Philanthropy Roundtable

UNDERSTANDING THE ACE ACT, A BILL TO RESTRICT CHARITABLE GIVING, S. 1981/H.R. 6595

BY: ELIZABETH MCGUIGAN, DIRECTOR OF POLICY

KEY CONCERNS WITH S. 1981/H.R. 6595:

- The bill creates more rules and mandates for donor-advised funds and private foundations that would restrict dollars from flowing to charities and the communities they support.
- The bill would add new definitions and complexity to the tax code, which could chill charitable giving overall.
- By imposing ineffective and counterproductive limits and requirements on private foundations, the bill would hamper them from achieving their charitable missions and threaten donor privacy.
- The bill makes it more difficult for charitable organizations to meet the IRS' public support test and retain their status as a public charity by changing the treatment of some donations.
- Unlike other proposals, this bill excludes a key incentive for charitable giving—an expansion of the charitable tax deduction.

INTRODUCTION

Senators Angus King (I-ME) and Charles Grassley (R-IA) have introduced a bill that would suppress charitable giving. The title of the bill, the Accelerating Charitable Efforts (ACE) Act, S. 1981, suggests the legislation will increase resources for charities. However, the provisions within the bill would do the opposite—harming the exact charitable organizations and communities they seek to help. In the House, a companion bill, H.R. 6595, was introduced by Rep. Chellie Pingree (D-ME) and Rep. Tom Reed (R-NY) in February 2022.

The bill targets private foundations and donor-advised funds, or DAFs. These are charitable giving accounts maintained by individual donor advisors and oftentimes hosted by national sponsoring charities or community foundations. Every dollar that goes into a DAF is immediately and permanently committed to charitable giving.

S. 1981/H.R. 6595 CREATES NEW DEFINITIONS, ADDS COMPLEXITY TO THE TAX CODE AND CHILLS GIVING

THE BILL WOULD UNNECESSARILY DIVIDE DAFS INTO TWO CATEGORIES: QUALIFIED AND NONQUALIFIED

S. 1981/H.R. 6595 divides charitable giving vehicles and organizations into complex buckets. By doing so, it injects additional complexity into the tax code and discourages people from contributing to DAFs in the first place.

QUALIFIED DAF

Offers the donor an immediate charitable tax deduction in the years gifts are made and extends advisory privileges for only 15 years, during which time all contributions must be distributed or the sponsoring organization faces a 50% tax penalty on the DAF assets.

NONQUALIFIED DAF

Offers the donor a charitable tax deduction only in the years gifts are distributed out of a DAF and extends advisory privileges up to 50 years before facing the 50% tax penalty. The donor may only deduct the amount of the qualifying distribution, and distributions are treated as made from contributions on a first-in, first-out basis.

THE BILL WOULD CREATE A SPECIAL DEFINITION FOR A NARROW SET OF "QUALIFIED" COMMUNITY FOUNDATIONS AND THEIR DAFS

QUALIFIED COMMUNITY FOUNDATION

Must serve a community no larger than four states and hold at least 25% of their assets outside of DAFs.

QUALIFIED COMMUNITY FOUNDATION DAF

Is exempt from the 50% penalty if the DAF is sponsored at a qualified community foundation and either:

- Has no individual donor advisor with an aggregate value of $1 million in DAF accounts with the foundation; or
- Must pay out at least 5% of the DAF's value annually.

IMPACT

- Such complexity will lead directly to increased administrative burdens and compliance costs for the charitable sector and givers—resulting in less funds for charities and the communities they support.
- It is also important to note that the tax penalty would be born by the sponsoring organization, a public charity, not by the donor. Taxing charitable assets runs counter to the purported goal of the bill as it would necessarily mean fewer dollars for charities.
- The bill would also limit the important ability for donors to allow their funds to grow over time and save up to make a larger charitable gift. Removing the timing flexibility that makes DAFs so popular would also come at a detriment to charities, especially for those with long-term goals or future projects in need of support.

THE BILL WOULD CREATE COMPLEX TAX DEDUCTION RULES FOR GIFTS TO DAFS

The bill would arbitrarily limit a donor's ability to give complex assets through DAFs.

- Contributions of non-cash assets and non-publicly traded assets (those without a price available on an established securities market) cannot be deducted until the asset is sold by the sponsoring organization.
- When these assets are sold, the deduction cannot exceed the gross proceeds received from the sale and credited to the donor's account.
- The sponsoring organization must report the sale in a written acknowledgment to the donor within 30 days of crediting the proceeds to the DAF. This acknowledgment must include the donor's name, certify the asset was sold, and include the gross proceeds as well as a statement that the deduction cannot exceed the proceeds credited to the donor's DAF. The acknowledgment must also be submitted to the IRS.

IMPACT

- There are ample real-world examples of donors giving non-cash assets, such as commercial real estate and operating businesses, to a DAF sponsor to provide ongoing charitable funding over an extended period of time.
- The Communities Foundation of Texas, for example, outlines on its website several cases in which their donors were able to support their communities through the donation of such assets. In one such case, a donor with property in Dallas was able to contribute a percentage of a business into a DAF, where it is able to produce income that can be used for grantmaking to nonprofits. Forcing a sale of such an asset at the time of donation is likely to yield less money for charities overall.
- The bill also disallows anonymous contributions of non-cash assets by requiring a formal acknowledgment that includes the name of the donor. Beyond the significant donor privacy concerns, the acknowledgment itself would impose new compliance costs onto DAF sponsors—themselves public charities.

S. 1981/H.R. 6595 IMPOSES INEFFECTIVE AND COUNTERPRODUCTIVE LIMITS ON PRIVATE FOUNDATIONS

THE BILL WOULD PROHIBIT PRIVATE FOUNDATIONS FROM COUNTING DAF GIFTS TOWARD THEIR REQUIRED 5% PAYOUT RATE, WITHOUT JUSTIFICATION

Under current law, private foundations may include contributions to a DAF toward their annual qualifying distributions.

- The bill would generally exclude DAF gifts from the definition of qualifying distributions, unless the DAF gift is distributed to a charity by the end of the following year of the gift.
- Any private foundation that contributes to a DAF would be subjected to new reporting requirements, including:
  - The amount of DAF contributions in a given year;
  - The name of the DAF sponsoring organization; and
  - Any donation advice given to the DAF sponsoring organization.

IMPACT

There are many valid and useful ways that private foundations use DAFs to further their charitable missions, including: to protect donor information when granting to a controversial cause; to issue a one-time, off-mission grant, such as COVID relief, without opening the door for further solicitations; and to pool resources with other givers, without burdening the receiving charity with extra administrative work.

The bill also imposes new reporting requirements on private foundations giving to DAFs that would undermine some of the legitimate reasons that foundations may use DAFs as a private giving vehicle. In our current divisive culture, donor privacy is crucial. Forced disclosure of some donations may threaten the safety and well-being of donors as well as chill charitable giving overall.

THE BILL WOULD ARBITRARILY PROHIBIT FAMILY FOUNDATIONS FROM INCLUDING SALARIES AND EXPENSES OF WORKING FAMILY MEMBERS AS ADMINISTRATIVE EXPENSES THAT COUNT TOWARD PAYOUT

Current law requires private foundations to distribute at least 5% of assets each year. Foundations are allowed to count certain administrative expenses associated with their grantmaking, such as the salaries and work-travel expenses of employees, as part of the required payout.

- The bill would exclude any administrative expenses (e.g. salary and travel expenses) that are paid to certain "disqualified persons" for purposes of payout. Under this provision, the definition of "disqualified persons" would:
  - ◇ Exclude foundation managers (officers, directors or trustees, so long as they are not related), meaning that their expenses would continue to count toward payout; and
  - ◇ Include substantial contributors to the foundation, along with family members (spouses, ancestors, children, grandchildren, great-grandchildren and their spouses), meaning that their expenses would no longer count toward payout.

IMPACT

- There is no evidence to support the discrimination against working family members at foundations. Data show family foundations are not more likely to claim higher administrative expenses than staff-run foundations.
- This bill will handcuff family foundations and hamper the work they do to effectively and efficiently achieve their charitable missions.

S. 1981/ H.R. 6595 MAKES IT MORE DIFFICULT FOR PUBLIC CHARITIES TO MEET THE PUBLIC SUPPORT TEST

THE BILL WOULD TREAT ALL ANONYMOUS DAF CONTRIBUTIONS RECEIVED FROM SPONSORING ORGANIZATIONS AS COMING FROM ONE PERSON—WHETHER THAT IS THE CASE OR NOT

Under current law, public charities must demonstrate broad support from the public to obtain and retain public charity status.

- This bill would prohibit public charities from using DAF contributions to meet the public support test, unless:
  - The DAF sponsoring organization identifies the donor by name, in which case the contribution is treated as coming from that donor; or
  - The DAF sponsoring organization specifies that no individual had advisory privileges over a contribution.

IMPACT

- When it comes to public charities, which must demonstrate broad support, DAF contributions are critical. There are many reasons that donors may want to remain anonymous, including for religious or modesty reasons.
- This bill ignores the fact that sponsoring organizations are themselves IRS-designated public charities and would also make it difficult for recipient charities to prove broad support with multiple, independent, anonymous DAF donations.

S. 1981/H.R. 6595 PROVIDES A SMALL "CARROT" FOR PRIVATE FOUNDATIONS

THE BILL WOULD EXEMPT A PRIVATE FOUNDATION FROM THE EXCISE TAX ON INVESTMENT INCOME IN A TAXABLE YEAR UNDER TWO SCENARIOS

S. 1981/H.R. 6595 does provide a small "carrot" for private foundations by creating an exemption for private foundations from the excise tax on investment income in a taxable year.

- If the foundation distributes at least 7% of its assets; or
- If the foundation is created for a term of no longer than 25 years and the foundation does not distribute funds to another disqualified (related) foundation.

IMPACT

- While this exemption is a positive for private foundations that choose to distribute funds faster than required, the punitive provisions through the legislation far outweigh the benefit of this one component.

S. 1981/H.R. 6595 EXCLUDES KEY INCENTIVE FOR CHARITABLE GIVING: AN EXPANSION OF THE CHARITABLE TAX DEDUCTION

The bill aligns with a proposal promoted by the so-called Initiative to Accelerate Charitable Giving with one key difference. The backers of the initiative also called for an expansion and extension of the above-the-line charitable deduction for non-itemizers created by the CARES Act. The bill inexplicably does not include this additional "carrot" that would encourage an increase in charitable giving without the damaging consequences of the other provisions.

ABOUT THE AUTHOR

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