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Request for Comments on Application of Excise Taxes With Respect to Donor Advised Funds in Certain Situations

Notice 2017-73

SECTION 1. PURPOSE

This notice describes approaches that the Department of the Treasury (Treasury Department) and the Internal Revenue Service (IRS) are considering to address certain issues regarding donor advised funds (DAFs) of sponsoring organizations and requests comments on those approaches. Specifically, the Treasury Department and the IRS are considering developing proposed regulations under § 4967 of the Internal Revenue Code (Code) that would, if finalized, provide that: (1) certain distributions from a DAF that pay for the purchase of tickets that enable a donor, donor advisor, or related person under § 4958(f)(7), to attend or participate in a charity-sponsored event result in a more than incidental benefit to such person under § 4967; and (2) certain distributions from a DAF that the distributee charity treats as fulfilling a pledge made by a donor, donor advisor, or related person, do not result in a more than incidental benefit under § 4967 if certain requirements are met. In addition, the Treasury Department and the IRS are considering developing proposed regulations that would change the public support computation for organizations described in §§ 170(b)(1)(A)(vi) and 509(a)(1) and in § 509(a)(2) to prevent the use of DAFs to circumvent the excise tax rules applicable to private foundations under Chapter 42 of the Code. This notice requests comments regarding the issues addressed in the notice as well as certain other issues.

SECTION 2. BACKGROUND

Section 4966(d)(2) defines a DAF as a fund or account owned and controlled by a sponsoring organization, which is separately identified by reference to contributions of a donor or donors, and with respect to which the donor, or any person appointed or designated by such donor (donor advisor), has, or reasonably expects to have, advisory privileges with respect to the distribution or investment of the funds. Section 4966(d)(2)(B) excepts from the definition of DAF any fund or account which makes distributions only to a single identified organization or governmental entity, or certain committee-advised funds that make grants to individuals for travel, study, or other similar purposes.

Section 4966(d)(1) defines a sponsoring organization as an organization that: (1) is described in § 170(c) (other than a governmental unit described in § 170(c)(1), and without regard to the requirement under § 170(c)(2)(A) that the organization be organized in the United States); (2) is not a private foundation (as defined in § 509(a)); and (3) maintains one or more DAFs.

Under § 170(f)(18), a deduction otherwise allowable under § 170(a) for a contribution to a DAF is allowed only if:

- (A) the sponsoring organization is described in § 170(c)(2) and is not a “type III supporting organization,” as defined in § 4943(f)(5)(A) (other than a functionally integrated type III supporting organization as defined in § 4943(f)(5)(B)); and
- (B) the taxpayer obtains a contemporaneous written acknowledgment from the sponsoring organization of the DAF that the sponsoring organization has exclusive legal control over the assets contributed.

Section 4966 imposes an excise tax on each taxable distribution from a DAF.

This excise tax is paid by the sponsoring organization. A separate excise tax, paid by fund managers, is imposed on the agreement of any fund manager to the making of a distribution, knowing that it is a taxable distribution. In general, under § 4966(c), a taxable distribution is any distribution from a DAF to any natural person, or to any other person if (i) the distribution is for any purpose not specified in § 170(c)(2)(B), or (ii) the sponsoring organization does not exercise expenditure responsibility with respect to such distribution in accordance with § 4945(h).

Under § 4966(c)(2), a taxable distribution does not include a distribution from a DAF to: (1) any organization described in § 170(b)(1)(A) (other than a disqualified supporting organization as defined in § 4966(d)(4)); (2) the sponsoring organization of such DAF; or (3) any other DAF.

Section 4967 imposes an excise tax on the advice that a person described in § 4967(d) provides regarding a distribution from a DAF that results in such person or any other person described in § 4967(d) receiving, directly or indirectly, a more than incidental benefit. Section 4967(d) refers to § 4958(f)(7), which describes a donor, donor advisor, a family member of a donor or donor advisor, or a 35-percent controlled entity of such persons as defined in § 4958(f)(3) (with the modifications described in § 4958(f)(7)(C)). This excise tax is paid by any person who advises the sponsoring organization as to the distribution or who receives the prohibited benefit. A separate excise tax, paid by fund managers, is imposed on the agreement of any fund manager of the sponsoring organization to the making of the distribution, knowing that it would confer a prohibited benefit. Section 4967(b) provides that, with respect to any distribution, no tax shall be imposed under § 4967 if a tax has been imposed under

§ 4958.

Section 4958 imposes an excise tax on any “excess benefit transaction.” Section 4958(c)(1) defines an excess benefit transaction generally as any transaction in which an economic benefit is provided by an applicable tax-exempt organization (including a § 501(c)(3) sponsoring organization of a DAF) directly or indirectly to or for the use of a disqualified person (including in the case of any transaction that involves a DAF a donor, donor advisor, or a person related to a donor or donor advisor, as described in § 4958(f)(7)), if the value of the economic benefit provided exceeds the value of the consideration received. In general, the term “excess benefit” refers to the amount by which the value of the economic benefit provided exceeds the value of the consideration received. Section 4958(c)(2) provides that, in the case of any DAF, an excess benefit transaction also includes any grant, loan, compensation, or other similar payment from the DAF to a donor, donor advisor, or related person. For purposes of this special rule for DAFs, the excess benefit includes the full amount of the grant, loan, compensation, or other similar payment. This excise tax under § 4958 is paid by the disqualified person with respect to the transaction. A separate excise tax, paid by organization managers, is imposed on the participation of any organization manager in the transaction, knowing that it is an excess benefit transaction, unless such participation is not willful and is due to reasonable cause.

Notice 2006-109, 2006-2 C.B. 1121, provided interim guidance on several DAF issues, including criteria for determining whether a supporting organization is a disqualified supporting organization, exclusion of certain employer-sponsored disaster relief funds from the definition of DAF, and transitional rules for educational grants. The

notice also requested comments regarding suggestions for future guidance on DAFs.

Notice 2007-21, 2007-1 C.B. 611, requested comments in connection with a study conducted by the Treasury Department and the IRS on the organization and operation of DAFs and supporting organizations, as required by § 1226 of the Pension Protection Act of 2006, Pub. L. No. 109-280, 120 Stat. 780 (2006).

In response to these notices, the Treasury Department and the IRS received a number of comments requesting guidance on various DAF issues. Several commenters indicated that guidance would be particularly helpful regarding whether § 4967 prohibits a donor, donor advisor, or person related to a donor or donor advisor of a DAF from advising a DAF distribution to pay the cost of any such person's attendance or participation in a charity-sponsored event or to fulfill the person's charitable pledge. The commenters noted that some DAF sponsoring organizations prohibit such DAF distributions, but others do not. One commenter expressed concern about improper use of DAFs by persons seeking to avoid application of the private foundation rules under Chapter 42 of the Code.

While the Treasury Department and the IRS continue to develop proposed regulations that would, if finalized, comprehensively address donor advised funds, this notice is intended to provide interim guidance on these specific issues and to solicit additional comments in anticipation of the issuance of further guidance.

SECTION 3. CERTAIN DISTRIBUTIONS FROM A DAF PROVIDING A MORE THAN INCIDENTAL BENEFIT TO A DONOR, DONOR ADVISOR, OR RELATED PERSON

Several commenters requested guidance on whether a distribution from a DAF to an organization described in § 501(c)(3) (a "charity") that enables a donor, donor advisor, or related person under § 4958(f)(7) (collectively referred to in this notice as a

“Donor/Advisor”) to attend or participate in an event results in the Donor/Advisor receiving a more than incidental benefit under § 4967.

Several commenters suggested that a distribution from a DAF should not be considered as conferring a more than incidental benefit as long as the amount of the distribution from the DAF does not exceed the portion of the ticket cost that would be deductible under § 170 if paid by the Donor/Advisor directly and the Donor/Advisor separately pays for the non-deductible portion. For example, if a charity sells tickets to a charity-sponsored event for \$1,000 per ticket and notifies purchasers that the fair market value of each ticket is \$100, then (assuming that the requirements of § 170 are satisfied), a person who purchases a ticket for \$1,000 may deduct up to \$900 of the payment as a charitable contribution. These commenters suggested that a Donor/Advisor with respect to a DAF does not receive a more than incidental benefit if the Donor/Advisor pays the \$100 ticket value and the sponsoring organization, on the advice of a Donor/Advisor, distributes \$900 from the DAF to the charity to pay the rest of the cost of the ticket, because the Donor/Advisor’s position is the same as if the Donor/Advisor had paid the full cost of the ticket (\$1,000) and claimed a \$900 charitable contribution deduction.

One commenter offered the contrary view that an arrangement under which a Donor/Advisor pays only the nondeductible portion of the cost of a ticket to a charity event and advises a DAF distribution to pay the deductible portion of the cost results in a more than incidental benefit, because but for the DAF distribution the Donor/Advisor would not have received the benefits that the ticket provides. Under this view, the \$900 distribution from the DAF in the example relieves the Donor/Advisor from a financial

obligation that the Donor/Advisor would otherwise incur in order to receive the same benefits.

The Treasury Department and the IRS currently agree that the relief of the Donor/Advisor's obligation to pay the full price of a ticket to a charity-sponsored event can be considered a direct benefit to the Donor/Advisor that is more than incidental. Therefore, proposed regulations under § 4967 would, if finalized, provide, that a distribution from a DAF pursuant to the advice of a Donor/Advisor that subsidizes the Donor/Advisor's attendance or participation in a charity-sponsored event confers on the Donor/Advisor a more than incidental benefit under § 4967. The Treasury Department and the IRS do not currently agree that, for purposes of § 4967, a distribution made by a sponsoring organization from a DAF to a charity upon advice of a Donor/Advisor should be analyzed the same as a hypothetical, direct contribution by the Donor/Advisor to the charity. A Donor/Advisor who wishes to receive goods or services (such as tickets to an event) offered by a charity in exchange for a contribution of a specified amount can make the contribution directly, without the involvement of a DAF.

The Treasury Department and the IRS recognize that a similar issue arises if a sponsoring organization makes a distribution from a DAF to a charity to pay, on behalf of a Donor/Advisor, the deductible portion of a membership fee charged by the charity, and the Donor/Advisor separately pays the nondeductible portion of the membership fee. Therefore, The Treasury Department and the IRS anticipate that the same analysis would apply to a case where the Donor/Advisor receives these types of membership benefits, so that the sponsoring organization cannot pay the deductible portion of the membership fee without conferring more than an incidental benefit on the

Donor/Advisor.

The Treasury Department and the IRS recognize that a distribution that results in a more than incidental benefit under § 4967 may also result in an excess benefit under § 4958. The Treasury Department and the IRS anticipate that any proposed regulations would address the application of excise taxes in the case of a distribution that is potentially subject to tax under both §§ 4958 and 4967. See § 4967(b).

SECTION 4. CERTAIN DISTRIBUTIONS FROM A DAF PERMITTED WITHOUT REGARD TO A CHARITABLE PLEDGE MADE BY A DONOR, DONOR ADVISOR, OR RELATED PERSON

Commenters have expressed uncertainty about whether a Donor/Advisor may advise a distribution from a DAF to satisfy a Donor/Advisor's pledge to make a contribution to a charity. Commenters noted that under § 4941, a private foundation's grant or other payment in fulfillment of the legal obligation of a disqualified person ordinarily constitutes a prohibited act of self-dealing. See § 53.4941(d)-2(f)(1) of the Excise Tax Regulations.

Most commenters favored allowing distributions from DAFs to fulfill a Donor/Advisor's charitable pledge. A few commenters expressed concern that requiring a sponsoring organization to determine, before making a DAF distribution, whether a Donor/Advisor made a legally binding pledge may unduly complicate charitable giving. In particular, these commenters noted the difficulty inherent in determining whether a commitment identified as a "pledge" is legally enforceable under state law or merely an indication of charitable intent. One commenter stated that whether a given pledge is legally enforceable under state law often turns on factual details that can be difficult for the sponsoring organization to ascertain. A few commenters noted that determining whether a pledge is legally enforceable is impractical and also places an undue

administrative burden on the IRS. These commenters also suggested that distributions from DAFs to charitable organizations should be encouraged and that allowing satisfaction of Donor/Advisors' charitable pledges facilitates the giving process.

The Treasury Department and the IRS currently agree with those commenters who suggested that it is difficult for sponsoring organizations to differentiate between a legally enforceable pledge by an individual to a third-party charity and a mere expression of charitable intent. The Treasury Department and the IRS are of the view that, in the context of DAFs, the determination of whether an individual's charitable pledge is legally binding is best left to the distributee charity, which has knowledge of the facts surrounding the pledge. Accordingly, to facilitate distributions from DAFs to charities, the Treasury Department and the IRS are considering proposed regulations under § 4967 that would, if finalized, provide that distributions from a DAF to a charity will not be considered to result in a more than incidental benefit to a Donor/Advisor under § 4967 merely because the Donor/Advisor has made a charitable pledge to the same charity (regardless of whether the charity treats the distribution as satisfying the pledge), provided that the sponsoring organization makes no reference to the existence of any individual's pledge when making the DAF distribution. Specifically, it is anticipated that under this approach a distribution from a DAF to a charity to which a Donor/Advisor has made a charitable pledge (whether or not enforceable under local law) will not be considered to result in a more than incidental benefit to the Donor/Advisor if the following requirements are satisfied:

- (1) the sponsoring organization makes no reference to the existence of a charitable pledge when making the DAF distribution;

- (2) no Donor/Advisor receives, directly or indirectly, any other benefit that is more than incidental (as discussed in this notice and as further defined in future proposed regulations) on account of the DAF distribution; and
- (3) a Donor/Advisor does not attempt to claim a charitable contribution deduction under § 170(a) with respect to the DAF distribution, even if the distributee charity erroneously sends the Donor/Advisor a written acknowledgment in accordance with § 170(f)(8) with respect to the DAF distribution.

Because the relationship between a private foundation and its disqualified persons typically is much closer than the relationship between a DAF sponsoring organization and its Donor/Advisors, this special rule regarding certain charitable pledges would apply for purposes of § 4967 only. The principles discussed in this section 4 would not be intended to affect the tax treatment of any item under any provision of the Code other than § 4967.¹

For example, assume that charity Z, an organization described in §§ 501(c)(3) and 170(b)(1)(A)(vi), holds an annual fundraising drive, and in response to the annual fundraising solicitation, individual B promises to contribute \$1,000x to Z. B has advisory privileges with respect to a DAF and advises that the sponsoring organization distribute \$1,000x from the DAF to Z. The sponsoring organization makes the advised distribution. Assume further that in its transmittal letter to Z, the sponsoring organization identifies B as the individual who advised the distribution, but makes no reference to a

¹ See, e.g., Revenue Ruling 81-110, 1981-CB 479 (January 1, 1981) (a payment by a third party to a charitable organization that explicitly is made to pay the legally enforceable pledge of a donor is treated as a gift from the third party to the donor and then a charitable contribution from the donor to the organization); Treas. Reg. § 53.4941(d)-2(f)(1).

charitable pledge by B or any other person. Z chooses to treat the sponsoring organization's distribution as satisfying B's pledge. Z also publicly recognizes B for B's role in facilitating the distribution from the sponsoring organization, but Z provides no other benefit to B. B does not attempt to claim a § 170 deduction with respect to the distribution. Under these facts, the Treasury Department and the IRS are currently of the view that the DAF distribution does not result in a more than incidental benefit to B under § 4967 merely because Z treats the distribution as satisfying B's pledge.

SECTION 5. PREVENTING ATTEMPTS TO USE A DAF TO AVOID "PUBLIC SUPPORT" LIMITATIONS

Publicly supported organizations under § 170(b)(1)(A)(vi) normally receive a substantial part of their support from governmental units and from direct or indirect contributions from the public. In determining whether an organization qualifies as "publicly supported" during any period, the organization generally may treat contributions (including grants) from a person as support from the general public (public support) only to the extent that such person's total contributions to the organization during the period do not exceed 2 percent of the organization's total support during the period (the 2-percent public support limitation). For this purpose, all contributions made by an individual, trust, or corporation and by any person or persons standing in a relationship to the individual, trust, or corporation that is described in § 4946(a)(1)(C) through (G) and the related regulations are treated as made by one person. See § 1.170A-9(f)(6)(i) of the Income Tax Regulations. The 2-percent public support limitation does not apply to contributions received by a donee organization from a § 170(b)(1)(A)(vi) organization, except to the extent that the contributions represent amounts earmarked by a donor to the § 170(b)(1)(A)(vi) organization as being for, or for

the benefit of, the donee organization. See § 1.170A-9(f)(6)(v).

Similarly, publicly supported organizations under § 509(a)(2) cannot treat contributions from a substantial contributor as public support, but contributions from an organization described in § 170(b)(1)(A) (other than clauses (vii) and (viii)) count as public support except to the extent that the contributions received by a donee organization represent amounts earmarked by a donor to the § 170(b)(1)(A) organization as being for, or for the benefit of, a particular recipient. See § 1.509(a)-3(j).

Because of the contributions they receive from the general public, DAF sponsoring organizations typically qualify as § 170(b)(1)(A)(vi) organizations whose distributions from DAFs would ordinarily be counted as public support without limitation to the distributee charity. The Treasury Department and the IRS are aware that some donors and distributee charities seek to use DAF sponsoring organizations as intermediaries. Rather than making contributions, which would be subject to the 2-percent public support limitation, directly to charities, these donors make contributions to DAFs maintained by sponsoring organizations and then advise the sponsoring organizations to make distributions from the DAFs to the distributee charities. In light of the potential for abuse, the Treasury Department and the IRS are considering treating, solely for purposes of determining whether the distributee charity qualifies as publicly supported, a distribution from a DAF as an indirect contribution from the donor (or donors) that funded the DAF rather than as a contribution from the sponsoring organization. Such treatment would better reflect the degree to which the distributee charity receives broad support from a representative number of persons.

Public support is defined in the regulations under §§ 1.170A-9(f) and 1.509(a)-3.

The Treasury Department and the IRS are considering proposing changes to these regulations to prevent the use of DAFs to circumvent the private foundation rules and excise taxes imposed by the Code by advising distributions from a DAF to a charity. It is currently anticipated that any proposed changes to these regulations would provide that a donee organization, for purposes of determining its amount of public support, must treat:

- (1) a sponsoring organization's distribution from a DAF as coming from the donor (or donors) that funded the DAF rather than from the sponsoring organization;
- (2) all anonymous contributions received (including a DAF distribution for which the sponsoring organization fails to identify the donor that funded the DAF) as being made by one person; and
- (3) distributions from a sponsoring organization as public support without limitation only if the sponsoring organization specifies that the distribution is not from a DAF or states that no donor or donor advisor advised the distribution.

The Treasury Department and the IRS recognize that a donee organization may need to obtain additional information from the sponsoring organization in order to determine its amount of public support. However, the Treasury Department and the IRS note that this additional information would only be needed if the donee organization intends to treat a distribution from a sponsoring organization as public support.

SECTION 6. REQUEST FOR PUBLIC COMMENTS

The Treasury Department and the IRS request comments regarding the issues addressed in this notice and suggestions for future guidance with respect to DAFs. In addition, the Treasury Department and the IRS request comments with respect to the following:

- (1) How private foundations use DAFs in support of their purposes.
- (2) Whether, consistent with § 4942 and its purposes, a transfer of funds by a private foundation to a DAF should be treated as a “qualifying distribution” only if the DAF sponsoring organization agrees to distribute the funds for § 170(c)(2)(B) purposes (or to transfer the funds to its general fund) within a certain timeframe.
- (3) Any additional considerations relating to DAFs with multiple unrelated donors under the proposed changes described in section 5 of this notice.
- (4) Methods to streamline any required recordkeeping under the proposed changes described in section 5 of this notice.

Written comments may be submitted by March 5, 2018 to Internal Revenue Service, CC:PA:LPD:PR (Notice 2017-73), Room 5203, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044, or electronically to Notice.Comments@irs.counsel.treas.gov (please include “Notice 2017-73” in the subject line). Alternatively, comments may be hand delivered between the hours of 8:00 a.m. and 4:00 p.m. Monday to Friday to CC:PA:LPD:PR (Notice 2017-73), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue NW, Washington, D.C. Comments will be available for public inspection and copying.

SECTION 7. RELIANCE ON NOTICE

Taxpayers may rely on the rules described in section 4 until additional guidance is issued.

SECTION 8. DRAFTING INFORMATION

The principal authors of this notice are Amber L. MacKenzie and Ward L. Thomas of the Office of Associate Chief Counsel (TEGE). For further information

regarding this notice, contact Ms. MacKenzie at (202) 317-5800 or Mr. Thomas at (202) 317-6173 (not a toll-free call).