DONOR ADVISED FUNDS

Issue Paper

> ***We Urge You to Demonstrate Your Support for Philanthropy by:***
>
> - Expanding the IRA rollover to DAFs, and preserving philanthropy's ability to serve communities across the country through the use of donor advised funds.

ISSUE

A donor advised fund (DAF) is a type of charitable giving fund that is established by a donor with an eligible charitable sponsoring organization (i.e. a community foundation) to support a cause (or causes) that the donor cares about. A donor advised fund allows the donor to remain involved and active in charitable giving by retaining "advisory privileges" to recommend how the sponsoring organization should make grants from that fund.

Some skeptics believe that donor advised funds are a mechanism for circumventing federal income taxes—referring to them as "warehouses of wealth." As such, these critics have influenced a policy conversation that has sparked varying proposals for payout requirements (both with respect to an amount payout, or payout over a specified period of time—i.e. a 5% annual payout, or a spend-down over a certain number of years).

POSITION

The Council strongly opposes any proposals that require a DAF to pay out a percentage of funds each year, or to exhaust funds within a specified period of time. Such proposals are misguided as to the realities of donor advised funds, and would be more harmful than helpful to supporting charitable causes in communities across the country.

The Council supports efforts to preserve and expand the ability of individuals to remain involved in community philanthropy through the use of DAFs. Donor advised funds are a unique philanthropic tool that allows individuals to remain involved in supporting charitable programs and initiatives in their communities beyond the single moment-in-time that a charitable contribution is made.

The Council also supports the clarification of certain issues related to DAFs. Carefully crafted regulations from the U.S. Department of Treasury are necessary to provide the nonprofit sector and public with additional guidance about the donor advised fund provisions in the *Pension Protection Act of 2006*—specifically:

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

RATIONALE

Donor advised funds are a unique philanthropic tool available for Americans to direct their philanthropic giving to support programs that build their communities and remain involved in supporting the causes and issues they care about. Community foundations, in particular, enable people to "give where they live" through such tools, and employ subject-matter experts with in-depth community knowledge to manage DAFs.

Establishing this type of fund with a community foundation provides the assurance of expert administration and stewardship of those charitable dollars, as well as the extensive knowledge of the community to inform decisions about how grants are made.

Furthermore, DAFs offer a greater level of flexibility in grantmaking than other fund types—which is crucial in responding to unanticipated community crises. For example, if there is a wildfire, hurricane, water contamination, or other tragic event, a community foundation in consultation with a donor advisor has the ability to respond quickly and make a grant to address that issue—whereas other funds managed by that community foundation may have less flexibility because they are reserved for supporting specific, non-related issue areas (i.e. education) or are already committed to be granted as part of a specified grant cycle.

The premise of requiring a payout for DAFs rests on the idea that donors are using these vehicles to "store" their personal dollars in tax-exempt "accounts" that require no further action or involvement by the donor. This premise is false for a handful of reasons. First, in order to claim the charitable deduction for a contribution to a 501(c)(3) organization (including a contribution to a donor advised fund—which are held within 501(c)(3)s such as community foundations), the donor must completely relinquish control of those dollars. This means that from the moment a donation is made, the community foundation possesses ultimate control and decision-making power over how those dollars are granted. This principle is commonly referred to as "variance power," and has historically been the hallmark of community foundations: the ability of the governing body to exercise the legal function of *cy pres* without having to first obtain court approval.

The second reason why this premise is incorrect is that it assumes donor intent for the establishing a DAF is sweeping, and overwhelmingly malicious—to shield dollars from being subject to taxes under the guise of charitable purpose. Again, this is just not correct. There are countless reasons why an individual would establish a DAF for genuinely charitable purposes—including: 1) needing help from community foundation experts to manage complex assets donated for charity, 2) seeking an alternative to a private foundation that will allow a relatively small contribution to grow over time and provide a sustained capacity for giving, 3) the donor intends to instill values of charitable giving within his or her family, and so on. As further evidence that donors predominantly establish DAFs with genuine charitable intent, a 2014 Survey of Community Foundations by the Urban Institute reports that 88% of foundations shared that donor advisors participate in special events held by the community foundation, and 81% report that donor advisors serve on the foundation's board or in another leadership role.

Lastly, the premise assumes that DAFs lay dormant after they are established—or at least that sponsoring organizations take no action to ensure that grants are actively being made from a DAF. In fact, as of January 1, 2017, the National Standards for U.S. Community Foundations® accreditation program implemented a fund activity policy requirement that all participating foundations must adhere to in order to remain compliant and maintain their accreditation status. Of the nearly 750 community foundation in the U.S., over 500 have voluntarily gone through the rigorous and time-consuming accreditation process in order to demonstrate their commitment to integrity and accountability as stewards of charitable dollars in communities.

RELEVANT LAW & LEGISLATION

Pension Protection Act (PPA) of 2006. When the PPA became law, it provided the first legal definition by Congress of a DAF as 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 privileges with respect to investments or distributions. The PPA also laid out basic rules and criteria for making grants from DAFs.

H.R. 1, Tax Reform Act of 2014. This bill, introduced in December of 2014 by then Chairman of the House Ways & Means Committee Dave Camp (R-MI-4), was the culmination of tax reform discussions during Camp's tenure as Chairman and was intended for use as a discussion draft for sparking momentum toward comprehensive tax reform.

This bill proposed a requirement that for every dollar contributed to a DAF, the same amount would need to be granted out within five years of the contribution or would otherwise be subject to a 20 percent excise tax. Essentially, this would have imposed a mandate to exhaust (or, "payout") the entirety of the fund within five years of establishment, unless additional contributions to the fund were made in the years following the original contribution. This payout requirement on a rolling basis would effectively eliminate the option of endowing a DAF, and would create a great administrative burden on the community foundation to calculate how much must be granted out over a specific time frame.

PATH Act (Protecting Americans from Tax Hikes). When the PATH act became law in December of 2015, it made the IRA charitable rollover permanent law.

The IRA charitable rollover was a provision that was formerly included as part of the charitable "tax extenders"—which required renewal by Congress every 1 – 2 years. In December of 2015, the IRA charitable rollover was made permanent by Congress and signed into law by President Obama as part of the *Protecting Americans from Tax Hikes (PATH) Act*.

Though this marked a momentous occasion for philanthropy, it failed to acknowledge that community foundations make as much as two-thirds of their grants from donor advised funds—and though community foundations were made eligible to be the recipients of IRA rollover contributions, DAFs held by community foundations were excepted.

H.R. 4709, Grow Philanthropy Act. This bill, introduced by Representative George Holding (R-NC-13) in April of 2016, would expand the IRA charitable rollover to allow for distributions to donor advised funds (DAFs).

This bill became null when the 114th Congressional session ended in December 2016.

S. 2750, CHARITY Act of 2016 (Charities Helping Americans Regularly Throughout the Year). This bill, introduced by Senators John Thune (R-SD) and Ron Wyden (D-OR) in April of 2016, contained a provision—to accompany the *Grow Philanthropy Act (HR. 4709)*—to expand the IRA charitable rollover to allow for distributions to DAFs.

This bill also would have required sponsoring organizations (i.e. community foundations) to 1) disclose whether they adhere to an "inactive" or "dormant" funds policy, and if so, to describe and attach the policy with their Form 990; and 2) to calculate and disclose average percentage of grants made from all managed DAFs during the current tax year and the immediate three years preceding.

This bill became null when the 114th Congressional session ended in December 2016.

S. 1343, CHARITY Act of 2017 (Charities Helping Americans Regularly Throughout the Year).

Senators John Thune (R-SD) and Bob Casey (D-PA), with Pat Roberts (R-KS) and Ron Wyden (D-OR), introduced the Charities Helping Americans Regularly Throughout the Year

(CHARITY) Act on June 13, 2017. The bill includes sense of the Senate language stating that "Congress should ensure that the value and scope of the deduction for charitable contributions is not diminished during a comprehensive reform of the tax code." Additionally, this bill would expand the IRA charitable rollover to allow for distributions to donor advised funds (DAFs), as well as simplifying the private foundation excise tax from the current two-tiered structure to a flat rate of one percent.

RESOURCES

2014 Urban Institute Survey of Community Foundations Overview:
http://www.cof.org/sites/default/files/documents/files/Urban-Survey-Summary.pdf

2014 Urban Institute Survey of Community Foundations Story Map:
http://www.cof.org/sites/default/files/documents/files/DAF_Map.pdf

Donor Advised Fund Letter of Support from the Field:
http://www.cof.org/news/donor-advised-fund-letter-support

National Standards for U.S. Community Foundations:
http://www.cof.org/public-policy/community-foundation-standards

For more information, contact the Council's Government Relations team at
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Or, visit our website at: www.cof.org/public-policy/issues.