

June 9, 2023

Internal Revenue Service  
Attn: CC:PA:LPD:PR (Notice 2023-36) Room 5203  
P.O. Box 7604  
Ben Franklin Station  
Washington, D.C. 20044

**RE: Recommendations for 2023-2024 Priority Guidance Plan Notice 2023-26**

Greetings:

On behalf of the Council on Foundations (the Council), we write to urge the Treasury Department and the Internal Revenue Service to include the items outlined below in the 2023-2024 Priority Guidance Plan.

The Council is a nonprofit membership association that serves as a guide for philanthropies as they advance the greater good. Building on our almost 75-year history, the Council supports over 850 member organizations in the United States and around the world to build trust in philanthropy, expand pathways to giving, engage broader perspectives, and co-create solutions that will lead to a better future for all.

Our foundation members, and the organizations that they help fund, would benefit significantly from further clarity on each regulatory issue outlined below.

- Donor Advised Funds: Regulations Addressing Certain Issues
- Foundation-Sponsored Student Loan Forgiveness Programs
- Provide Guidance on Economic Development as a Charitable Activity
- Update Guidance Relating to Grants to Mexican Charities under the U.S.-Mexico Income Tax Convention (the "Treaty")
- Address Tax-Exemption Granted to Organizations Promoting Discrimination and Violence
- Request for Clarification on Application of Corporate Alternative Minimum Tax to Tax-Exempt Organizations

To assist Treasury in developing guidance, the Council has compiled information as well as examples of situations our members have encountered that illustrate the need for guidance in each area described above.

**Donor Advised Funds: Regulations Addressing Certain Issues**

We support the continuation of the work that Treasury and the IRS have done to provide guidance on donor advised funds ("DAFs"), and particularly believe that proposed regulations under sections 4966 and 4967 should be a high priority. Seventeen years have passed since the Pension Protection Act of 2006 codified the definition of DAFs in section 4966 of the Internal Revenue Code, and yet there are no regulations that provide guidance on how those definitions should be applied. In addition, new proposals

regarding DAFs build on sections 4966 and 4967 and would result in additional confusion and uncertainty if there continues to be little guidance.

Under sections 4966 and 4967, a fund that meets the definition of a DAF must be managed subject to certain restrictions on “taxable distributions” and the provision of more than an “incidental benefit” on disqualified persons and may result in significant taxes. These rules also generally prohibit DAFs from making grants to individuals or grants to non-charities and certain other organizations unless the sponsoring organization exercises expenditure responsibility over the grant.

Although we have concerns regarding some of the proposals in Notice 2017-23, we appreciate the guidance on pledges and bifurcated payments. However, there are still significant areas in which DAF sponsors have had no guidance from Treasury or the IRS. This lack of guidance results in inconsistency across the sector and confusion for sponsoring organizations and donors contributing to DAFs. It has also hampered our efforts to establish standards for sponsoring organizations.

For example, there is no guidance on the key terms in the statute, including the definition of what is and what is not a donor advised fund, as well as what constitutes advice that confers more than an incidental benefit upon a disqualified person. Regulations can also provide certainty to sponsoring organizations, so they know the parameters and where there is room for innovation in improving philanthropy using DAFs. The Council would be pleased to offer the IRS both our assistance and the experience of our members to help bring this rulemaking effort to fruition expeditiously.

### **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 for the benefit of individuals, such as backpacks full of school supplies to schools to then be distributed to the students. 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 unclear whether distributing the school supplies to schools for the benefit of children is a taxable distribution. Regulations clarifying whether and how sponsoring organizations may use donor advised funds to make in-kind distributions would be helpful as these issues regularly occur and sponsoring organizations may have differing interpretations of what is acceptable under the statute.

### **Exemptions or Exclusions for Certain 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, 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 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.

With respect to private foundation use of DAFs, we understand the concern about qualifying distributions to DAFs without a timeline for the subsequent distribution of those funds out of the DAF. Many private foundations use DAFs for various activities, including simplifying grantmaking activities, partnering with their local community foundation on grantmaking, or other reasons related to their strategic grantmaking. The proposal to require distribution from a DAF in a year will significantly limit some of those legitimate uses as well as create undue burden on the different organizations. Therefore, we request that guidance allow private foundations five years to advise funds out of the DAF and be considered a qualifying distribution.

## Other Funds with Limited Advisory Privileges

The Council requests that the Secretary except from the definition of DAF certain scholarship funds (student loan forgiveness described below) and other funds regarding which donors have limited advisory privileges.

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 DAF, 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 individual 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 the 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. They 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.

### **Foundation-sponsored Student Loan Forgiveness Programs**

With many U.S. communities struggling to retain local college graduates as part of their economic growth strategies, community foundations are exploring programs for funds that would offer student loan forgiveness to individuals who agree to live and work in these smaller communities. This assistance would 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 individuals is a charitable purpose within the meaning of section 170(c)(2)(B), similar to the qualification of scholarships.

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

While these are not government-sponsored programs, the student loan forgiveness program in any guidance could resemble the structure of the National Health Services Corps Loan Repayment Program for medical professional or the Teacher Loan Forgiveness program for teachers committing to serve a specific period in a high-need area. The program dollars are primarily intended to help workers 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 funding, and any payments would go directly to the lenders.

These programs are a response to foundations investing in students via scholarships only to see them use that investment to leave the community. Donors are excited by the idea of supporting the community by offering graduates 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 professionals in high-need communities, increase entrepreneurship, fill skilled and educated job openings, and give farmers and small business 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 tool for our communities to build resiliency and talent.

### **Provide Guidance on Economic Development as a Charitable Activity**

The Council seeks further clarification regarding when economic development activities 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 members regarding economic development. Community foundations have been 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. Since the start of the pandemic, this desire has expanded to help businesses and workers that were heavily impacted by the COVID crisis. Foundations and philanthropies have also been on the forefront of rebuilding as the crisis abates.

Foundations have been able to 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 IRS has determined that certain activities are not charitable. However, it can be particularly difficult to determine when and how organizations can support for-profit businesses or work with governmental entities. As the world of philanthropy has grown and developed over the past forty years, there is a consensus in the field that this type of guidance needs to be provided so there is a consistent test that can be applied by foundations and other organizations working in economic development.

The Council urges Treasury to consider updating previous guidance regarding economic development as a charitable activity in ways that can also be helpful for those organizations continuing to work in COVID relief, 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.

- 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 to this 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 government 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.
- The 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.

## **Address Tax-Exemption Granted to Organizations Promoting Discrimination and Violence**

We understand that tax-exemption is available for organizations that provide education and advocacy on a wide range of issues. It is also clear that organizations that promote racial and ethnic discrimination and violence are neither educational nor charitable. We encourage the IRS to continue to enforce the requirements for educational activity set forth in Revenue Procedure 86-43 and deny or revoke exemption to organizations that are not operating as a charitable entity. We also urge consideration of whether the guidance can be updated to address online and social media activity.

## **Request for Updated Guidance under the U.S.–Mexico Income Tax Convention**

Under Article 22 of the U.S.–Mexico Income Tax Convention (the “Treaty”), and Article 17 of the Protocol to that convention, the U.S. and Mexico have agreed that certain Mexican charities meeting standards “essentially equivalent” to those applicable to U.S. public charities (originally those described in Article 70-B of the Mexican Income Tax Law) would be treated as public charities for purposes of grants from U.S. public charities and private foundations. Such Mexican charities are also exempt from U.S. income taxes to the same extent as their U.S. counterparts, and charitable contributions to such Mexican charities are eligible for U.S. income tax deductions (subject to some limitations).

In Information Letter 2003-158 (Sept. 30, 2003), the IRS confirmed that U.S. grantmakers could rely on the Mexican Ministry of Finance and Public Credit’s determination of Article 70-B status, set forth either in a letter from that agency providing special authorization under Article 70-B, or reflected in the current official list of Mexican charities published in the Mexican *Official Gazette* (*el diario oficial de la Federacion*). That guidance, however, is now out of date. Mexico has renumbered its income tax provisions a few times since ratification of the Treaty; for more than a decade, former Article 70-B has been found in Article 97. However, it was moved to Article 82 of a Mexican Income Tax Law that took effect January 1, 2014, which also contains provisions governing other types of charities. There have been some minor substantive changes made to Article 97 at various points over the years. Article 82

includes additional changes (particularly regarding activities influencing legislation), and it was further amended in legislation that took effect April 23, 2021. However, the core requirements for public charities under former Article 70-B (to be organized and operated exclusively for exempt purposes, to avoid private inurement, to have a valid dissolution clause, etc.) are still in place.

The most current version of the list of Mexican charities eligible to receive tax-deductible contributions is available online at <https://www.sat.gob.mx/consultas/27717/conoce-el-directorio-de-donatarias-autorizadas>. Those organizations qualifying for treaty benefits have been specially designated as type "M" organizations; the list expressly states that such organizations meet the requirements of Article 82, formerly Article 70-B.

Until 2014, private foundations and other donors could generally rely on the Mexican authorities' determination that an organization qualified under Article 97 and former Article 70-B to treat it as a public charity. However, the recent changes inhibit many grantmakers from relying on the Mexican Treaty until Treasury and the IRS provide clear guidance about how it applies following the changes made to the Mexican Income Tax Law. We would specifically request that Treasury, consulting with the Mexican government as necessary, do the following:

- Identify the class of Mexican charities that will be treated as "essentially equivalent" to sections 509(a)(1) and 509(a)(2) public charities under the new Mexican Income Tax Law in effect as of January 1, 2014 and provide updated information as to the documentation upon which U.S. grantmakers can rely for purposes of determining status of a Mexican organization under the Treaty.
- Confirm that under Article 2(4) of the Treaty, section 4966's excise tax is a subsequently added excise tax "identical or substantially similar" to section 4945, and that donor advised funds can therefore rely on the Treaty to the same extent as private foundations and other public charities.

The Council continues to hear from members about issues arising from Mexico's anti-money laundering and anti-terrorist financing rules that are causing considerable confusion among U.S. grantmakers and are having an impact on the grantmaking authorized by the Treaty. Public statements by officials from the Treasury financial crimes enforcement agency, FinCEN, indicate that there has been coordination between Mexico and FinCEN on various enforcement matters. Many of the concerns of our members arise from confusion regarding the nature and extent of information that U.S. grantmakers must provide to the Unidad de Inteligencia Financiera ("UIF"), particularly personal identifying information. Given the impact of the rules on Treaty-authorized grantmaking, we ask that Treasury consider raising the need for greater clarity in the reporting obligation when it discusses the Treaty issues with Mexico noted above.

### **Request for Clarification on Application of Corporate Alternative Minimum Tax to Tax-Exempt Organizations**

The Inflation Reduction Act of 2022 established a corporate alternative minimum tax (CAMT) for certain "applicable corporations" with average annual "adjusted financial statement income" (AFSI) exceeding \$1 billion for the preceding three taxable years. Section 56A(c)(12) of the IRC provides that tax-exempt



nonprofit corporations' AFSI will be "adjusted to only take into account any AFSI—(A) of an unrelated trade or business (as defined in section 513) or such organization, or (B) derived from debt-financed property (as defined in section 514) to the extent that income from such property is treated as unrelated business taxable income (UBTI)."

As enacted, section 56A(c)(12) creates some ambiguity regarding the calculation of AFSI by tax-exempt organizations for purposes of determining whether they meet the definition of an "applicable corporation" and for determining their CAMT, if necessary. While section 56A(c)(12)(A) refers to income from an organization's "unrelated trade or business" as defined in section 513, it includes no reference to the various modifications to an organization's UBTI available under section 512(b), which allow for the exclusion of certain types of income—such as dividends, interest payments, royalties, or rents—from UBTI unless that income is derived from debt-financed property. The Council requests guidance clarifying that a tax-exempt organization's AFSI under section 56A(c)(12)(A) does not include any income that would be excluded from UBTI under section 512(b)—such as dividends, interest payments, royalties, or rents—except to the extent that such income excluded under section 512(b) is derived from debt-financed property.

## **Conclusion**

Thank you for the opportunity to comment on priorities to include in the 2023-2024 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. In particular, the Council offers its support for convening more informal discussions of the compliance issues faced by U.S. grantmakers. Please contact me for additional information or analysis on any of these topics.

Sincerely,

Kathleen P. Enright  
President and CEO  
Council on Foundations