



May 31, 2017

**Via Hand Delivery**

Courier's Desk  
Internal Revenue Service  
Attn: CC:PA:LPD:PR (Notice 2016-26)  
1111 Constitution Avenue N.W.  
Washington, D.C. 20224

**RE: Recommendations for 2017-2018 Priority Guidance Plan Notice 2017-28 - Domestic**

Dear Ladies and Gentlemen:

On behalf of the Council on Foundations, we write to urge the Treasury Department and the Internal Revenue Service to include three items in the 2017-2018 Priority Guidance Plan that impact our foundation members. These are listed below in order of urgency, though the Council emphasizes that our foundation members would benefit significantly from further clarity on each of these regulatory issues.

**First**, guidance on the statutory provisions related to donor advised funds, which became law in the Pension Protection Act of 2006 (PPA) and are codified in Internal Revenue Code Sections 4966 and 4967. Related to these sections, we also request the Secretary exercise the authority given in Section 4966(d)(2)(C) to define funds that include advisory privilege but fall outside of the definition of donor advised funds and the scholarship exception in Internal Revenue Code Section 4966.

The lack of guidance on key terms in the regulations, including the definition of what is and is not a donor advised fund and what constitutes advice that confers more than an incidental benefit upon a disqualified person, creates uncertainty and hampers our efforts to establish standards for sponsoring organizations of donor advised funds. At the same time, we are concerned that regulations will go beyond the scope of the statute to impose private foundation payout rules on a fund-by-fund basis, treat grants from donor advised funds as 2% limited rather than public support from a public charity described in section 509(a)(1), prevent private foundation terminations into donor advised funds, or other rulemaking efforts that are unnecessary and would disrupt the sector. We would be pleased to offer you our assistance and the experience of our members to help bring this rulemaking effort to fruition expeditiously. To that end, we have provided specific recommendations in the comments below.

**Second**, we request guidance on foundation-sponsored student loan forgiveness programs. We

and our members are deeply concerned about the growing student loan crisis in America, particularly as it affects low income individuals in economically distressed areas. We believe that foundation-sponsored student loan forgiveness programs should be treated as qualifying distributions for 4945(g)(1) and that providing student loan forgiveness to low-income individuals is a charitable purpose within the meaning of Section 170(c)(2)(B). Student loan forgiveness should qualify as scholarships for qualified tuition and related expenditures under section 117 and that the student should not have cancellation of indebtedness income as a result of such forgiveness, which would undermine the effectiveness of such relief efforts.

**Third**, we request updated guidance regarding economic development as a charitable activity, including a more definitive test and/or examples of acceptable charitable activities that reflect the current needs and economic climate in many communities. In the 1960-1970s, as community tensions rose, PLRs recognized that economic development could be charitable activity. However, in the past three decades, PLRs find most economic development is not a charitable activity. The gulf between the haves and have-nots in America continues to widen, and foundations are looking for new ways to help communities that are left out or left behind economically.

To assist Treasury in developing guidance, our members provided examples of situations they have encountered that illustrate the need for guidance in each area described above.

### **1. Donor Advised Funds: Regulations Addressing Certain Issues**

The Pension Protection Act of 2006 codified the definition of “donor advised fund” in Section 4966 of the Internal Revenue Code, which provides that donor advised funds must have three distinct characteristics:

- Separately identified by reference to contributions of a donor or donors
- Owned and controlled by a sponsoring organization
- A donor, or any person appointed or designated by the donor, has, or reasonably expects to have, advisory privileges regarding the distribution or investment of amounts held in such fund or account by reason of the donor’s status as a donor

Under Sections 4966 and 4967, a fund that meets this definition must be managed subject to certain restrictions on “taxable distributions” and the provision of more than an “incidental benefit” on disqualified persons. These rules generally prohibit donor advised funds from making grants to individuals or grants to non-charities and certain other organizations unless the sponsoring organization exercises expenditure responsibility over the grant.

#### Section 4966 Definition of “Taxable Distribution”

One common situation encountered by sponsoring organizations of donor advised funds is the request to make in-kind grants to individuals of goods such as backpacks full of school supplies to schools for the benefit of children. While clearly charitable, this request can be difficult for sponsoring organizations to effectuate for many reasons. First, it is not clear that a sponsoring organization may purchase goods or services from vendors due to the risk that the payment to the vendor would be treated as a taxable distribution. Second, if the vendor is a disqualified person

under Section 4958(f)(7), it is unclear whether a purchase at fair market value would confer “more than an incidental benefit” upon the vendor. Third, it is not clear whether distributing the school supplies to schools for the benefit of children is a taxable distribution. Regulations clarifying whether sponsoring organizations may use donor advised funds to purchase goods and services from vendors, the appropriate price to pay disqualified persons for goods and services, and whether donor advised funds may make grants to organizations for the benefit of natural persons would be helpful as these issues regularly occur and sponsoring organizations may have differing interpretations of what is acceptable under the statute.

### Application of Section 4967 Penalties to Pledges and Bifurcated Payments

The Council requests regulatory guidance clarifying the standard for “more than incidental benefit” to assess penalties under Section 4967, and specifically, guidance addressing two common situations encountered by our foundation members:

- Whether grants from donor advised funds may satisfy a legally enforceable pledge made by a disqualified person; and
- Whether a donor advised fund and a disqualified person may jointly contribute funds to an organization that results in a substantial return benefit to the disqualified person (i.e., one that requires a reduction in the value of the donor’s charitable contribution deduction) such that the donor advised fund pays only the portion that would be deductible, and the donor pays the nondeductible portion.

### Definition of Donor Advised Funds

Section 4966(d)(2)(C) grants the Secretary of the Treasury authority to exempt a fund or account from treatment as a donor advised fund “(i) if such fund or account is advised by a committee not directly or indirectly controlled by the donor or any person appointed or designated by the donor for the purpose of advising with respect to distributions from such fund (and any related parties), or (ii) if such fund benefits a single identified charitable purpose.”

There is significant confusion within the philanthropic community over whether the statutory definition of “donor advised fund” under Section 4966(d)(2)(B) includes these types of funds:

- Funds with multiple unrelated donors including giving circles
- Funds established by civic organizations and other membership associations
- Funds established by public charities and governmental entities
- Funds established by private foundations
- Memorial funds

Our members would benefit significantly from additional precision around the definition of “donor” as applied to these situations. The Council on Foundations suggests that groups of unrelated individuals, whether organized informally as a giving circle, or more formally as a civic club such as Rotary, who contribute to a fund at a sponsoring organization, and who collectively decide on grant recommendations, do not meet the definition of “donor” for purposes of a donor advised fund, and therefore, should not be subject to the restrictions set forth in Sections 4966 and

4967.

Additionally, the Council suggests that a fund established by another charitable organization, whether public charity, private foundation, church or school, to make grants to other charitable organizations or for charitable purposes also should not be treated as a donor advised fund, even if individuals associated with the charitable funder provide advice regarding grants from the fund. As an example: a church establishes a fund at a community foundation to accept contributions to support various charitable activities of the church. The church understands the requirements of a component fund, and wants to benefit from the financial management and investment of the community foundation, while keeping the fund assets separate from the general operating funds of the church. The church intends to appoint a committee of church members to advise the community foundation regarding distributions from the fund. Occasionally, the church may want to recommend a grant from the fund to itself, for an unexpected need such as a building repair. If the fund were considered a donor advised fund, Section 4967 would prohibit such a grant due to the benefit flowing back to the donor. The Council believes such a prohibition does not reflect the intent of Section 4967 and the purpose of prohibiting benefits from donor advised funds to individual donors rather than other charitable organizations.

#### Other Funds with Limited Advisory Privileges

The Council requests that the Secretary except from the definition of donor advised funds certain scholarship funds (student loan forgiveness described below) and other funds regarding which donors have limited advisory privileges. The Council previously submitted this proposal in its 2016 letter to Treasury regarding the Priority Guidance Plan. We reiterate this proposal for your consideration in the coming Priority Guidance Plan.

As stated above, the Pension Protection Act of 2006 and IRC Section 4966 codified the definition of “donor advised fund.” Section 4966 also provides for several important exceptions to the definition of donor advised fund; specifically:

- A fund that makes distributions only to a single identified organization or government entity
- A fund with *limited donor advisory privileges* the purpose of which is to provide grants to individuals for travel, study or similar purposes (the “scholarship exception”)

To qualify for the scholarship exception, several rules related to donor participation must be followed including:

- The donor (or person appointed or designated by the donor) exercises his/her advisory privileges exclusively as a member of a committee, all members of which are appointed by the sponsoring organization
- No combination of donors, persons appointed or designated by the donor, or persons related to either, may control, directly or indirectly, the committee
- All grants from the fund must be awarded according to objective and nondiscriminatory criteria approved in advance by the board of the sponsoring organization and procedures meeting certain requirements of IRC Section 4945(g)

Many community foundations maintain donor advised funds in which the donor, or persons appointed or designated by the donor, expect, and are given sole advisory privileges regarding, the distributions or investment of the fund. Many community foundations also maintain funds that comply with the “scholarship exception” rules and allow donor participation, but only as part of a committee appointed by the sponsoring organization. Finally, many community foundations maintain various other types of funds, including field of interest funds, designated funds and geographic affiliate funds, and allow varying degrees of participation by one or multiple donors in decisions related to distributions from these funds. Often referred to as “advisory committees,” these groups, made up of donors and other community members, provide valuable recommendations and input to the sponsoring organization.

Funds should be excluded from the definition of donor advised funds if the sponsoring organization (as opposed to the donor or related parties) either (a) controls the advisory committee that selects grant recipients, (b) appoints the fund advisors, or (c) the fund is not separately identified by reference to contributions of a donor or donors.

The Council also proposes that “Community Informed Funds” be recognized as non-donor advised funds. These funds operate with donor and community involvement and have been in practice at community foundations for many years, long before the Pension Protection Act of 2006. There are no specific rules regarding how and when a donor or other members of the community can advise or be involved with these funds, and it would be helpful to have these issues specifically addressed through regulations. Community Informed Funds serve an important function for the community foundation by providing a vehicle for community engagement and facilitate the foundation’s role as a community partner, leader and convener that actively brings other community institutions, resources and individuals together to address a community’s greatest opportunities and critical challenges.

The Council further proposes that guidelines be adopted to define a consistent approach to donor and community involvement with these funds and provide assurance to community foundations that an option exists, outside the donor advised fund model, for donors and community members to be engaged with particular funds and grant making decisions without the restrictions placed on donor advised funds.

## **2. Student Loan Forgiveness**

With many U.S. communities struggling to retain local college graduates as part of their economic growth strategies, community foundations are exploring programs or funds that would offer student loan forgiveness to individuals who agree to live and work in these smaller communities. This assistance would be in addition to or in replacement of traditional scholarship programs. These types of programs offer the added benefit of addressing the student loan crisis affecting many young adults.

We believe that foundation-sponsored student loan forgiveness programs should be treated as qualifying distributions for purposes of 4945(g)(1) and that providing student loan forgiveness to low-income individuals is a charitable purpose within the meaning of Section 170(c)(2)(B).

Student loan forgiveness should qualify as scholarships for qualified tuition and related expenditures under section 117 and that the student should not have cancellation of indebtedness income because of such forgiveness, which would undermine the effectiveness of such relief efforts.

Foundations view student loan forgiveness programs as one part of an overall economic development strategy. Treasury has a history of providing Revenue Rulings, Private Letter Rulings, and additional examples regarding economic development as a charitable purpose; and the Council is requesting specific guidance related to student loan forgiveness programs in an economic development context.

While we are not suggesting a government sponsored program, the student loan forgiveness program could resemble the structure of the National Health Service Corps Loan Repayment Program for medical professionals or the Teacher Loan Forgiveness program for teachers committing to serve a specific period of time in a high-need area. The program dollars are primarily intended to help pay off student debt. Foundations would work with donors to raise funding for the program and the foundations would manage the administration of the program. Award recipients are expected to live and work in their communities to be eligible for the program.

This program is a response to foundations investing in students via scholarships only to see them use that investment to leave the community that provided the scholarship. Donors are excited by the idea of supporting the community by offering students an opportunity to return and to receive assistance with the burdensome student debt regularly in the headlines. Our foundation members have an opportunity to bring young people back to high-need communities, slow or reverse the “brain drain,” bring skilled, educated and trained professional into high-need communities, increase entrepreneurship, fill skilled and educated job openings, and give farmers and small shop owners hope that a family member or community member will take over their business.

Guidance from Treasury including foundation sponsored student loan forgiveness programs would be a critical step facilitating an important new tool for our communities to build resiliency and talent.

### **3. Clarification of Economic Development as Charitable Activity**

The Council seeks further clarification regarding when economic development will be considered a charitable activity and requests reliable guidance for foundations wishing to support such activity with charitable dollars.

The Council often fields questions from its foundation members regarding economic development. Community foundations in particular are interested in creating funds and using charitable dollars to support activities such as redevelopment of city centers, small business incubation, job training programs, home purchase assistance, and promotion of local communities for new business relocation and tourism. As guidance in this area, we can look at several rulings dating to the 1970s that provide guidance regarding the factors that will support a finding by the IRS that an activity is charitable. We also have several more recent rulings, whereby the Service has determined that certain activities are not charitable. There is a consensus in the field that this type of guidance

needs to be reconciled to provide a consistent test that can be applied by Foundations and other organizations working in economic development. Foundations are also often asked to partner with local government entities and organizations qualified as tax-exempt but are not Section 501(c)(3) organizations, and guidance specifically addressing these types of partnerships is needed as well.

The Council urges the Treasury to consider updating previous guidance regarding economic development as a charitable activity by providing a more definitive test and/or examples of acceptable charitable activities that reflect the current needs and economic climate in many communities. For reference, we are including examples involving fact patterns encountered by the Council's foundation members that Treasury could utilize in illustrative guidance. These examples were also provided by the Council in our 2016 letter regarding the Priority Guidance Plan.

- The Chamber of Commerce is sponsoring an initiative to encourage new small businesses to locate in a deteriorating section of downtown. They approach a community foundation about establishing a charitable fund to solicit and collect charitable contributions from individuals and businesses. The community foundation will then make grants to assist individuals with expenses associated with establishing new small businesses provided they agree to locate in this particular area. The grants will be awarded based on an objective and nondiscriminatory application process. No grants will be awarded to the Chamber of Commerce, but members of the Chamber may volunteer as part of the application review committee.
- A rural airport needs to build a new control tower. The airport is owned by a governmental entity (the airport authority) and is used by the public. The authority would like to accept charitable contributions for this purpose, or work with a community foundation to establish a temporary fund that would accept contributions and make grants to the authority to be used for the building expenses.
- A rural municipality desires to expand internet services to its citizens and wants to collect charitable donations to build infrastructure.
- A city government wants to promote the city as a location for filming television and movies and wants to establish a charitable fund to collect donations to be used to pay expenses of a promotional campaign.

#### **4. Executive Order 13771**

Recognizing Executive Order 13771, along with related guidance issued by the Office of Information and Regulatory Affairs (OIRA), which is part of the White House Office of Management and Budget (OMB), the Council on Foundations hopes to be a resource to the Treasury regarding how philanthropy engages in self-regulation. The Council on Foundations also recognizes the importance of Treasury's ability to issue new rules given the current discussion on tax reform and multi-year requests for further guidance on existing regulations (discussed above). We hope working with you will provide opportunities to identify existing rules that can be eliminated or offset because they are ineffective, overbroad, contradictory, or obsolete. We are working with our members to identify these areas and will share what we learn from them. In addition, we'd like to share nongovernmental practices within philanthropy with you. Philanthropy has long standing fiduciary practices and private sector conformity assessment such as stewardship principles and the National Standards for U.S. Community Foundations® accreditation body. The

Council on Foundations is open to stakeholder-driven regulatory tools, such as serving on official agency rulemaking committees to issue recommendations to the agency on specific rules.

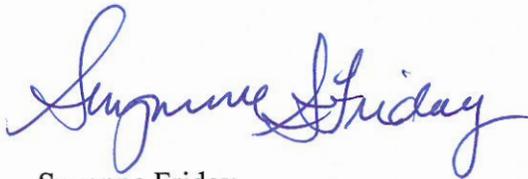
### **Johnson Amendment**

We urge the IRS and Treasury to continue enforcing the prohibition against political activity by Section 501(c)(3) organizations and to maintain the standard established in Revenue Ruling 2007-41 and other published guidance that limit political campaign intervention. It is critical to preserve the demarcation between political activity and charitable activity for the good of the sector. We are concerned that if Section 501(c)(3) organizations are permitted to engage in political activity, donors will use them to claim charitable contribution deductions and anonymity for political contributions. To the extent regulation in this area is desirable, Treasury may wish to consider offering a legislative proposal to deem all funds used for political activity to have been conducted by a Section 527 organization, which are designed for that purpose and include an appropriate disclosure mechanism.

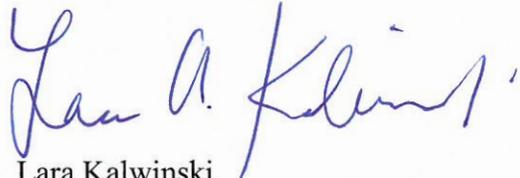
### **Conclusion**

Thank you for the opportunity to comment on priorities to include in the 2017-2018 Priority Guidance Plan. We would welcome the opportunity to discuss any of these matters with the IRS or with the Department of Treasury if it would be helpful. Please contact me for additional information or analysis on any of these topics.

Sincerely,



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### **CC:**

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