to ensure the community foundation exercise their exclusive legal control over all funds, gifts, and grants with donor input. DAFs build stronger communities, encourage civic engagement, and empower foundations to respond to immediate and long-term community needs.

Opposition

Although there is little disagreement that DAF regulations are needed, in some recent legislation and news articles, policymakers, journalists, and academics have gone a step further and questioned whether DAFs should have a minimum distribution requirement similar to the 5% minimum distribution requirement applicable to private foundations.