

Memorandum

Final Regulations Relating to Foreign Grantmaking Activities by Private Foundations and Sponsoring Organizations of Donor-Advised Funds

September 30, 2015

Introduction

On September 25, 2015, the Department of the Treasury (“Treasury”) issued final regulations (the “Final Regulations”) relating to equivalency determinations by private foundations and sponsoring organizations of donor-advised funds. The Final Regulations amend and finalize proposed regulations that were issued on September 24, 2012 (the “Proposed Regulations”).

The Final Regulations

Equivalency determinations are one of the two longstanding methods used by private foundations to make grants to organizations outside of the United States.¹ A private foundation that makes an equivalency determination in connection with a grant to a foreign organization will avoid the excise tax on taxable expenditures with respect to the grant and may count the grant as a qualifying distribution. Prior to the publication of the Proposed Regulations, existing law permitted private foundations to make an equivalency determination by making a “good faith determination,” based on an affidavit of a foreign organization (a “grantee affidavit”) or an opinion of counsel, that a foreign organization was an eligible public charity (a “U.S. public charity”) described in section 509(a)(1), (2) or (3) of the Internal Revenue Code of 1986, as amended (the “Code”), so long as the grantee affidavit or opinion of counsel set forth sufficient facts concerning the operations and support of the foreign organization for the Internal Revenue Service (the “IRS”) to determine that the foreign organization would be likely to qualify as a U.S. public charity. The Proposed Regulations expanded the scope of the existing law to permit private foundations to make a good faith determination

¹ Private foundations that do not make an equivalency determination in connection with a grant to a foreign organization must perform expenditure responsibility with respect to the grant. The expenditure responsibility process is not affected by the Final Regulations.

based on the written advice of a qualified tax practitioner, as opposed to an opinion of counsel.² The Final Regulations adopt certain provisions included in the Proposed Regulations, but also include several important changes to the Proposed Regulations.

Highlights of the Final Regulations include:

- (i) Adoption of the Proposed Regulations' expansion of the class of tax practitioners upon whose written advice private foundations may rely when making a good faith determination that a foreign organization is the equivalent of a U.S. public charity;
- (ii) A change to the Proposed Regulations (and to prior law) such that a good faith determination made by a private foundation on the basis of a grantee affidavit only (i.e., not based upon the written advice of a qualified tax practitioner) no longer will fall under the "special rule" (discussed in more detail below) set forth in the Final Regulations;
- (iii) Confirmation that written advice demonstrating that a foreign organization is the equivalent of a publicly supported U.S. public charity will be considered "current," with respect to the public support determination, for the two taxable years of the foreign organization immediately following the end of the five-year test period described in the written advice (e.g., taxable years 2015 and 2016, where a foreign organization provides financial information for the taxable years 2010 through 2014);
- (iv) Confirmation that a private foundation relying on written advice shared by another private foundation (i.e., as opposed written advice provided directly by a qualified tax practitioner) will not fall under the special rule set forth in the Final Regulations; and
- (v) Confirmation that sponsoring organizations of donor-advised funds may rely on the Final Regulations when making equivalency determinations.

Use of Grantee Affidavits

Given that a good faith determination on the basis of a grantee affidavit only is excluded from the special rule set forth in the Final Regulations, private foundation and sponsoring organization grantors should review their internal procedures with respect to equivalency determinations.

The Final Regulations provide that a determination by a private foundation that a foreign organization is the equivalent of a U.S. public charity "ordinarily will be considered a good faith determination if the determination is based on current written advice received from a qualified tax practitioner" concluding that a

² Private foundations were permitted to rely on the Proposed Regulations for grants made on or after September 24, 2012.

foreign organization is the equivalent of a U.S. public charity. This special rule provides private foundation and sponsoring organization grantors with certainty that the IRS views reliance on the written advice of a qualified tax practitioner as an acceptable method of making an equivalency determination. Under the Proposed Regulations (and under prior law), determinations based on a grantee affidavit provided by a foreign organization were explicitly included in the special rule, such that private foundation and sponsoring organization grantors had certainty that reliance on a grantee affidavit also was an acceptable method of making an equivalency determination. Because the Final Regulations do not reference grantee affidavits, private foundation and sponsoring organization grantors no longer can rely on a grantee affidavit and be afforded the benefit of the special rule.

That said, the Final Regulations do not necessarily foreclose reliance on a grantee affidavit when making an equivalency determination. The preamble to the Final Regulations notes that a foundation manager with an understanding of United States charity tax law may rely on a grantee affidavit and make an equivalency determination under the “general rule” (i.e., that, as a general matter, if a foundation manager makes a good faith determination that a foreign organization is the equivalent of a U.S. public charity, a grant to the foreign organization will not be a taxable expenditure and will be a qualifying distribution). However, that private foundation would not have the assurance provided by the special rule that the determination made by the foundation manager based on the grantee affidavit is one that the IRS “ordinarily” would consider a good faith determination.

Rev. Proc. 92-94

The preamble to the Final Regulations also confirms that, in light of comments received from the public regarding the need for revisions and amplifications to Revenue Procedure 92-94, 1992-2 CB 507 (“Rev. Proc. 92-94”), which provides a simplified procedure that private foundations may follow when making equivalency determinations, the IRS intends to publish an updated revenue procedure. The preamble indicates that the updated revenue procedure will reflect both the changes implemented by the Final Regulations as well as changes to the public support tests for publicly supported organizations in light of recent changes to Code sections 170(b)(1)(A)(vi) and 509(a)(2). The preamble states that Treasury and the IRS also will consider additional issues regarding Rev. Proc. 92-94 raised by commenters in response to the Proposed Regulations. No timetable was provided for publication of the updated revenue procedure.

The Final Regulations are effective as of September 25, 2015 and apply to any grants paid after that date. However, private foundation and sponsoring organization grantors may continue to rely on prior law as to equivalency determinations made in reliance on grantee affidavits (i) with respect to grants paid on or before December 24, 2015, and (ii) with respect to grants distributed pursuant to written commitments made on or prior to September 25, 2015, pursuant to good faith determinations made on or before such date, so long as such grants are paid out within five years.

The Final Regulations can be found at

<https://www.federalregister.gov/articles/2015/09/25/2015-24346/reliance-standards-for-making-good-faith-determinations>

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