



February 14, 2024

Internal Revenue Service
CC:PA:01:PR (REG-142338-07)
Room 5203
P.O. Box 7604
Ben Franklin Station
Washington, DC 20044

RE: Taxes on Taxable Distributions from Donor Advised Funds under Section 4966 Proposed Rule, REG-142338-07

The North Carolina Center for Nonprofits (the Center) welcomes this opportunity to submit formal comments on the proposed regulations providing guidance on Sections 4966 and 4967 of the Internal Revenue Code, which govern donor advised funds (DAFs). The Center is a 501(c)(3) nonprofit that connects, educates, and advocates for charitable nonprofits throughout North Carolina. Many of the Center's 1,110+ member nonprofit organizations receive grants through DAFs, and some serve as sponsoring organizations of DAFs. In addition, several of the Center's members have funds that are not currently treated as DAFs but which may meet the definitions of DAFs set forth in the proposed regulations.

The Center fully supports the [formal comments on the Proposed Rule](#) submitted by the National Council of Nonprofits (NCN) on February 12, 2024. Rather than restating the excellent analysis in the NCN comments, the Center is highlighting a few of NCN's observations and recommendations that have resonated with the Center's members that receive grants from and/or sponsor DAFs or other similar types of funds and noting two additional observations on the proposed regulations. The Center shares NCN's appreciation of Treasury and the IRS for providing clarifying guidance on the definitions of DAF, donor, and donor-advisor, on exceptions to the definition of a DAF, and on taxable distributions from a DAF. The Center shares NCN's concern that some of the provisions in the proposed regulations "may inadvertently increase the compliance burden on DAF sponsors and DAF donors, and therefore may result in unnecessary burdens on the flow of philanthropic dollars to the work of charitable nonprofits."

Proposed Definition of a DAF and a Donor

Like NCN, the Center agrees with the proposed regulations that most public charities (with the exception of disqualified supporting organizations) should be excluded from the definition of "donor" and that private foundations should be included in the definition of "donor" in Proposed Regulation Section 53.4966-1(f). Presuming that the final regulations include private foundation within the definition of "donor," the Center agrees with NCN that it is essential to provide clarity on whether

contributions from a private foundation to a DAF should be considered qualified distributions under IRC Section 4942(g).

Proposed Definition of Donor-Advisor

In its comments, NCN refers to the provision in the proposed regulations establishing an exception to the donor-advisor classification for a personal investment advisor who provides advice to the sponsoring organization as a whole and who charges a uniform fee to all DAFs of the sponsoring organization as “a trap for the unwary.” The Center agrees with NCN’s description of this provision. The Center has heard that many sponsoring organizations do not impose uniform fees on all DAFs under their control. Consequently, under the definition of donor-advisor in the proposed regulations, some DAFs might be subject to taxes under IRC Section 4958, IRC Section 4966, and/or IRC Section 4967 for any compensation or other payments they make to investment advisors at sponsoring organizations. Ultimately, these taxes would result in fewer funds being distributed from DAFs to charitable nonprofits for their mission-related programs and services. The Center concurs with NCN’s recommendation that the final regulations should provide greater flexibility in the application of charged fees in the exception to the “donor-advisor” definition for personal investment advisors. The Center also encourages the IRS and Treasury Department to take feedback from community foundations and other DAF sponsors on the provisions on personal investment advisors into consideration when developing final regulations.

Taxable Distributions for Legal Advocacy Activities of Charitable Nonprofits

Certain types of nonpartisan advocacy activities – including influencing legislation and nonpartisan voter registration, voter education, and get-out-the-vote activities – are legal for charitable nonprofits and are an important part of the missions activities of many 501(c)(3) public charities. In its public comments, NCN correctly notes that the preamble language in the proposed regulations do not clearly explain the distinction between impermissible partisan electioneering activities and permissible nonpartisan advocacy activities of charitable nonprofits. The Center shares NCN’s concern that the language in the preamble of the proposed regulations could “have a chilling effect on potential grants from DAFs to public charities engaged in perfectly legal nonprofit advocacy as well as nonpartisan, election-related activities.” The Center agrees with NCN that it is imperative that the final regulations “must correct and clarify the harmful language in the preamble to protect rather than stifle these vital charitable roles and activities that communities need to be healthy and strong.”

Exception to the Definition of DAFs – Fiscal Sponsors

The Center agrees with NCN’s observation that “the proposed regulations could contain a trap for the unwary, especially in the context of so-called ‘fiscal sponsorship arrangements.’” The Center is aware of several charitable projects and activities in North Carolina that are carried out through fiscal sponsorship arrangements. Typically, programs that are fiscally sponsored by a charitable nonprofit are separately identified by one or more donors, and these programs often have advisory bodies that provide recommendations to the fiscal sponsor’s governing board about the fiscally-sponsored program. Under the proposed regulations, it appears that many fiscal sponsorship arrangements that do not meet the “single identified charitable purpose” exception would be treated as DAFs if one of their donors was part of the advisory body. The applicability of DAF rules to fiscal sponsorships would create significant challenges for charitable programs that are operating under this relatively common structure. The

Center encourages the IRS and Treasury Department to expressly exempt fiscal sponsorship arrangements from the definition of DAFs in the final regulations.

Exception to the Definition of DAFs – Other Types of Funds

As with fiscal sponsorships, it is possible that other types of funds, including giving circles, could meet the definition of a DAF under the proposed rules. The applicability of DAF rules to giving circles and other types of funding arrangements could create unintended consequences that could reduce the flow of dollars from these types of funds to support the work of charitable nonprofits serving communities. The Center encourages the IRS and Treasury Department to address more clearly and directly the applicability of the definitions of a DAF – and the exceptions to the definition – to giving circles and other types of funding arrangements in the final regulations.

Implementation of Final Regulations

When the IRS and Treasury Department issue final regulations on DAFs, it is likely that many DAFs and sponsoring organizations – and potentially other types of funds like fiscal sponsorships and giving circles – will need to make changes to their structures to comply with the new definitions and rules. This will be true regardless of whether the final regulations are identical to the proposed regulations or whether they incorporate suggestions from the Center, NCN, and other individuals and organizations submitting public comments. If DAF donors, DAF sponsors, fiscally-sponsored programs, giving circles, and other affected funds do not have adequate time to make the necessary changes after final regulations are issued, the result could be fewer dollars being distributed from DAFs to support the work of charitable nonprofits. Consequently, the Center recommends that the final regulations follow the recommendations from DAF sponsors, DAF donors, fiscally-sponsored programs, giving circles, and other affected funds on the appropriate timing for implementation of the rules.

Thank you for the opportunity to submit these comments on behalf of North Carolina's nonprofit sector.

Respectfully submitted,

A handwritten signature in black ink that reads "David R. Heinen". The signature is written in a cursive, slightly slanted style.

David R. Heinen
Vice President for Public Policy and Advocacy
North Carolina Center *for* Nonprofits