

## Note

### Show Me the Money: Addressing the Oversight Gap in Private Foundation Donations to Donor-Advised Funds

Kerry Gibbons\*

“Sunlight is said to be the best of disinfectants.”

— Louis D. Brandeis,

Other People’s Money and How the Bankers Use It<sup>1</sup>

#### INTRODUCTION

The landscape of American charitable giving is changing. For years, if asked to name the largest charity in the United States, most would likely point to a roster of familiar names—United Way, perhaps, or the Salvation Army.<sup>2</sup> It may come as a surprise that, as of 2015, the largest charity in the United States is Fidelity Charitable, the nonprofit arm of Fidelity Investments.<sup>3</sup> Even since 2015, though,

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\* Lead Articles Editor, *Minnesota Law Review*, Vol. 106; J.D. Candidate 2022, University of Minnesota Law School. I am very grateful to Professor Kristin Hickman and Claire Topp for their guidance and feedback; to the MLR Note and Comment Department for their thoughtful suggestions; and to Jon Pratt and Kari Aanestad at the Minnesota Council of Nonprofits, who sparked this research into donor-advised funds and who continue to advocate for equity and transparency each and every day. And finally, to Matt—I couldn’t do it without you. Copyright © 2022 by Kerry Gibbons.

1. LOUIS D. BRANDEIS, OTHER PEOPLE’S MONEY AND HOW THE BANKERS USE IT 92 (1914).

2. See, e.g., William P. Barrett, *America’s Top Charities*, FORBES (Dec. 11, 2020) [hereinafter Barrett, *Top Charities*], <https://www.forbes.com/lists/top-charities> [<https://perma.cc/LL33-UA37>] (listing the top charities by private donations received in 2020). *Forbes’s* methodology purposefully focused on organizations that solicit the public for donations (not just organizations receiving charitable giving); several categories of charities, including academic institutions and donor-advised funds, were excluded from this list. See William P. Barrett, *How Forbes Picked America’s Top Charities for 2019—And What to Look for in Yours*, FORBES (Dec. 11, 2019), <https://www.forbes.com/sites/williambarrett/2019/12/11/how-forbes-picked-americas-top-charities-for-2019-and-what-to-look-for-in-yours> [<https://perma.cc/6AUK-RK3S>] (explaining the methodology behind their 2019 Top Charities list).

3. Roger Colinvaux, *Donor Advised Funds: Charitable Spending Vehicles for 21st*

Fidelity Charitable's growth has skyrocketed.<sup>4</sup> In 2019, Fidelity Charitable collected \$10.7 billion in donations—over \$7 billion more than United Way,<sup>5</sup> which for several decades had been considered the largest charity in the United States.<sup>6</sup> What is truly remarkable is how quickly Fidelity Charitable gained this status. United Way was founded in 1887 and built its charitable reputation over a century;<sup>7</sup> Fidelity Charitable accomplished the same in less than three decades.<sup>8</sup>

Fidelity Charitable is just one example of a donor-advised fund, or “DAF.”<sup>9</sup> To the consumer, DAFs function like a philanthropic intermediary.<sup>10</sup> A donor opens up an account with a DAF sponsor (such as a national sponsoring organization or a community foundation)<sup>11</sup> and makes an irrevocable contribution.<sup>12</sup> Upon contribution, the DAF sponsor legally owns the donation, and the

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*Century Philanthropy*, 92 WASH. L. REV. 39, 40 (2017) (explaining that Fidelity Charitable overtook United Way as the largest charity in the United States in 2015).

4. *Id.*

5. *Compare 2020 Annual Report*, FID. CHARITABLE 14 (2021), <https://www.fidelitycharitable.org/content/dam/fc-public/docs/annual-reports/2020-annual-report.pdf> [<https://perma.cc/2GN2-THRV>] (reporting that Fidelity Charitable received \$10,716,447,620 in donor contributions in 2020), with Barrett, *Top Charities*, *supra* note 2 (reporting that United Way received \$3.6 billion in donor contributions in 2020).

6. David Crary, *United Way Loses Its Ranking as America's Largest Charity*, AP NEWS (Oct. 27, 2016), <https://apnews.com/article/42c5ca1acd0b48af8611413be4f6fd0a> (last visited Nov. 20, 2021).

7. *Our History*, UNITED WAY, <https://www.unitedway.org/about/history> [<https://perma.cc/RH5G-EQB2>].

8. *About Fidelity Charitable*, FID. CHARITABLE, <https://www.fidelitycharitable.org/about-us.html> [<https://perma.cc/P24P-XAZT>] (noting that Fidelity Charitable was founded in 1991).

9. Other donor-advised funds operating on the same scale as Fidelity Charitable include Schwab Charitable, Vanguard Charitable, Goldman Sachs Philanthropy Fund, and the National Philanthropic Trust.

10. This characterization is true from the consumer's perspective—but from a tax law point of view, DAF sponsors legally own all contributions.

11. There are three main types of organizations that act as DAF sponsors: single-issue charities, community foundations, and national sponsoring organizations (such as Fidelity Charitable). Of these three, national sponsoring organizations manage, by far, the largest share of assets. See Chuck Collins, Helen Flannery & Josh Hoxie, *Warehousing Wealth: Donor-Advised Charity Funds Sequestering Billions in the Face of Growing Inequality*, INST. POL'Y STUDIES 13 fig.4 (July 2018), <https://ips-dc.org/wp-content/uploads/2018/07/Warehousing-Wealth-IPS-Report-1.pdf> [<https://perma.cc/5L79-2SAS>].

12. Once granted, an irrevocable contribution cannot be returned to the original donor. *What Is a Donor-Advised Fund?*, NAT'L PHILANTHROPIC TR., <https://www.nptrust.org/what-is-a-donor-advised-fund> [<https://perma.cc/84VB-3DWD>].

original donor receives an immediate tax benefit.<sup>13</sup> The DAF sponsor places the contribution into an investment account, where it can grow in size.<sup>14</sup> At any point in the future, the donor can “advise” that the funds be directed towards specific charities or charitable causes, at which point a grant is made by the DAF sponsor.<sup>15</sup> The original donation can live in perpetuity in the DAF; there is no time limit on when charitable grantmaking must be completed, and the original donor can designate successors to inherit advisory privileges.<sup>16</sup> DAFs are governed by few restrictions—namely, restrictions on which organizations can receive funds. Both the Treasury Department and Congress have proposed more restrictive regulations on DAF payout requirements, but neither Treasury nor Congressional proposals have passed.<sup>17</sup>

The philanthropy industry often compares DAFs to private foundations, their much more tightly regulated cousin.<sup>18</sup> Private foundations, unlike DAFs, are subject to two key Internal Revenue Service (“IRS”) regulations designed to promote transparency and prevent hoarding wealth: the annual disclosure of all charitable giving recipients<sup>19</sup> and the five percent annual payout requirement.<sup>20</sup> DAFs, on the other hand, are subject to few legal requirements.<sup>21</sup>

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13. *Id.*

14. *Id.*

15. *Id.* Many scholars argue that because the original donor maintains such strong advisory powers over these charitable funds after they legally pass into the DAF sponsor’s hands, the very foundation upon which the system rests—that the donor is eligible to receive a tax benefit because the DAF sponsor legally “owns” the donation—is a sham. *See, e.g.,* Edward Kleinbard, *The Law and Policy of Donor-Advised Funds*, TAXPROF BLOG (Aug. 10, 2018), [https://taxprof.typepad.com/taxprof\\_blog/2018/08/kleinbard-donor-advised-funds.html](https://taxprof.typepad.com/taxprof_blog/2018/08/kleinbard-donor-advised-funds.html) [<https://perma.cc/W7EK-8SHB>].

16. *What Is a Donor-Advised Fund?*, *supra* note 12.

17. Colinvaux, *supra* note 3, at 49–50; *see also General Explanations of the Administration’s Fiscal Year 2001 Revenue Proposals*, DEP’T TREASURY 105 (2000), <https://home.treasury.gov/system/files/131/General-Explanations-FY2001.pdf> [<https://perma.cc/A7C5-98X4>]; Tax Reform Act of 2014, H.R. 1, 113th Cong., 2d Sess. (2014) (introduced by Rep. Dave Camp).

18. *See, e.g., Giving Vehicle Comparison*, NAT’L PHILANTHROPIC TR., <https://www.nptrust.org/donor-advised-funds/daf-vs-foundation> [<https://perma.cc/5MSC-SES6>].

19. 26 C.F.R. § 1.6033-3.

20. I.R.C. § 4942; *see, e.g.,* Thomas A. Troyer, *The 1969 Private Foundation Law: Historical Perspective on Its Origins and Underpinnings*, 27 EXEMPT ORG. TAX REV. 52, 57 (2000).

21. *See* discussion *infra* Part I.B.

Interestingly, private foundations sometimes grant money to DAFs.<sup>22</sup> For example, between 2010 and 2018, private foundations granted over \$3 billion to DAFs.<sup>23</sup> Once the donation is made to a DAF, the transparency and payout requirements no longer apply. A donation to a DAF counts towards the IRS's five percent annual payout requirement—and the private foundation, normally subject to more stringent disclosure and time-sensitive payout rules, can direct its DAF dollars to charities anonymously and at its own leisure.

These private foundation-to-DAF donations are on the rise, increasing several-fold over the past decade.<sup>24</sup> In doing so, private foundations subvert the Tax Reform Act of 1969's goals: preventing wealth warehousing by requiring an annual minimum payout and requiring private and public oversight of private foundation grantmaking.<sup>25</sup> But this framework failed to foresee the rise of DAFs, which did not become commonplace until the mid-1990s.<sup>26</sup> The lack of regulatory oversight on such grantmaking results in billions of dollars escaping public and governmental scrutiny and delays billions of dollars in gifts to working charities.<sup>27</sup> Private foundations appear to increasingly take advantage of DAFs as tax loopholes to avoid the IRS's minimum payout requirements.

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22. Theodore Schleifer, *Google's Larry Page Gave \$400 Million in Christmas Donations. Not a Penny Went Straight to Charity*, VOX: RECODE (Dec. 18, 2019), <https://www.vox.com/recode/2019/12/18/21010108/larry-page-philanthropy-foundation-donor-advised-fund-christmas> (last visited Nov. 20, 2021) (detailing grantmaking from the Carl Victor Page Foundation to DAFs).

23. The Carl Victor Page Foundation is only one such example. Between 2010 and 2018, 2,203 private foundations granted \$3 billion to the five largest national sponsoring organizations (NSOs). See Kari Aanestad, Kerry Gibbons & Jon Pratt, *Private Foundation Grants to DAFs: Attorney General Charitable Trust Oversight Calls for Disclosure of Use of Funds*, MINN. COUNCIL NONPROFITS 4 (Mar. 17, 2021), <https://ssrn.com/abstract=3745330> [<https://perma.cc/8XZ9-YLDC>].

24. See discussion *infra* notes 143–144.

25. See discussion *infra* Parts I.A, I.B.

26. Colinvaux, *supra* note 3, at 47–48. While the major litigation around DAFs began in the 1990s with NSOs seeking 501(c)(3) status, DAFs have existed since 1931. They were pioneered by community foundations, like the New York Community Trust. Lila Corwin Berman, *Donor Advised Funds in Historical Perspective*, B.C. F. ON PHILANTHROPY & PUB. GOOD 23 (Oct. 23 2015), <https://lawdigitalcommons.bc.edu/cgi/viewcontent.cgi?article=1014&context=philanthropy-forum> [<https://perma.cc/B5L9-L76H>]. By the 1990s, most community foundations were already considered public charities by the IRS. George Johnson & David Jones, *Community Foundations*, in EXEMPT ORGANIZATIONS CONTINUING EDUCATION: TECHNICAL INSTRUCTIONS PROGRAM FOR FISCAL YEAR 1994, <https://www.irs.gov/pub/irs-tege/eotopick94.pdf> [<https://perma.cc/M6JJ-2C8C>].

27. See discussion *infra* Parts II.A, II.B.

The question of whether—and how—to reform DAFs has been the subject of much scholarly discussion over the past several years.<sup>28</sup> While several scholars have noted the problem posed by private foundation-to-DAF grantmaking,<sup>29</sup> this Note presents the first effort to analyze such grantmaking in detail and propose a solution to mitigate its harms.

Part I of this Note provides a history on the background and attempts to regulate both private foundations and DAFs. Part II explores the ways that private foundation grantmaking to DAFs frustrates the regulations put in place by the Tax Reform Act of 1969 and names the specific harms produced by such grantmaking—specifically, a substantial delay in gifts to working charities and a decline in philanthropic transparency. Finally, Part III of this Note proposes a two-pronged solution to prevent the wealth warehousing engendered through DAFs and promote transparency in grantmaking. This Note builds upon federal DAF reform arguments proposed by leading philanthropy scholars and applies specific, compromise-focused reform to the narrow foundation-to-DAF issue. It proposes a solution that recognizes the federalist scheme governing charities regulation and provides narrowly tailored guidance to address this specific type of DAF grantmaking. Specifically, this two-pronged solution includes both a federal component geared towards addressing the harm of wealth warehousing and delaying benefits to working charities and a state-level component that broadens oversight and transparency in private foundation-to-DAF grantmaking.

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28. See Colinvaux, *supra* note 3; Brian Galle, *Pay It Forward? Law and the Problem of Restricted-Spending Philanthropy*, 93 WASH. L. REV. 1143 (2016) (analyzing “restricted spending” charity); James A. Borrasso, Jr., Note, *Opening the Floodgates: Providing Liquidity to the Charitable Marketplace through Changes to Donor-Advised Funds*, 2018 U. ILL. L. REV. 1533 (advocating for the protection of donor-advised funds); Samuel D. Brunson, “I’d Gladly Pay You Tuesday for a [Tax Deduction] Today”: *Donor-Advised Funds and the Deferral of Charity*, 55 WAKE FOREST L. REV. 245 (2020) (proposing that donor-advised funds be “required to qualify as public charities individually”).

29. See Philip Hackney, *The 1969 Tax Reform Act and Charities: Fifty Years Later*, 17 PITT. TAX REV. 235, 241 (2020) (“It seems hard to argue with the claim that payouts to DAFs should not count [towards the five percent payout requirement].”); Ray D. Madoff, *The Five Percent Fig Leaf*, 17 PITT. TAX REV. 341, 342 (2020) (“In particular, the ability to meet payout requirements by ... making unlimited contributions to donor-advised funds ... give[s] private foundations ample opportunity to skirt the purpose, while still fulfilling the letter, of the law governing payout.”); Galle, *supra* note 28, at 1148 (“Congress also should close the loopholes presented by lightly regulated alternatives to the foundation form, especially those offered by the so-called donor-advised funds.”).

## I. DONOR-ADVISED FUNDS AND PRIVATE FOUNDATIONS: TWO SIDES OF THE SAME COIN

DAFs and private foundations coexist like a two-faced Janus.<sup>30</sup> Both charitable giving mechanisms are geared towards promoting philanthropy and providing resources to the organizations that need it most; however, the processes governing DAF and private foundation existence, operation, and donation differ greatly.<sup>31</sup> The time, expense, and regulatory oversight involved in setting up and operating private foundations almost certainly resulted in the popularity of DAFs, which promised to democratize philanthropy.<sup>32</sup> The skyrocketing popularity of DAFs, however, portends a decline in transparency and a rise in hoarding of charitable dollars—two outcomes that the Tax Reform Act of 1969 sought to prevent.<sup>33</sup> This Part introduces the history and evolution of both DAFs and private foundations. Section A outlines the evolution and legislative history of laws governing private foundations' conduct and charitable giving. Then, Section B discusses the emergence and popularity boom of DAFs and compares the limited landscape of DAF regulation to the more onerous requirements applicable to private foundations.

### A. PRIVATE FOUNDATIONS, WEALTH WAREHOUSING, AND THE ORIGINS OF THE TAX REFORM ACT OF 1969

The history of private foundations in the United States is intertwined with that of the great 19th-century industrialists.<sup>34</sup> Private foundations emerged as a tool, largely for a single individual or group, to direct personal wealth towards charitable causes.<sup>35</sup> These early foundations were often founded with certain “self-defined” goals: bettering the public good.<sup>36</sup> Despite the very

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30. The Roman god Janus is usually depicted with two faces—one looking to the future, the other towards the past. *Janus*, ENCYC. BRITANNICA, <https://www.britannica.com/topic/Janus-Roman-god> (last visited Nov. 20, 2021).

31. See discussion *infra* Parts I.A., I.B.

32. See discussion *infra* Parts I.A., I.B.

33. See discussion *infra* Part I.A.

34. See, e.g., Nina J. Crimm, *A Case Study of a Private Foundation's Governance and Self-Interested Fiduciaries Calls for Further Regulation*, 50 EMORY L.J. 1093, 1102–03 (2001) (discussing the role Andrew Carnegie played in developing the modern private foundation); see also Joel R. Gardner, *Oral History and Philanthropy: Private Foundations*, 79 J. AM. HIST. 601 (1992).

35. Paul Arnsberger, Melissa Ludlum, Margaret Riley & Mark Stanton, *A History of the Tax-Exempt Sector: An SOI Perspective*, STAT. INCOME BULL. 105, 105 (2008).

36. Crimm, *supra* note 34, at 1103 (“[T]he first modern foundation . . . [is] an open-ended endowment devoted to self-defined goals of reforming the public’s

substantial public benefits extended by these foundations, the magnitude of wealth held by the robber barons—and by extension, committed to their foundations—invited scrutiny.<sup>37</sup> President William Howard Taft’s Commission on Industrial Relations, convened to study “wealth and influence,”<sup>38</sup> sharply criticized private foundations for reinforcing plutocratic influence and creating a bottomless well of wealth.<sup>39</sup> Despite the Commission’s reproach towards private foundations, Congress passed no legislation circumscribing their size or influence.<sup>40</sup>

The growing popularity of private foundations throughout the middle of the 20th century prompted Congress to reconsider the topic of regulation. The number of private foundations doubled in size throughout the 1930s,<sup>41</sup> and after World War II, the number of foundations with assets over \$1 million doubled as well.<sup>42</sup> This uptick in the number and wealth of foundations can be partially attributed to two factors: post-World War II economic prosperity and an attractive tax structure.<sup>43</sup> Congress passed several pieces of

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social, economic, and political existence.”).

37. *Id.* at 1104 (noting congressional, presidential, and public distrust of private foundations in the early twentieth century).

38. *Id.*

39. In 1916, after several years of hearings, the Commission on Industrial Relations published its findings. U.S. COMM’N INDUS. REL., FINAL REPORT OF THE COMMISSION ON INDUSTRIAL RELATIONS, S. DOC. NO. 64-415, at 81 (1st Sess. 1916); see also Joseph J. Thorndike, *Making the World Safe for Philanthropy*, URB. INST. 8 (Apr. 2013), <https://www.urban.org/sites/default/files/publication/23586/412812-Making-the-World-Safe-for-Philanthropy-The-Wartime-Origins-and-Peacetime-Development-of-the-Tax-Deduction-for-Charitable-Giving.PDF> [https://perma.cc/GKD3-BUA3] (contextualizing the Commission’s report amidst the broader conversation on corporate income and excise taxes).

40. Crimm, *supra* note 34, at 1105 (“Congress took no steps at that time to implement the Walsh Commission’s proposals or recommendations.”). The Commission (sometimes called the Walsh Commission, after its chairman Frank P. Walsh) suggested many limitations on foundations’ size, activities, and lifespan. *Id.* at 1104–05 (“The report proposed restrictions on the size, functions, powers, and lives of foundations, and proposed limitations on the accumulation of unexpended income of private foundations. The report further suggested strict scrutiny of foundations’ investments and open reports to government officials.”).

41. Crimm, *supra* note 34, at 1107.

42. Teresa Odendahl, *Independent Foundations and Wealthy Donors: An Overview*, in AMERICA’S WEALTHY AND THE FUTURE OF FOUNDATIONS 1, 21 (Teresa Odendahl ed., 1987).

43. Tanya D. Marsh, *A Dubious Distinction: Rethinking Tax Treatment of Private Foundations and Public Charities*, 22 VA. TAX REV. 137, 143–44 (2002). Post-World War II, many wealthy Americans sought refuge for their wealth in private foundations in response to soaring income and estate tax rates. See Crimm, *supra*

legislation throughout the 1950s and 1960s attempting to minimize abuses of private foundation status and even considered repealing the unlimited charitable deduction.<sup>44</sup> However, populist concerns about the wealthy using private foundations as tax shelters and political tools prevailed into the 1960s.<sup>45</sup>

The 1960s marked a turning point for foundation reform. Congressman Wright Patman, a Democrat from Texas largely known for his dogged criticism against concentrated economic power,<sup>46</sup> led the charge to reform the regulatory landscape.<sup>47</sup> While concerns about the wealthy using private foundations as tax shelters largely militated these hearings,<sup>48</sup> the resulting 1965 Treasury Department report instead found several other problems: namely, increased concentration of power in foundations, private enrichment of donors and families through foundations, and concerning time lags between the time a donation was gifted and the time the donation was ultimately used for a charitable purpose.<sup>49</sup> The report recommended several legislative fixes to address these issues, ranging from prohibitions on self-dealing to requiring regular payouts to

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note 34, at 1108 n.84–88. In addition, at that time private foundations—like other tax-exempt organizations—could invest in both charitable and commercial opportunities and earn tax-free income. The only caveat was that income needed to be used for exempt (for example, charitable) purposes. Arnsberger et al., *supra* note 35, at 107.

44. See Troyer, *supra* note 20, at 52–59 (explaining the evolution of Congressional treatment of and studies on private foundations from the 1950s to the 1960s).

45. Marsh, *supra* note 43, at 150 (“[Private foundation critics] concluded that large foundations without countervailing accountability possessed too much financial and political power and that wealthy Americans were using foundations to abuse tax laws.”).

46. Eileen Shanahan, *Wright Patman, 82, Dean of House, Dies*, N.Y. TIMES (Mar. 8, 1976), <https://www.nytimes.com/1976/03/08/archives/new-jersey-pages-wright-patman-82-dean-of-house-dies-wright-patman.html> [https://perma.cc/CNV4-ARP5].

47. Marsh, *supra* note 43, at 150 (“In 1961, Representative Wright Patman . . . began a series of high-profile investigations into the activities of private foundations.”).

48. Crimm, *supra* note 34, at 1113–14 (explaining that Congressman Patman’s concern was that some taxpayers were purposefully using private foundations to escape estate taxes).

49. STAFF OF S. COMM. ON FINANCE, 89TH CONG., 1ST SESS., U.S. TREASURY DEPARTMENT REPORT ON PRIVATE FOUNDATIONS (Comm. Print 1965) [hereinafter 1965 TREASURY REPORT]. Despite Congressman Patman’s concerns about private foundations being used as tax shelters, the 1965 Treasury Report found that most private foundations were not abusing the existing tax systems. See *id.* at 2; see also Crimm, *supra* note 34, at 1114–17.



charitable organizations.<sup>50</sup> Despite the call-to-arms in the 1965 Treasury Department report and three subsequent reports in 1966, 1967, and 1968,<sup>51</sup> Congress did not begin to take action until 1969.<sup>52</sup>

The Tax Reform Act of 1969 (“1969 Act”) came into existence after several months of contentious hearings involving both ardent foundation reformers and foundation executives.<sup>53</sup> The hearings highlighted the tension between foundation reformers and proponents of the status quo—reformers focused on the potential for abuse and exploitation of tax-exempt status, while executives from the Ford and Rockefeller Foundations defended their foundations’ philanthropic mission and warned that more stringent regulation may undermine charitable giving.<sup>54</sup> In many ways, the 1969 Act successfully compromised between these two viewpoints<sup>55</sup>—the final legislation did not include more stringent proposals, such as the call to disband private foundations after forty years of existence,<sup>56</sup> but successfully authorized excise taxes on certain activities and imposed a four percent tax on all investment income.<sup>57</sup>

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50. 1965 TREASURY REPORT, *supra* note 49, at 6–10. For an extensive response to the 1965 Treasury Report, see Thomas A. Troyer, *The Treasury Department Report on Private Foundations: A Response to Some Criticisms*, 13 UCLA L. REV. 965 (1966).

51. Marsh, *supra* note 43, at 150; *see also* Crimm, *supra* note 34, at 1117.

52. The House Ways and Means Committee began hearings on private foundations in February 1969. The first witness called to the floor was Congressman Patman. WALDEMAR A. NIELSEN, *THE BIG FOUNDATIONS* 9 (1972).

53. While hearings began in February, the final bill was not enacted until December 30. Tax Reform Act of 1969, Pub. L. No. 91-172, 83 Stat. 487. Before the hearings began, the Secretary of the Treasury—Joseph Barr—gave a “widely publicized” speech to Congress, which warned of a “smoldering ‘tax revolt’ due to tax law inequities, especially ‘loopholes’ such as private foundations permitting very wealthy individuals to avoid taxation.” Crimm, *supra* note 34, at 1118 (quoting Statement of outgoing Secretary of Treasury Joseph Barr, Joint Economic Comm., 91st Cong. (Jan. 17, 1969), reproduced in 115 CONG. REC. 2772 (1969)). Some suggest that this speech spurred national support for private foundation tax reform. *See* Troyer, *supra* note 20, at 59.

54. Marsh, *supra* note 43, at 151–52; Crimm, *supra* note 34, at 1117–20.

55. *Cf.* Troyer, *supra* note 20, at 65 (noting that given the bubbling anti-foundation sentiment amongst members of Congress, the 1969 Act could have been much harsher).

56. John G. Simon, *The Regulation of American Foundations: Looking Backward at the Tax Reform Act of 1969*, 6 VOLUNTAS 243, 245 (1995) (noting that Senator Albert Gore, Sr.’s proposal to “liquidate all foundations at age 40” fared well in the Senate Finance Committee but failed on the Senate floor).

57. Crimm, *supra* note 34, at 1120.

A full discussion on the breadth of regulations engendered through the 1969 Act is beyond the scope of this Note, but two regulations merit deeper explication: the payout and disclosure requirements.

### 1. The Annual Payout Requirement

Serious concerns about the delay between charitable donation and public benefit spurred the creation of a payout requirement for private foundations.<sup>58</sup> In the years leading up to the 1969 Act's passage, Congress considered capping the lives of private foundations to twenty-five or forty years.<sup>59</sup> Instead, the IRS vaguely required that private foundations avoid the "unreasonable" accumulation of income or risk losing tax-exempt status.<sup>60</sup> Professor Ray Madoff suggests that the threat invoked by the IRS—the potential loss of tax-exempt status—was "so draconian that it was rarely imposed," essentially rendering the IRS requirement useless.<sup>61</sup>

In order to spur real action among private foundations and to more fully prevent wealth hoarding, the 1969 Act imposed an annual minimum payout requirement.<sup>62</sup> After some debate over the proper minimum<sup>63</sup> and the exact assets that should be taxed,<sup>64</sup> in 1981 the IRS eventually settled on a flat five percent payout of net investment assets.<sup>65</sup> The payout requirement reflects a central tension in private foundation regulation—how to simultaneously promote

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58. Madoff, *supra* note 29, at 344 ("Congress was particularly concerned about the disconnect between the time of tax benefit for donors and the time of benefit for society.").

59. *Id.* at 345; *see also* Simon, *supra* note 56 (discussing Senate support for proposals to liquidate foundations at forty years of age).

60. Madoff, *supra* note 29, at 345; I.R.C. § 504(a)(1) (1954) (repealed by Pub. L. No. 91-172, § 101(j)(15)).

61. Madoff, *supra* note 29, at 345. In multiple instances when the IRS moved to strip an organization of its tax-exempt status for "unreasonable" accumulation of income, courts reversed the rulings. *See* 1965 TREASURY REPORT, *supra* note 49, at 25–26.

62. Homer C. Wadsworth, *Private Foundations and the Tax Reform Act of 1969*, 39 L. & CONTEMP. PROBS. 255, 260 (1975).

63. Troyer, *supra* note 20, at 57 (noting that at the time of the 1965 Treasury Report, the Treasury Department suggested an annual rate at 3 to 3.5%); Stefan Toepler, *Ending Payout as We Know It: A Conceptual and Comparative Perspective on the Payout Requirement for Foundations*, 33 NONPROFIT & VOLUNTARY SECTOR Q. 729, 730 (2004) (discussing the decision to shift the annual requirement from six percent to five percent).

64. Marsh, *supra* note 43, at 158.

65. I.R.C. § 4942(e)(1).

philanthropy while ensuring a public benefit. The payout requirement prevents wealthy donors from using foundations as tax shelters; while donors still receive an immediate tax benefit when creating a private foundation, the payout requirement helps to ensure that some public benefit occurs each year.<sup>66</sup>

There remains some debate over the efficacy and continued utility of the five percent payout. Some scholars suggest that in times of economic growth, the payout rate should be raised to match investment growth<sup>67</sup> or other economic factors.<sup>68</sup> Others doubt that the five percent payout rate does any good at all.<sup>69</sup> Regardless of the debates over the payout rate, though, there is evidence that the five percent payout rate has helped to legitimize private foundations<sup>70</sup> and likely guards against the same populist, anti-wealth hoarding concerns that led to the 1969 Act.

### 1. The Required Disclosure of Funding Recipients

There is a general presumption that when it comes to preventing fraud, disclosure is preferable to regulation.<sup>71</sup> This is evident in the laws governing private foundation disclosure requirements. The 1969 Act required that private foundations make annual reports—including an itemized list of all grants and contributions, noting the amount and recipient name<sup>72</sup>—available for inspection at their principal offices.<sup>73</sup> Such disclosure is essential

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66. Madoff, *supra* note 29, at 341.

67. See, e.g., Toepler, *supra* note 63, at 731.

68. Elizabeth Boris & C. Eugene Stuerle, *Philanthropic Foundations: Payout and Related Public Policy Issues*, URB. INST. 3 (2004), [http://webarchive.urban.org/UploadedPDF/311032\\_philanthropic\\_foundations.pdf](http://webarchive.urban.org/UploadedPDF/311032_philanthropic_foundations.pdf) [<https://perma.cc/N26N-3BPV>].

69. *But see id.* (“Interestingly, no one really argued for reducing [the payout rate].”).

70. Hackney, *supra* note 29, at 240 (“Professor Madoff . . . believes that the 5% payout has been successful in legitimizing private foundations in the larger culture of the United States.”).

71. See, e.g., *Vill. of Schaumburg v. Citizens for a Better Env’t*, 444 U.S. 620, 637–38 (1980) (“The Village’s legitimate interest in preventing fraud can be better served by measures less intrusive than a direct prohibition on solicitation . . . . Efforts to promote disclosure of the finances of charitable organizations also may assist in preventing fraud by informing the public of the ways in which their contributions will be employed.”).

72. 26 C.F.R § 1.6033-3(a)(2).

73. The Tax Reform Act of 1969, Pub. L. No. 91-172, § 101(e)(3), 83 Stat. 487 (1969) (adding I.R.C. § 6104(d) and requiring private foundations make annual reports available for inspection).

for enforcing the regulations in the 1969 Act. IRS oversight via Form 990-PF<sup>74</sup> filings holds private foundations accountable for fulfilling their charitable purpose and prevents private foundations from engaging in self-dealing and other misuse.<sup>75</sup>

While at first these disclosures were only granted to the IRS, the Tax and Trade Relief Extension Act of 1998 opened up these disclosures for public inspection.<sup>76</sup> Presently, the IRS requires that foundations make their annual tax returns publicly available (i.e., posted online or available upon request).<sup>77</sup> Legislative history of the development of IRS Form 990-PF, the primary tax reporting form that lists funding recipients from private foundations, supports the disclosure of such information to the public.<sup>78</sup> By requiring foundations to disclose grant recipients and relationships via 990-PF forms, a legislative sponsor theorized, members of the public could hold private foundations accountable.<sup>79</sup> Public disclosure of private foundation grantmaking benefits the public in other ways, such as assisting grant applications in identifying potential benefactor foundations.<sup>80</sup>

Regulations applicable to private foundations have evolved over the past several decades in response to concerns about wealth warehousing and charitable dollars potentially languishing in foundations.<sup>81</sup> Many of the same concerns apply to DAFs, which are subject to far fewer regulations.

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74. IRS Form 990-PF is used to “report charitable distributions and activities” and is the key mechanism the IRS uses to track private foundations’ charitable activities. *About Form 990-PF*, IRS (2021), <https://www.irs.gov/forms-pubs/about-form-990-pf> [<https://perma.cc/HZ76-6BNA>].

75. Crimm, *supra* note 34, at 1149–50; *see also* I.R.C. § 4941; I.R.C. § 53.4941.

76. Pub. L. No. 105-277, 112 Stat. 2681 (requiring that private foundations make their annual information returns available for public inspection like public charities).

77. Crimm, *supra* note 34, at 1128.

78. *IRS Oversight of Tax-Exempt Foundations: Hearing Before a Subcomm. of the H. Comm. on Gov’t Operations*, 98th Cong. 1 (1983) (statement of Johnny C. Finch, Assistant Director’ General Government Division, General Accounting Office).

79. *Id.* at 2–5; *see also* U.S. GOV’T ACCOUNTABILITY OFF., GAO/GGD-83-58, PUBLIC INFORMATION REPORTING BY TAX-EXEMPT PRIVATE FOUNDATIONS NEEDS MORE ATTENTION BY IRS ii (1983) (finding that the IRS needs to better enforce private foundation reporting requirements).

80. Carla A. Neeley, *The Private Foundation Rules: Impact of the Tax Reform Act of 1984*, 63 TAXES 251, 266 (1985).

81. *See supra* Part I.A.

B. DONOR-ADVISED FUNDS: DEMOCRATIZERS OF CHARITABLE GIVING OR A NEW FORM OF WEALTH HOARDING?

While DAFs have existed since the 1930s, they were a little-used tool, mostly operated by community foundations,<sup>82</sup> until the 1990s.<sup>83</sup> In 1991, financial institutions like Fidelity Charitable sought—and won—tax-exempt status for their DAFs, paving the way for other national sponsoring organizations (NSOs) to gain public charity status.<sup>84</sup> It is difficult to overstate the impact that the emergence of NSOs<sup>85</sup> had on the DAF landscape; the integration of DAFs into investment funds introduced what had previously been a niche philanthropic tool to the broader market.<sup>86</sup> NSOs could use their corporate means, including marketing ability and efficiencies of scale, to expand the DAF market well beyond its previous confines.<sup>87</sup>

Fidelity Charitable's remarkable emergence as the largest charity in the United States parallels the skyrocketing popularity of DAFs as a charitable giving mechanism. The number of DAF account holders has increased severalfold over just in the past half-decade,

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82. The first DAF was founded in 1931. See Berman, *supra* note 26, at 13. They were pioneered by community foundations, like the New York Community Trust. *Id.* These original DAFs were tied to individual community foundations and were closely intertwined with supporting their unique charitable missions, and there was a presumption that upon donation, the donor placed their trust in the community foundation's board to direct the charitable assets in the most beneficial direction. See Alan M. Cantor, *Donor-Advised Funds and the Shifting Charitable Landscape: Why Congress Must Respond*, B.C. F. ON PHILANTHROPY & PUB. GOOD 131, 132–33 (Oct. 23, 2015), <https://lawdigitalcommons.bc.edu/cgi/viewcontent.cgi?article=1020&context=philanthropy-forum> [<https://perma.cc/G2ZN-EVSZ>]. By the 1990s, most community foundations were already considered public charities by the IRS. Johnson & Jones, *supra* note 26, at pt. 2.D.

83. DAFs stepped into the spotlight when NSOs began seeking 501(c)(3) status. Colinvaux, *supra* note 3, at 47–48.

84. *Id.* at 45–46.

85. As noted previously, DAFs are often broken up into three categories: community foundations, single-issue charities (like universities or certain religious organizations), and NSOs (like Fidelity Charitable or the National Philanthropic Trust). For scale, in 2018 there were approximately 332 single-issue charities, 603 community foundations, and 54 NSOs. See *2019 Donor-Advised Fund Report*, NAT'L PHILANTHROPIC TR. 6 (2019), <https://www.nptrust.org/wp-content/uploads/2019/11/2019-Donor-Advised-Fund-Report-NPT.pdf> [<https://perma.cc/Y474-T84K>]. While relatively few NSOs exist as compared to community foundations, NSOs reported \$72.35 billion in charitable assets in 2018—over twice the amount reported by all community foundations combined (\$33.87 billion). *Id.* at 26, 30.

86. Cf. Berman, *supra* note 26, at 11–14 (describing how early DAFs only existed through community foundations).

87. Cantor, *supra* note 82, at 134.

from 241,507 in 2014 to 728,563 in 2018.<sup>88</sup> Similarly, the value of assets held in DAFs has more than doubled in the past decade, totaling nearly \$73 billion held in NSOs alone.<sup>89</sup> Finally, the rates of DAF grantmaking to charitable organizations has grown as well. In 2018, DAFs granted \$23.42 billion to charitable organizations.<sup>90</sup> The rate of donor-to-DAF grantmaking has increased by ninety percent in recent years and vastly outpaces growth in giving by individuals and charitable giving overall.<sup>91</sup>

The rapid growth in DAFs can partially be attributed to a few factors. First, DAFs of all stripes—including those sponsored by NSOs—characterize their charitable work as democratizing philanthropy.<sup>92</sup> While private foundations involve high start-up costs, require legal input, and carry large administrative burdens, opening a DAF account only requires a signed check.<sup>93</sup> Because of their lower cost and ease of entry, sponsors like DonorsTrust proffer that they bring the opportunity for “thoughtful, strategic charitable giving” to the everyman.<sup>94</sup> And these lower barriers to entry are working. More and more donors are opening DAFs, especially those

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88. See *2019 DAF Report*, *supra* note 85, at 19.

89. See, e.g., *id.* at 28 (finding that the total charitable assets in NSOs’ DAFs increased from \$33.53 billion in 2014 to \$72.35 billion in 2018).

90. *Nonprofits and Donor-Advised Funds: Perceptions and Potential Impacts*, IND. UNIV. LILLY FAM. SCH. PHILANTHROPY 1 (2020) <https://scholarworks.iupui.edu/bitstream/handle/1805/24001/DAF-report201007.pdf> [<https://perma.cc/K9RC-LJHV>].

91. *Id.* (“Between 2014 and 2018, grants made by DAFs increased 90%—over four times as quickly as growth in giving by individuals (17%) and total giving (21%) over the same time frame.”).

92. Benjamin Soskis, *What We Talk About When We Talk About Democratizing Philanthropy*, URB. INST. (June 2017), <https://www.urban.org/policy-centers/center-nonprofits-and-philanthropy/projects/what-we-talk-about-when-we-talk-about-democratizing-philanthropy> [<https://perma.cc/G2WC-2YJ4>] (“Donor-advised funds (DAFs), whether sponsored by commercial firms like Fidelity, community foundations, or web-based entities, have all invoked the rhetoric of democratization to promote their cause.”).

93. See, e.g., *Giving Vehicle Comparison*, *supra* note 18 (noting the administrative requirements for private foundations and how they usually involve “substantial” legal fees).

94. *Myths and Misconceptions About Donor-Advised Funds Part 1*, DONORSTRUST (Sept. 30, 2015), <https://www.donorstrust.org/donor-advised-funds/myths-and-misconceptions-part-1> [<https://perma.cc/DM92-Q5D2>]. DonorsTrust, like many DAF sponsors, has been criticized for enabling anonymous donations to right-wing causes or groups. See, e.g., Andy Kroll, *Exposed: The Dark-Money ATM of the Conservative Movement*, MOTHER JONES (Feb. 5, 2013), <https://www.motherjones.com/politics/2013/02/donors-trust-donor-capital-fund-dark-money-koch-bradley-devos> [<https://perma.cc/F5XG-C35S>].

held by NSOs, each year.<sup>95</sup> But some hurdles remain, especially for some NSOs. While Fidelity Charitable recently removed its minimum contribution requirement,<sup>96</sup> Vanguard Charitable requires a \$25,000 minimum deposit to open a DAF account.<sup>97</sup>

Beyond lofty goals to democratize philanthropy, DAFs are popular with donors for logistical and fiscal reasons, namely “efficiency, convenience, and tax benefits.”<sup>98</sup> DAFs managed by NSOs are particularly efficient and accessible; most NSOs have integrated their charitable arm with their investment management arm, streamlining the process for donors.<sup>99</sup> Perhaps the most compelling reason why DAFs managed by NSOs are so popular, though, is something that feels out of step with their oft-cited mission to democratize philanthropy—a donation to a DAF confers an immediate tax benefit to the donor.<sup>100</sup> This immediate benefit has attracted considerable scrutiny.<sup>101</sup> Despite claims to democratize philanthropy, evidence suggests that DAFs are most frequently used by the wealthiest Americans.<sup>102</sup> Such Americans have the financial

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95. See *supra* notes 88–91 and accompanying text.

96. Alex Daniels, *Fidelity Charitable Allows Donors to Create Fund with Any Amount, No Matter How Small*, CHRON. PHILANTHROPY (Sept. 30, 2020), <https://www.philanthropy.com/article/fidelity-charitable-allows-donors-to-create-fund-with-any-amount-no-matter-how-small> (last visited Nov. 20, 2021) (describing how Fidelity Charitable eliminated its minimum contribution requirement, which used to be \$5,000).

97. *Giving Tools*, VANGUARD CHARITABLE, <https://www.vanguardcharitable.org/resources/giving-vehicles> [<https://perma.cc/RA2P-UQFC>].

98. Colinvaux, *supra* note 3, at 41; see also *A Philanthropic Boom: “Donor-Advised Funds”*, ECONOMIST (Mar. 23, 2017), <https://www.economist.com/finance-and-economics/2017/03/23/a-philanthropic-boom-donor-advised-funds> [<https://perma.cc/HLB2-C5GC>] (discussing one DAF user who “is delighted with his DAF, praising the convenience and tax advantages”).

99. See, e.g., Michael J. Hussey, *Avoiding Misuse of Donor Advised Funds*, 58 CLEV. ST. L. REV. 59, 62–64 (2010).

100. 26 U.S.C. § 170(a)(1) (2018). The Internal Revenue Code (“IRC”) *does* limit the donation amount allowable as a tax deduction to the donor. Cash donations are subject to a sixty percent limitation of the taxpayer’s gross income; donations of appreciated assets are subject to a thirty percent limitation of the taxpayer’s adjusted gross income. See 26 U.S.C. §§ 170(b)(1)(C)(i), 170(b)(1)(G)(i) (2018); see also Borrasso, *supra* note 28, at 1540.

101. See, e.g., Lewis B. Cullman & Ray Madoff, *The Undermining of American Charity*, N.Y. REV. (July 14, 2016), <https://www.nybooks.com/articles/2016/07/14/the-undermining-of-american-charity> [<https://perma.cc/Y8U6-8BBY?type=image>].

102. “The average DAF donor is a member of the wealthiest one tenth of one percent of Americans, with annual income over \$1 million.” Collins et al., *supra* note 11, at 3. High-net-worth donors also engage with DAFs in different ways than other

ability to donate large sums of money to charity; DAFs can accept complex assets like non-publicly traded stocks or land, unlike private foundations or standalone charities; and donations to DAF accounts are taxed at their current full fair market value, rather than the initial investment (as donations to private foundations are).<sup>103</sup>

Criticism directed towards DAF donors for taking advantage of existing tax schemes to avoid paying taxes on certain economic windfalls,<sup>104</sup> unsurprisingly, feels reminiscent of similar criticism towards private foundations from the 1950s.<sup>105</sup> To this end, DAFs are frequently criticized for two perceived issues: a lack of a payout requirement and a lack of transparency.

#### 1. Unlike Private Foundations, There Are No Payout Requirements for DAFs

While DAFs are governed by *some* restrictions—namely, restrictions on who can receive DAF distributions (registered charities, not individuals or private foundations)—IRS regulations do not require any DAF payout minimums.<sup>106</sup> While payout requirements were discussed by the federal government several times, including a Treasury Department budget proposal in 2000<sup>107</sup> and a proposed five-year payout for all DAFs as part of Congressional tax reform in 2014,<sup>108</sup> no legislation resulted. Still, donors receive an immediate tax benefit when giving money to a DAF.<sup>109</sup>

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donors. For example, high-net-worth donors are more likely to use DAFs as an investment growth tool for their charitable assets and are more likely to involve family members in conversations around charitable giving. *See 2015 Giving Report*, FID. CHARITABLE 20–22, <https://www.fidelitycharitable.org/content/dam/fc-public/docs/insights/2015-giving-report.pdf> [<https://perma.cc/P24L-KS2C>].

103. Collins et al., *supra* note 11, at 20; *see also A Philanthropic Boom: “Donor-Advised Funds”*, *supra* note 98 (“In 2013 around 28% of donations to DAFs were non-cash.”).

104. *See, e.g.*, Paul Sullivan, *Lawsuit Could Cool a Fast-Growing Way of Giving to Charities*, N.Y. TIMES (May 31, 2019), <https://www.nytimes.com/2019/05/31/your-money/donor-advised-funds-charitable-giving-lawsuit.html> [<https://perma.cc/REU4-VJUH>] (“[DAFs] have been particularly popular in Silicon Valley, where tech executives time the donation of stock in conjunction with their firm’s initial public offering to maximize their tax benefit and avoid paying a capital-gains tax.”).

105. *See supra* Part I.A.

106. This stands in contrast to private foundations’ annual five percent payout requirement. *See* I.R.C. § 4942(e)(1).

107. *General Explanations of the Administration’s Fiscal Year 2001 Revenue Proposals*, *supra* note 17, at 105–07.

108. Colinvaux, *supra* note 3, at 50; *see also* Tax Reform Act of 2014, H.R. 1, 113th Cong. § 4968 (2014) (introduced by Rep. Dave Camp).

109. *See supra* note 100 and accompanying text.



Concerns around the time-lapse between donation and disbursement have led some to call for a required annual payout.<sup>110</sup> In particular, critics note that the structure and systems in place at DAF sponsors (especially NSOs) disincentivize grantmaking.<sup>111</sup> NSOs like Fidelity Charitable profit off the administrative fees associated with DAFs, and because larger fund sizes lead to more fees, some suggest that the NSOs tacitly disincentivize donors from making grants from their accounts.<sup>112</sup> However, the aggregate payout rate of one NSO—the National Philanthropic Trust—has held steady at around 20 percent for the past several years, causing some to question the rationale behind requiring a payout rate.<sup>113</sup>

Beyond concerns around payout rates and the time elapsed between the original donation and the grant to a charity, DAF reformers also focus on another concern: the use of DAFs to shield donors' identity.

## 2. DAF Sponsors Only Disclose Grant Recipients at a Macro Level, Limiting Transparency

Much like private foundations, each DAF sponsor—as a tax-exempt organization—must file and publicize their IRS Form 990 annually.<sup>114</sup> However, DAF sponsors report grantmaking from all accounts *in aggregate*—no data from each individual account or its grantmaking is identified.<sup>115</sup> This is because each DAF *sponsor*, not

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110. See Colinvaux, *supra* note 3, at 47–51; Ann Charles Watts, *The Wolf in Charity's Clothing: Behavioral Economics and the Case for Donor-Advised Fund Reform*, 43 U. DAYTON L. REV. 417, 421–23 (2018).

111. Watts, *supra* note 110, at 438.

112. *Id.*

113. 2019 DAF Report, *supra* note 85, at 20. It is worth noting that these reports cover payout in *aggregate* across *all* DAF accounts and that NSOs do not publish disaggregated payout rates. Other DAF reformers suggest that if requiring a payout rate proves unfeasible, DAFs should at least be required to disclose the payout rate for each account in order to promote transparency. See generally H. Daniel Heist & Danielle Vance-McMullen, *Understanding Donor-Advised Funds: How Grants Flow During Recessions*, 48 NONPROFIT & VOLUNTARY SECTOR Q. 1066, 1071 (2019) (discussing a lack of data at the individual account level).

114. While the principle of disclosing all grant recipients works well in theory, it provides little utility in practice. For example, in 2018 Fidelity Charitable's IRS Form 990 was more than 17,000 pages long and listed grant recipients from 114,245 DAF accounts. Fidelity Investments Charitable Gift Fund, Income Tax Form for 2018, Form 990, Schedule D, Part I [hereinafter Fidelity Charitable 990], [https://apps.irs.gov/pub/epostcard/cor/110303001\\_201806\\_990\\_2019071116477237.pdf](https://apps.irs.gov/pub/epostcard/cor/110303001_201806_990_2019071116477237.pdf) [https://perma.cc/5GSZ-SZGU].

115. See, e.g., *id.* Grantmaking is also published through Schedule B forms, which shows donations over a particular dollar amount. See *Schedule of Contributors (2020)*,

each individual fund, is the organization that holds the tax-exempt determination with the IRS.<sup>116</sup> No identifiable information with regard to the individual fund is shared with the IRS. Individual funds can choose to make their donations anonymously (i.e., their identity is not revealed to the recipient), or they can choose to be recognized for their gift.<sup>117</sup>

The perceived lack of transparency involved with DAF donations has garnered criticism. Nonprofit advocates tend to focus on the interruption of relationship-building; by opening up the ability to give anonymously, nonprofits worry that the growing popularity of DAFs may make it more difficult to build a traditional donor-recipient relationship.<sup>118</sup> Transparency advocates voice concern over DAFs' ability to obfuscate donor identity, particularly when donating to less-than-savory causes.<sup>119</sup> A recent bill in

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IRS, <https://www.irs.gov/pub/irs-pdf/f990ezb.pdf> [<https://perma.cc/TBV6-R5HF>].

116. *Donor-Advised Funds*, IRS, <https://www.irs.gov/charities-non-profits/charitable-organizations/donor-advised-funds> [<https://perma.cc/KWM5-HHJK>].

117. See, e.g., *What Is a Donor-Advised Fund?*, FID. CHARITABLE, <https://www.fidelitycharitable.org/guidance/philanthropy/what-is-a-donor-advised-fund.html> [<https://perma.cc/ZUF6-JFFK>]. For example, MacKenzie Scott—the author and former spouse of Amazon founder, Jeff Bezos—notably directed much of her recent philanthropy through a Fidelity Charitable DAF. She disclosed the identity of several of her gift recipients but was under no obligation to do so. See Nicholas Kulish, *Giving Billions Fast, MacKenzie Scott Upends Philanthropy*, N.Y. TIMES (June 15, 2021), <https://www.nytimes.com/2020/12/20/business/mackenzie-scott-philanthropy.html> [<https://perma.cc/QG8M-5A8Z>] (“[MacKenzie Scott’s] fund will eventually disclose the groups that received money, but is not required to say who is behind each gift. Ms. Scott is under no obligation to publicly disclose anything about her giving.”).

118. Many nonprofits value the ability to build relationships with donors for several reasons, including establishing connections, sharing their message, and identifying donors to ask for donations. Donor-advised funds, because they act as an intermediary, can interrupt this relationship. *2020 Nonprofit and DAF Report*, *supra* note 90, at 9 (“Nonprofit organizations have some concerns about DAFs, primarily about the donor-recipient relationship.”). Identifying donors plays a crucial role in a nonprofit’s strategy to build and retain a consistent donor base (and, by extension, consistent financial support). See, e.g., Adrian Sargeant, *Donor Retention: What Do We Know & What Can We Do About It?*, NONPROFIT Q. (Aug. 15, 2013), <https://nonprofitquarterly.org/donor-retention-nonprofit-donors> [<https://perma.cc/8WTJ-NGNV>] (discussing actions that nonprofits can take to improve donor loyalty, such as keeping in regular contact with donors).

119. See, e.g., Kroll, *supra* note 94 (discussing DonorsTrust, a DAF sometimes used for large-scale donations to right-wing causes); see also *Bullock v. IRS*, 401 F. Supp. 3d 1144, 1159 (D. Mont. 2019) (“Plaintiffs . . . suggest that information concerning the identity of exempt organizations’ contributors remains critical for enforcing limits on political activity.”). But see Victoria B. Bjorklund, *The Rise of Donor-Advised Funds: Why Congress Should Not Respond*, B.C. F. ON PHILANTHROPY &

California attempted to address several of these transparency issues.<sup>120</sup> The legislation would have required California-based DAFs to report both “asset size and grant distributions” annually for each individual fund.<sup>121</sup> The bill never made it to the governor’s desk; in early 2020, it stalled in the California legislature.<sup>122</sup>

Further, critics of transparency-focused reform note that increasing reporting requirements may raise administrative fees, placing DAFs out of reach for some potential donors and harming smaller DAF sponsors like community foundations.<sup>123</sup> Others argue that the ability to anonymize donations provides certain safeguards against public backlash, especially when giving to socially unpopular causes.<sup>124</sup>

Beyond the criticisms and arguments in favor of DAFs, it is irrefutable that the IRS regulatory regime treats DAFs and private foundations distinctly. The stringent IRS regulations applicable to private foundations—and the lack thereof applicable to DAFs—has

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PUB. GOOD 69, 92 (Oct. 23, 2015), <https://lawdigitalcommons.bc.edu/cgi/viewcontent.cgi?article=1018&context=philanthropy-forum> [https://perma.cc/WS8P-PKQ5] (noting that some donors prefer to give anonymously for religious reasons).

120. Assemb. B. 1712, 2019 Assemb., Reg. Sess. (2019).

121. Alan M. Cantor, *Why Vested Interests Don't Want Donor-Advised Funds to Do More for Charities*, CHRON. PHILANTHROPY (Mar. 4, 2020), <https://www.philanthropy.com/article/why-vested-interests-dont-want-donor-advised-funds-to-do-more-for-charities> (last visited Nov. 20, 2021) (outlining the California bill and explaining that those pushing for “tighter regulation” have reemphasized the viewpoint that “many donor-advised funds sit idle or are barely used”); *see also id.*

122. Cantor, *supra* note 121. Reporting on the bill suggests that it stalled due to concerns about the costs that increased administrative burdens (i.e., reporting requirements) would impose on NSOs. *See* Robert Tigner, *California Would Be First State Law to Reach DAFs*, NONPROFIT TIMES (Feb. 10, 2020), <https://www.thenonproffitimes.com/legal/california-would-be-the-first-state-law-to-reach-dafs> [https://perma.cc/H2T3-NY2E].

123. Ellen Steele & Eugene Steuerle, *Discerning the True Policy Debate Over Donor-Advised Funds*, URB. INST. 8 (Oct. 2015), <https://www.urban.org/sites/default/files/publication/72241/2000481-Discerning-the-True-Policy-Debate-over-Donor-Advised-Funds.pdf> [https://perma.cc/86CU-FQAU].

124. Marc Gunther, *Foundations Are Sending More Dollars to Donor-Advised Funds, Chronicle Analysis Finds*, CHRON. PHILANTHROPY (Oct. 13, 2020), <https://www.philanthropy.com/article/foundations-are-sending-more-dollars-to-donor-advised-funds-chronicle-analysis-finds> (last visited Nov. 20, 2021) (“The Bolthouse Foundation, for example, faced criticism many years ago because it funded conservative nonprofits, including those opposed to abortion rights and gay marriage. Some critics called for boycotts of the family business, Bolthouse Farms, which sells baby carrots, high-end juices, and salad dressings, even though the company was no longer owned by the family. In any event, the foundation has made all its grants since 2006—\$120.4 million in total—to a donor-advised fund at the National Christian Foundation.”).

altered the landscape of charitable giving. DAFs continue to grow in popularity, and private foundations have taken advantage of DAFs' welcoming regulatory regime. As discussed in Part II, private foundations sometimes take advantage of DAFs' lenient regulatory structure, which limits governmental oversight and subverts the intent behind the 1969 Act.

## II. THE NEED TO REGULATE PRIVATE FOUNDATION-TO-DAF GIVING

For many charitable donors, DAFs present an accessible opportunity to thoughtfully direct philanthropic dollars. Democratizing charitable giving and promoting philanthropy should not be discouraged. But for private foundations, several benefits associated with DAFs—including the opportunity to meet the five percent payout requirement and the ability to obfuscate their identity—subvert the 1969 Act's central goals: preventing wealth warehousing and promoting public disclosure of charitable giving.<sup>125</sup> While there are certainly valid reasons why private foundations may choose to direct their charitable giving through DAFs,<sup>126</sup> the availability of the DAF loophole presents a troubling opportunity for bad actors to avoid federal regulation.

This Part names the specific harms created by private foundation-to-DAF giving. It first demonstrates how private foundation donations to DAFs are quickly growing in popularity. As these donations become more popular and widely used, they aggravate an existing problem—the delay of billions in donations to working charities who, but for the existence of DAFs, might have received charitable donations. Further, DAFs present opportunities for private foundations to build charitable wealth therein, signaling a troubling return to the environment that led to the 1969 Act and the introduction of the payout requirement. This Part then explores the ways that DAFs allow private foundations to evade public scrutiny in their grantmaking and how DAFs particularly frustrate the government-level and public transparency efforts sought through the 1969 Act and other IRS regulations. Finally, this Part situates these harms within the growing body of work calling for legislation

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125. See discussion *supra* Part I.A.

126. See Bjorklund, *supra* note 119, at 92 (discussing the reasons why donors choose to give through DAFs, such as for religious reasons, to avoid solicitation, or to avoid additional paperwork).

to address wealth inequality, greater transparency in government and campaign finance laws, and fallout from the COVID-19 pandemic.

A. THE RISE OF PRIVATE FOUNDATION-TO-DAF GIVING IS DELAYING BILLIONS IN DONATIONS TO WORKING CHARITIES

The 1969 Act attempted to thread the needle between promoting philanthropy and ensuring that charitable dollars did not just sit, gathering dust, in private foundations' coffers.<sup>127</sup> Imposing a payout floor was one aspect of the Act's intent. By requiring that private foundations annually grant at least five percent of their net investment assets for the previous year,<sup>128</sup> the IRS ensured that, at a minimum, charitable organizations and the public received some benefit from tax-exempt dollars.<sup>129</sup> But the availability of DAFs as a tool to meet this payout requirement has resulted in a substantial increase in private foundation-to-DAF giving.<sup>130</sup> Below, this Part explores this growing trend and demonstrates its very real consequences—billions of dollars in delayed charitable giving.<sup>131</sup>

1. Private Foundation-to-DAF Giving Is on the Rise

Evidence suggests that a majority of private foundations use DAFs infrequently, if at all.<sup>132</sup> But recent research shows evidence that some private foundations grant the majority of their annual charitable giving to DAFs, rather than directly to charities.<sup>133</sup> Perhaps the most egregious example is Larry Page's private foundation: the Carl Victor Page Memorial Foundation.<sup>134</sup> In 2017, the Foundation

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127. Wadsworth, *supra* note 62, at 258, 261–62; Madoff, *supra* note 29, at 341.

128. I.R.C. § 4942(e)(1).

129. Madoff, *supra* note 29, at 341.

130. *See infra* Part II.A.1.

131. *See infra* Part II.A.2.

132. *Cf. A Philanthropic Boom: "Donor-Advised Funds"*, *supra* note 98 ("The Economist examined grants from a random sample of about 4,000 foundations. Some 40 of them routed cash to the biggest DAF providers . . .").

133. For example, a 2020 Minnesota Council of Nonprofits report found 2,203 instances of private foundation grantmaking to the five largest DAF sponsors between 2010 and 2018. In total, such grantmaking amounted to \$3 billion. Aanstad et al., *supra* note 23, at 6.

134. Larry Page is one of the two co-founders of Google; the foundation is named after his late father. *Larry Page*, ENCYC. BRITANNICA, <https://www.britannica.com/biography/Larry-Page> [<https://perma.cc/VL36-UZYY>]; *see also Carl Victor Page Memorial Foundation*, BLOOMBERG, <https://www.bloomberg.com/profile/company/0208884D:US> [<https://perma.cc/2B89-8ZZS>] (noting that Larry Page, a founder of Google, is the chairman of the foundation).

gave \$901,000 directly to charities—and \$180 million to DAFs.<sup>135</sup> The 2017 grantmaking that went directly to charities would not have satisfied the five percent payout requirement.<sup>136</sup> The five percent threshold was only reached through the DAF donations.<sup>137</sup> Another smaller private foundation, the 136 Fund, granted \$100 million to charities from 2014 to 2016.<sup>138</sup> All of these funds went directly to DAFs; not a single dollar was given directly to a working charity.<sup>139</sup> The Carl Victor Page Foundation and 136 Fund exemplify a particular kind of private foundation—one that gives nearly all of its charitable dollars to a DAF.<sup>140</sup>

While the number of individual foundations that engage in such activity may be relatively small, the considerable monetary value of the donations going to DAFs instead of directly to working charities should invite scrutiny. A Chronicle of Philanthropy report from 2018 found that, from 2014 to 2016, private foundations granted \$737 million to the five largest DAF sponsors.<sup>141</sup> Currently, this amount represents a small percentage of all private foundation giving—but it also signals an increasing trend.<sup>142</sup> In 2018 alone, the latest year for which foundation grantmaking data is available, private foundations granted \$740 million to DAFs—exceeding the sum of private foundation-to-DAF grantmaking for 2014, 2015, and 2016 combined.<sup>143</sup> As DAFs grow in popularity, more and more private foundations are choosing to use DAFs as a conduit for their

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135. Schleifer, *supra* note 22.

136. The Carl Victor Page Memorial Foundation's endowment in 2017 was measured at \$3 billion—the aggregated \$901,000 donated directly to charities would not satisfy the five percent payout requirement. *Id.*

137. *Id.*

138. Peter Olsen-Phillips, *Foundations Move \$737 Million to Donor-Advised Funds, Chronicle Study Shows*, CHRON. PHILANTHROPY (May 14, 2018), <https://www.philanthropy.com/article/foundations-move-737-million-to-donor-advised-funds-chronicle-study-shows> (last visited Nov. 20, 2021). The 136 Fund received \$154 million from 2014 to 2016. *Id.*

139. *Id.*

140. The research from the *Economist* noted above found additional examples of private foundations granting a vast majority of their charitable dollars to DAFs. *A Philanthropic Boom, "Donor-Advised Funds"*, *supra* note 98 (discussing how in their study of 4,000 random private foundations, they found eleven foundations that granted over 90 percent of their annual charitable giving to DAFs).

141. Olsen-Phillips, *supra* note 138.

142. Compare Olsen-Phillips, *supra* note 138 (noting that in 2014, private foundation giving totaled \$41 billion), with Gunther, *supra* note 124 (pointing out that foundations are sending increasing percentages of their funds to DAFs).

143. Gunther, *supra* note 124.

charitable donations. By using the DAF mechanism, these foundations are—intentionally or unintentionally—escaping regulatory and public oversight of their charitable activity and delaying the benefit received by working charities.

## 2. Donations to DAFs Delay the Benefit Received by Working Charities

One of the greatest harms engendered through foundation-to-DAF grantmaking is the delay in funding to working charities.<sup>144</sup> Private foundations and those who contribute to them receive numerous tax advantages and other benefits: for the donor, savings on income and capital gains taxes; for the foundation itself, the opportunity to grow its endowment in a tax-advantaged environment.<sup>145</sup> In exchange, the IRS places limitations and rules on how the funds can be used in order to prevent misuse—including the annual minimum payout requirement.<sup>146</sup> In many ways, the act of charitable gift-giving and the resulting tax benefits received by the donor creates a bargain between the donor and the federal government.<sup>147</sup> With DAFs, the bargain becomes unequal. The donor

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144. Another action that creates a delay in monetary benefit to working charities is a DAF-to-DAF transfer, which is outside the scope of this paper. As discussed in Part I.B, because DAFs are categorized as charities, it is entirely legal for DAFs to grant money to *other* DAFs. Such a donation incurs no tax benefit; some believe that DAF account holders engage in such activity for the sake of convenience (i.e., if the account holder changes wealth management from Fidelity Charitable to Vanguard) or to take advantage of different funds' investment options. Eden Stiffman, *At Least \$1 Billion Has Been Shuttled From One Commercial Donor-Advised Fund to Another in a Year—and Not to Working Charities*, CRON. PHILANTHROPY (Sept. 15, 2021), <https://www.philanthropy.com/article/at-least-1-billion-has-been-shuttled-from-one-commercial-donor-advised-fund-to-another-in-a-year-and-not-to-working-charities> (last visited Nov. 20, 2021); Ken Nopar, *Significant Increase in Donor Advised Fund Transfers*, AM. ENDOWMENT FOUND., <https://www.aefonline.org/blog/significant-increase-donor-advised-fund-transfers> [<https://perma.cc/DX7D-KM4F>]. Because other DAFs are categorized as charitable organizations, though, a DAF-to-DAF transfer counts towards each DAF sponsor's payout rate—even though a working charity hasn't yet received the funds. *See, e.g., id.*

145. *See, e.g.,* Page Snow, *The Tax Benefits of Creating a Private Foundation*, FORBES (Apr. 8, 2019), <https://www.forbes.com/sites/pagesnow/2019/04/08/the-tax-benefits-of-doing-the-right-thing> [<https://perma.cc/787F-5SX6>].

146. *See* I.R.C. §§ 4941–4945 (describing taxes that private foundations may face for failing to adhere to IRS regulations, including taxes on self-dealing, failure to distribute income, and excess business holdings).

147. *Cf.* Collins et al., *supra* note 11, at 22 (“[T]he bargain that was struck with the public was that in exchange for their donors getting a deduction for their gifts, the

receives the same immediate tax benefit if they give to a working charity or to DAF. But a gift to a DAF results in a delayed benefit to working charities, and the IRS does not account for this delay.

In analyzing the difficulties created by delayed charitable benefit and DAFs, scholars argue that DAFs function as substitutes for working charities. As Professor Roger Colinvaux notes: “In a zero-sum game, the success of DAFs comes at the expense of other public charities, deferring the date when operating charities can benefit from funds.”<sup>148</sup> Instead of granting money to, say, a charity organization for pediatric cancer (where the funds can be put to immediate use), a grant to a DAF further delays the benefit because the donor is under no time pressure to disburse the funds.

Further, the mechanics of DAF sponsors—particularly NSOs—have been criticized for implicitly delaying grantmaking from donor accounts.<sup>149</sup> Once in a DAF, donors may assume a growth mindset towards the charitable funds—that is, focus more strongly on the DAF sponsor’s ability to grow the account value through investments rather than on the eventual recipients of the funds.<sup>150</sup> Such attitudes are likely compounded by the assignable nature of DAFs. Because DAF accounts can be assigned successors, donors are under no pressure to grant funds within their own lifetimes.<sup>151</sup> Such criticisms are especially relevant for private foundations, which (theoretically) could exist in perpetuity.

Concerns about delayed benefit are not just academic or theoretical. In 2016, the President of CharityWatch—a charity watchdog group—estimated that the popularity of DAFs has delayed \$15 billion in donations to American charities.<sup>152</sup> The lack of a payout requirement compounds concerns over delayed benefit;

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charity’s work would benefit the public as a whole, and not any single individual.”).

148. Colinvaux, *supra* note 3, at 54.

149. *Id.* at 56–57; *see also* discussion *supra* notes 106–09.

150. *See* Colinvaux, *supra* note 3, at 57 (“Before the DAF, the donor might have made contributions to a variety of public charities in small amounts each year. But now that the donor’s annual giving may accumulate in a DAF, the donor starts to think about giving differently—less as making current contributions and more as saving for the future . . . . For the donor, this reinforces the idea that money set aside in a DAF is more of an investment than a spending transaction.”).

151. *Id.* at 57–58.

152. Ana Swanson, *Wall Street Is Sitting on Billions Meant for American Charities*, WASH. POST (June 21, 2016), <https://www.washingtonpost.com/news/wonk/wp/2016/06/21/the-questionable-new-way-wealthy-people-are-giving-to-charity> [<https://perma.cc/VL36-98V6>] (“Our charitable resources are getting locked away . . . it’s problematic for us to be taking \$15 billion off the table for later.” (quoting Borochoff, president of CharityWatch)).



because DAFs are not subject to any required disbursement, there is no telling when these funds will *actually* reach working charities.<sup>153</sup>

In sum, private foundation donations to DAFs throw tax-exempt dollars into philanthropic limbo. The charitable funds, possibly granted to a DAF for the sole purpose of meeting IRS payout rules, enter an unlimited holding pattern with no date by which the funds must be granted out to working charities. The 1969 Act sought to prevent such behavior by imposing annual payout requirements—but such requirements can be effectively pushed aside through donations to DAFs.<sup>154</sup> Beyond the subversion of the 1969 Act, though, private foundation-to-DAF giving creates tangible consequences in the philanthropic sector—billions in funding delays to working charities.<sup>155</sup>

The effects of private foundation grantmaking to DAFs goes beyond delayed donations to working charities. As discussed in the next Part, DAFs allow private foundations to anonymize grantmaking and avoid public and governmental oversight of the recipients of their philanthropic funds.

#### B. PRIVATE FOUNDATION-TO-DAF GRANTMAKING ALLOWS FOUNDATION DONATIONS TO EVADE PUBLIC SCRUTINY

The evolution of IRS regulation of charitable organizations arches in favor of disclosure.<sup>156</sup> Since the 1960s, federal legislation has required increased disclosure—first to the IRS, via Form 990s, then to the public, via mandatory public disclosures—of private foundations' grantees.<sup>157</sup> Disclosure, both to the public and to governmental regulators, holds organizations accountable and putatively prevents misuse.<sup>158</sup> But because DAFs only report grantmaking in the aggregate, rather than by each individual account,<sup>159</sup> they provide a loophole for private foundations to (intentionally or unintentionally) obfuscate the identities of their grantees.

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153. Borrasso, *supra* note 28, at 1557–60.

154. See Madoff, *supra* note 29, at 347–49.

155. Swanson, *supra* note 152.

156. See *supra* Part I.A.2; see also Vill. of Schaumburg v. Citizens for a Better Env't, 444 U.S. 620, 637–38 (1980) (“Efforts to promote disclosure of the finances of charitable organizations also may assist in preventing fraud by informing the public of the ways in which their contributions will be employed.”).

157. See *supra* Part I.A.2.

158. *Id.*

159. See discussion *supra* notes 114–17.

### 1. Grants Made Through DAFs Cannot Be Traced Back to a Private Foundation via Public- or Government-Facing Documents

Private foundation laws have evolved to require both public- and IRS-facing disclosure of all funding recipients. The 1969 Act required that private foundations make annual reports of all grants and contributions, including recipient names, available for inspection by the IRS.<sup>160</sup> The Tax and Trade Relief Extension Act of 1998 went a step further and required that all private foundations open up these documents for public inspection.<sup>161</sup> The importance of public trust and accountability underlies this evolution, something underscored through the legislative history of Form 990-PF—the principal tax form used by private foundations to disclose funding recipients.<sup>162</sup> It is clear that the federal government—to a certain extent—envisions the public as playing a key role in maintaining oversight of charitable dollars.

But private foundation donations to DAFs interrupt public disclosure. Private foundations are required to report all grants to 501(c)(3) organizations (including DAFs) on their Form 990-PF.<sup>163</sup> Under the current IRS Form 990 reporting requirements, DAF sponsors only report annual grantmaking at a macro-level—Form 990 reports the amount granted to each charitable organization and does not publish any account-level information.<sup>164</sup> Unless a private foundation were to publish their annual DAF account grantmaking themselves, there is no way to distinguish account-level grantmaking from DAFs' Form 990s. It would be impossible to determine which charities receive a private foundation's funds through a DAF via published forms.<sup>165</sup> In essence, once a private foundation grants

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160. 26 C.F.R. § 1.6033-3(a)(2); Tax Reform Act of 1969, Pub. L. No. 91-172, § 101(e)(3), 83 Stat. 487 (1969) (adding I.R.C. § 6104(d) and requiring private foundations make annual reports available for inspection).

161. Pub. L. No. 105-277, § 1004, 112 Stat. 2681 (1999) (requiring that private foundations make their annual information returns available for public inspection, like public charities).

162. See discussion *supra* note 78; see also *About Form 990-PF*, *supra* note 74.

163. DAF sponsors are registered 501(c)(3) charitable organizations, and, as such, a donation to a DAF satisfies the payout requirement. *Donor-Advised Funds*, *supra* note 116. Of course, such reporting only tells you how much money the foundation is granting to the DAF—the private foundation has no reporting requirement to identify the ultimate recipients of the funds.

164. See, e.g., *Fidelity Charitable 990*, *supra* note 114.

165. As previously noted, private foundations disclose grant recipients via IRS Form 990-PF, and 501(c)(3) charities (including DAF sponsors) disclose grant recipients via IRS Form 990. When a private foundation makes a grant to a DAF, the DAF is listed as the recipient on the private foundation's Form 990-PF; when the

money to a DAF, IRS regulations promoting public disclosure cease to have an effect and public disclosure evaporates.<sup>166</sup>

## 2. Foundations Can Use DAFs to Discreetly Give to Unsavory Causes

As discussed above, part of the bargain between private foundations and regulators is that private foundations disclose who receives their funds. So despite this regulatory (and normative) expectation that private foundations disclose their fund recipients, some foundations use DAFs to anonymously give to politically unpopular or unsavory causes.<sup>167</sup> For example, the DAF DonorsTrust has come under criticism for its role in helping channel dollars towards right-wing causes denying climate change.<sup>168</sup>

There is also a power component at play here. Private foundations—and even DAFs, despite their claims to democratize philanthropy—are nearly exclusively the purview of the very wealthy.<sup>169</sup> Private foundations are especially so, given the time and legal expertise necessary to establish one. Private foundations don't route charitable giving through DAFs for a \$20 donation to a local art museum; these are gifts of a substantial size.<sup>170</sup>

There are, of course, valid reasons why private foundations might choose to route charitable giving through a DAF.<sup>171</sup> Anonymous grantmaking through DAFs allows private foundations

private foundation eventually advises the DAF to make a donation to a charity, then that grant would be listed on the *DAF sponsor's* Form 990—with no indication that it came from the private foundation's DAF account. *See supra* notes 71, 113–14.

166. *See discussion supra* Part I.B.2.

167. *Myths and Misconceptions About Donor-Advised Funds-Part 1, supra* note 94. Donors Trust, like many DAF sponsors, has been criticized for enabling anonymous donations to right-wing causes or groups. *See Kroll, supra* note 94.

168. Kroll, *supra* note 94.

169. *See discussion supra* note 102.

170. *See, e.g.,* David Callahan, *The Price of Privacy: What's Wrong with the New Shadow Giving System*, HISTPHIL (Aug. 1, 2018), <https://histphil.org/2018/08/01/the-price-of-privacy-whats-wrong-with-the-new-shadow-giving-system> [<https://perma.cc/4AV7-YKDP>]; *see also Zoom Foundation 990-PF 2016*, PROPUBLICA, <https://projects.propublica.org/nonprofits/organizations/61600601/201633149349101018/full> [<https://perma.cc/L2LH-GP5E>] (showing that in 2016, the Zoom Foundation—a private foundation based in Connecticut—gave nearly \$47 million to donor-advised funds).

171. Arguably, however, if a donor is concerned about anonymous giving, they could just make the donation personally, rather than through a private foundation. Personal donations are not subject to any disclosure requirements. *See* Daniel Hemel, *Who's Afraid of Donor Advised Funds?*, MEDIUM (Aug. 14, 2018), <https://medium.com/whatever-source-derived/whos-afraid-of-donor-advised-funds-669846573095> (last visited Nov. 20, 2021).

to give to causes that may be divisive or indirectly aligned with their charitable mission.<sup>172</sup> Others argue that granting money through a DAF promotes efficiency and lessens administrative burdens.<sup>173</sup> But regardless of *why* a private foundation might choose to anonymize their giving, anonymous donations cloaked through a DAF run evades both public and governmental scrutiny.

Beyond the specific harms named above, the issue of private foundation-to-DAF grantmaking stands in stark relief when discussed in the context of COVID-19 and contemporary reforms to address growing wealth inequality and promote transparency in government. The next Section analyzes how the private foundation giving to DAFs fits into these other progressive movements and argues that regulating private foundations and DAFs is something that must be tackled sooner, rather than later.

### C. REGULATING PRIVATE FOUNDATION-TO-DAF DONATIONS FITS INTO CURRENT CALLS TO ADDRESS WEALTH INEQUALITY AND INSTITUTIONAL TRANSPARENCY

This Note's call to regulate private foundations and their donations to DAFs exists within an environment strikingly similar to the one leading up to the 1969 Act. Much like how private foundations faced little regulation throughout the 1950s and 1960s,<sup>174</sup> DAFs operate with few oversight mechanisms.<sup>175</sup> And much like how private foundations' endowments ballooned in the mid-20th century,<sup>176</sup> the amount of charitable dollars held by DAF sponsors continues to skyrocket.<sup>177</sup>

Within this environment, the lenient regulatory structure governing DAFs allows some private foundations to take advantage of regulations and avoid the IRS rules put in place to govern private foundations' wealth accumulation and public disclosure. This Section builds on the specific harms named in Section II.A and II.B and contextualizes them within contemporary calls to tackle rising wealth inequality and increase transparency in philanthropy.

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172. Olsen-Phillips, *supra* note 138 (quoting the general counsel of the National Philanthropic Trust, one of the largest DAF sponsors).

173. *Id.*

174. *See* discussion *supra* Part I.A.

175. *See* discussion *supra* Part I.B.

176. *See* Odendahl, *supra* note 42.

177. *See* discussion *supra* notes 88–91.

### 1. Rising Wealth Inequality and COVID-19

Wealth inequality in the United States has reached a peak not seen in decades.<sup>178</sup> A 2018 report by the Economic Policy Institute found that families within the top 1% of income earned 26.3 times more than the bottom 99%.<sup>179</sup> The typical worker in the United States has experienced stagnant real wages and declining intergenerational economic mobility.<sup>180</sup> The COVID-19 pandemic has only exacerbated these concerns,<sup>181</sup> as the brunt of pandemic-related job losses impacted historically disadvantaged groups, including people of color and minimum-wage earners.<sup>182</sup>

As the gap between the wealthy and working class continues to widen, it is worth reiterating that private foundations and DAFs are primarily utilized by those at the top of the income pyramid—high-net worth individuals.<sup>183</sup> Private foundations are costly—both in time and money—to set up and properly run.<sup>184</sup> Because of the difficulty inherent in setting one up, it is likely that only those with a substantial interest in setting up a long-term vehicle to hold and disburse philanthropic gifts establish private foundations. The average American—who may be living paycheck-to-paycheck and, on average, has under \$9,000 in savings<sup>185</sup>—likely has no motive or

178. Estelle Sommeiller & Mark Price, *The New Gilded Age*, ECON. POL'Y INST. (July 19, 2018), <https://www.epi.org/publication/the-new-gilded-age-income-inequality-in-the-u-s-by-state-metropolitan-area-and-county> [<https://perma.cc/5WC9-XYQH>] (describing report findings that since the 1970s, income inequality has risen in every U.S. state); see also David Huyssen, *We Won't Get out of the Second Gilded Age the Way We Got out of the First*, VOX (Apr. 1, 2019), <https://www.vox.com/first-person/2019/4/1/18286084/gilded-age-income-inequality-robber-baron> [<https://perma.cc/J2HF-AEYA>].

179. Sommeiller & Price, *supra* note 178; see also Huyssen, *supra* note 178.

180. Zia Qureshi, *Tackling the Inequality Pandemic: Is There a Cure?*, BROOKINGS INST. (Nov. 17, 2020), <https://www.brookings.edu/research/tackling-the-inequality-pandemic-is-there-a-cure> [<https://perma.cc/ET35-NNSF>].

181. See, e.g., Brea L. Perry, Brian Aronson & Bernice A. Pescosolido, *Pandemic Precarity: COVID-19 Is Exposing and Exacerbating Inequalities in the American Heartland*, PNAS, Feb 23, 2021, at 3–4 (arguing that the pandemic disproportionately affected historically disadvantaged groups and contributed to widening inequality indices).

182. Heather Long, Andrew Van Dam, Alyssa Fowers & Leslie Shapiro, *The Covid-19 Recession Is the Most Unequal in Modern U.S. History*, WASH. POST (Sept. 30, 2020), <https://www.washingtonpost.com/graphics/2020/business/coronavirus-recession-equality> [<https://perma.cc/J67X-AB74>].

183. See Collins et al., *supra* note 11, at 3 (discussing how the average DAF donor has an income of over \$1 million per year).

184. *Giving Vehicle Comparison*, *supra* note 18.

185. See Adrian D. Garcia, *This Is the Average Amount in Savings Accounts—How*

ability to set up a private foundation. And DAFs, which often tout themselves as the everyman's answer to private foundations, still have monetary barriers to entry.<sup>186</sup> While Fidelity Charitable recently lowered its required initial contribution to zero dollars<sup>187</sup> (a laudable move by an organization that touts its mission to bring long-term philanthropic grantmaking to all individuals), other NSOs require a \$25,000 initial contribution.<sup>188</sup> Even community foundations sometimes require substantial initial contributions in the thousands of dollars.<sup>189</sup>

It is within this landscape that the private foundation-to-DAF issue stands in sharpest relief. Charitable dollars held in DAF accounts delays the benefit to working charities,<sup>190</sup> many of which urgently needed funds in 2020 given the COVID-19 pandemic.<sup>191</sup> Some community foundations responded to the pandemic by urging its donors to give at least five percent of their DAF assets to aid in the pandemic response.<sup>192</sup> But such requests were just that: an *ask* to donate more, rather than a directive.

Much has been written about the normative rationales underlying wealth taxes or other taxes aimed at redistributing

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*Does Your Cash Stack Up?*, BANKRATE (Dec. 3, 2018), <https://www.bankrate.com/personal-finance/savings-account-average-balance> [<https://perma.cc/L2L7-223N>] (reporting that Federal Reserve data reveals that the average American household has \$8,863 in a savings account).

186. See, e.g., *Giving Vehicle Comparison*, *supra* note 18.

187. Daniels, *supra* note 96.

188. *Giving Tools*, *supra* note 97.

189. See, e.g., *Types of Funds*, SILICON VALLEY CMTY. FOUND., <https://www.siliconvalleycf.org/types-of-funds> [<https://perma.cc/TXU7-DU8M>] (noting that the Silicon Valley Community Foundation requires an initial contribution of \$5,000).

190. See discussion *supra* Part II.B.

191. See, e.g., Tim Marx, *COVID-19: Update and We Need Your Help*, CATH. CHARITIES ST. PAUL & MINNEAPOLIS, <https://www.cctwincities.org/covid-19-update-and-we-need-your-help> [<https://perma.cc/KX9H-KLJA>].

192. Theodore Schleifer, *Silicon Valley's Favorite Charity Is Asking Its Donors to Give Away Hundreds of Millions of Dollars. Right Now.*, VOX: RECODE (Apr. 20, 2020), <https://www.vox.com/recode/2020/4/20/21221613/silicon-valley-community-foundation-coronavirus-billionaires-donor-advised-funds> [<https://perma.cc/WDM5-CYSQ>] (describing how the head of the Silicon Valley Community Foundation urged donors to give funds to aid in the local pandemic response). But Fidelity Charitable reported an 18% increase in DAF disbursements in May 2020 when compared to the prior year, suggesting that some DAF accounts heeded the call. *Fidelity Charitable Donors Recommend Over \$236 Million in Grants to Nonprofits for COVID-19 Relief; Just Part of the \$2.5 Billion Granted so far This Year*, FID. CHARITABLE (May 6, 2020), <https://www.fidelitycharitable.org/about-us/news/fidelity-charitable-donors-recommend-over-200-million-in-grants-to-nonprofits-for-covid-19-relief.html> [<https://perma.cc/462W-5EYC>].

wealth—namely, a desire to prevent wealth concentration (which may hinder democracy) and combating dynastic wealth.<sup>193</sup> The aging baby boomer population and the imminent intergenerational transfer of wealth amplifies these concerns.<sup>194</sup> In the early 2000s, baby boomers were estimated to leave estates worth \$12–18 trillion, some of which will be donated to charitable organizations.<sup>195</sup> Given the aforementioned concerns about rising wealth inequality and the ongoing intergenerational transfer of wealth from baby boomers to their successors and gift recipients, reform—if it is undertaken—must occur soon.

## 2. Growing Backlash Against a Decline in Philanthropic Transparency

Beyond concerns about wealth inequality, skepticism towards private foundations and DAFs fits neatly into the contemporary debate over the First Amendment and campaign finance reform. Private foundations' use of DAFs to obfuscate identity when making charitable gifts bears substantial similarities to the growing use of so-called “dark money” in politics and campaign finance.<sup>196</sup> Since the Supreme Court's decision in *Citizens United v. FEC*,<sup>197</sup> calls to promote transparency in campaign finance and government have remained legion.<sup>198</sup> A recent federal district court decision, *Bullock v. IRS*, brought these conversations into the nonprofit sphere.<sup>199</sup> The decision briefly invalidated a new IRS rule that allowed certain exempt organizations, including 501(c)(4) social welfare groups and 501(c)(6) trade or business association groups, to avoid disclosing their donors' identities.<sup>200</sup> The rule encountered immediate

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193. See, e.g., Miranda Perry Fleischer, *Not So Fast: The Hidden Difficulties of Taxing Wealth*, 58 NOMOS: AM. SOC'Y POL. LEGAL PHIL. 261, 270–72 (2017) (discussing common normative rationales reasons for taxing the wealthy).

194. Marsh, *supra* note 43, at 165 (“Since the greatest inter-generational transfer of wealth in American history is likely to occur in the next twenty years, the effects of the outdated provisions of the [Tax] Code have immediate importance.”).

195. *Id.*

196. See JANE MAYER, DARK MONEY (2016) (analyzing the rise in use of “dark money”).

197. 558 U.S. 310 (2010).

198. See, e.g., Sheldon Whitehouse, *Dark Money and U.S. Courts: Problems and Solutions*, 57 HARV. J. LEGIS. 273, 291–300 (2020).

199. *Bullock v. IRS*, 401 F. Supp. 3d 1144, 1158 (D. Mont. 2018).

200. *Id.*; see Rev. Proc. 2018-38; 2018-31 I.R.B. 280. Before this rule, the IRS required that these groups list their donors on their IRS returns. While such information was only made available to the IRS—not to the public—it still maintained some level of accountability and transparency. See Miriam Galston,

controversy, as it limited the IRS's ability to properly oversee certain activities, such as election funding.<sup>201</sup> The court in *Bullock* ultimately invalidated the IRS action because it failed to follow notice and comment procedures of the Administrative Procedure Act ("APA"),<sup>202</sup> and the IRS subsequently reinstated the rule after complying with the proper procedures.<sup>203</sup>

As new regulations chip away at nonprofit disclosure requirements, the importance of maintaining transparency should be kept front-of-mind. Transparency plays a crucial role in ensuring public confidence in philanthropy. Declines in public confidence can lead to downturns in philanthropic giving.<sup>204</sup> Hits to public trust can also affect non-monetary actions, like volunteerism.<sup>205</sup> As contemporary criticisms of private foundation and DAF donations continue to proliferate, special concern should be paid to the importance of maintaining public trust, as failure to do so can result in negative consequences across the philanthropy sphere.<sup>206</sup>

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Private foundation-to-DAF grantmaking facially satisfies IRS requirements but chafes against the spirit of public benefit and disclosure that militated the private foundation regulations in the first place. As private foundation-to-DAF grantmaking becomes more common, private foundations' ability to meet IRS regulations through granting money to a DAF—where it could live in

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*Buckley 2.0: Would the Buckley Court Overturn Citizens United?*, 22 U. PA. J. CONST. L. 687, 701 (2020) (describing the aftermath of the *Bullock* decision).

201. See Press Release, David E. Price, Rep., U.S. House of Representatives, Rep. Price Introduces Legislation to Overturn Controversial "Dark Money" Rule (Dec. 13, 2018), <https://price.house.gov/newsroom/press-releases/rep-price-introduces-legislation-overturn-controversial-dark-money-rule> [<https://perma.cc/GBC2-FGPC>]; see also Galston, *supra* note 200, at 701–02 ("[T]he new IRS policy will also prevent the IRS from easily determining contributions to . . . entities by corporations, LLCs, and other business entities or by labor unions and similar organizations.").

202. *Bullock*, 401 F. Supp. 3d at 1158–59.

203. Guidance Under Section 6033 Regarding the Reporting Requirements of Exempt Organizations, 85 Fed. Reg. 31,959 (May 28, 2020) (to be codified at 26 C.F.R. pt. 1, 56).

204. Paul C. Light, *How Americans View Charities: A Report on Charitable Confidence*, BROOKINGS INST. 1 (2008), [https://www.brookings.edu/wp-content/uploads/2016/06/04\\_nonprofits\\_light.pdf](https://www.brookings.edu/wp-content/uploads/2016/06/04_nonprofits_light.pdf) [<https://perma.cc/JH58-9Y33>] (describing how the American Red Cross's post-9/11 scandals led to a downturn in giving).

205. *Id.*

206. *Id.* at 5–8.



perpetuity—instead of granting it to a working charitable organization bears the potential to upend the philanthropy industry. Such opportunistic grantmaking also threatens to undermine public trust in private foundations and DAFs, as is evidenced through the growing body of criticism levied against DAF sponsors. To restore confidence in private foundations and ensure that the bargain between private foundations and the public interest is met, Congress and state governments should consider enacting a regulatory scheme that promotes oversight and limits private foundation-to-DAF grantmaking.

### III. REGULATORY REFORM AT THE FEDERAL AND STATE LEVELS

Charities (including DAFs) and private foundations are regulated through a complex and overlapping scheme of federal and state law.<sup>207</sup> The IRS maintains oversight on all federal tax-related matters, but the state attorneys general or secretaries of state (depending on the jurisdiction) often manage the quotidian aspects of charities regulation.<sup>208</sup> A workable regime to inject accountability and oversight into private foundation-to-DAF grantmaking should function within this federalist scheme.

This Part proposes complementary federal and state-level regulatory approaches to addressing the oversight gaps created by private foundation-to-DAF grantmaking, responds to potential criticism of these approaches, and demonstrates why further regulatory oversight is necessary to instill public trust in modern philanthropic tools like DAFs. First, this Part delves into a narrow federal solution that would address the wealth warehousing concerns of private foundation-to-DAF grantmaking: a ban by the IRS on using DAF donations as a way to meet the five percent payout requirement. Federal efforts to reform DAFs have failed in the past, and any successful approach would likely need to be narrowly tailored to address the harm. Next, this Part proposes reforms at the state level that would lead to greater transparency: statutory

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207. See, e.g., Lloyd Hitoshi Mayer & Brendan M. Wilson, *Regulating Charities in the Twenty-First Century: An Institutional Choice Analysis*, 85 CHI.-KENT L. REV. 479, 486–89 (2010).

208. *Id.* at 493 (noting that Congress and the IRS's inroads into charities regulation is a relatively recent development, as most charities regulation duties flow from state-level common law). See generally Cindy M. Lott, Marcus Gaddy, Elizabeth T. Boris, Maura Farrell, Karin Kunstler Goldman & Belinda J. Johns, *State Regulation and Enforcement in the Charitable Sector*, URB. INST. 10–13 (2016), <https://www.urban.org/sites/default/files/publication/84161/2000925-State-Regulation-and-Enforcement-in-the-Charitable-Sector.pdf> [<https://perma.cc/8RJB-CXNV>].

amendments to expand state attorney general or secretary of state oversight into private foundations' DAF grantmaking. This Note, while the first to propose a dual-pronged approach, builds upon existing efforts to regulate DAFs. Ultimately, it argues that the private foundation-to-DAF issue—precisely because it violates the spirit of the 1969 Act's reform efforts—is ripe for regulation.

A. A NARROWLY TAILORED FEDERAL SOLUTION

Demands for the Treasury Department, the IRS, and Congress to consider regulating DAFs began in earnest in the 2000s, sparked by the massive growth in DAF accounts after NSOs gained public charity status.<sup>209</sup> Many DAF reformers are calling for a payout floor—similar to private foundations' five percent annual payout requirement—to be imposed across *all* DAF accounts, regardless of the original donors' identity.<sup>210</sup> But DAF proponents argue that because DAF sponsors report higher payout percentages than the five percent minimum, applying a DAF payout requirement would serve little purpose.<sup>211</sup> However, there is little useful data to corroborate either side of the debate, as no disaggregated account-level data on payouts exists. DAF sponsors are only required to report payout levels averaged across *all* accounts.<sup>212</sup> The DAF providers report payout rates at about twenty percent, but this has fallen in recent years.<sup>213</sup>

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209. For example, the Bush Administration's Fiscal Year 2001 budget contained a proposal to "Clarify Public Charity Status of Donor Advised Funds" and urged legislative action regarding DAFs. The Senate Finance Committee held hearings in 2004 and released a white paper containing reform proposals. *See Report to Congress on Supporting Organizations and Donor Advised Funds*, DEP'T TREASURY 22–23 (2011), <https://www.treasury.gov/resource-center/tax-policy/Documents/Report-Donor-Advised-Funds-2011.pdf> [<https://perma.cc/Z2GK-GERD>] (describing recent reform efforts focused on DAFs).

210. *See* Colinvaux, *supra* note 3, at 48–49 (noting that multiple recent congressional proposals to require an annual five percent payout on DAFs' aggregate funds failed); Brunson, *supra* note 28, at 256–58; *cf.* Ray D. Madoff, *5 Myths About Payout Rules for Donor-Advised Funds*, CHRON. PHILANTHROPY (Jan. 13, 2014), <https://www.philanthropy.com/article/5-Myths-About-Payout-Rulesfor/153809> (last visited Nov. 20, 2021) ("Advised funds do not need payout rules because they already give a higher percentage of their assets than private foundations.").

211. John F. Coverdale, *Legislating in the Dark: How Congress Regulates Tax-Exempt Organizations in Ignorance*, 44 U. RICH. L. REV. 809, 829 (2010) ("It is far from clear that there is any need for a mandatory aggregate payout requirement . . . . The median payout rate for donor-advised funds . . . was 17.5% . . . [while] [p]ayout rates for private foundations hover near the legally mandated five percent . . .").

212. The Pension Protection Act of 2006 requires that DAF account sponsors report their aggregate assets, grants, and contributions; therefore, DAF sponsors—even those as large as Fidelity Charitable—are only required to report the aggregate

Despite vociferous advocacy from reformers regarding the overall DAF payout rate, the history of federal regulation concerning DAFs indicates a preference for incremental change.<sup>214</sup> The most substantial regulations concerning DAFs addressed issues of donor control, clarified that distributions from DAFs must be directed to another public charity, and required the Treasury Department to author a report on potential reforms for DAF payout requirements and charitable deductions.<sup>215</sup> More substantial reforms, such as Representative Dave Camp's 2014 proposal for a five percent payout requirement across all DAFs, have failed to garner Congressional support.<sup>216</sup> Critics of Representative Camp's effort questioned why minimum payouts should be required when DAF sponsors regularly cite payout rates well-above private foundations' five percent minimum.<sup>217</sup>

Prior reform efforts point in one direction—crafting a solution that is narrowly tailored to address the problem. To address the specific private foundation-to-DAF problem, pursuing DAF reform writ large would pose a challenge. DAF reformers suffer from a data crisis; because payout rates are only reported in the aggregate,<sup>218</sup> it is impossible to point to specific bad actors (i.e., individual funds) that languish and gather dust. Further, broad DAF reform—as evidenced by Representative Camp's failed proposal—has struggled to gain federal traction.<sup>219</sup> A narrowly-tailored solution might garner more support.

The Treasury Department and the IRS should propose a regulation to ban private foundations from using donations to DAFs to fulfill their annual five percent payout requirement.<sup>220</sup> In fact, the

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payout rate across *all of their accounts*. See Pension Protection Act, Pub. L. No. 109-280, §§ 1224–1225, 120 Stat. 780, 1091–94 (2006).

213. Across the major NSOs, the DAF payout rate is dropping—between 2008 and 2014, Fidelity's payout rate fell from 21 to 16% and Vanguard's fell from 18 to 11%. Some also suggest that the DAF payout rates are misleading, as DAF payout rates likely vary across accounts (with some accounts granting a majority of their funds in a given year, and some likely granting nothing). *A Philanthropic Boom, "Donor-Advised Funds"*, *supra* note 98.

214. See Colinvaux, *supra* note 3, at 48–50.

215. Pension Protection Act § 1226; see also *Report to Congress on Supporting Organizations and Donor Advised Funds*, *supra* note 209.

216. See Tax Reform Act of 2014, H.R. 1, 113th Cong. (2014).

217. Bjorklund, *supra* note 119, at 70.

218. See discussion *supra* notes 212–13.

219. See discussion *supra* note 217.

220. While others have suggested this particular reform, this Note is the first to discuss it at length. See James J. Fishman, *The Private Foundation Rules at Fifty: How*

IRS has already solicited comments on a similar issue, asking for feedback on whether private foundation-to-DAF transfers should be treated as “qualifying distributions” in certain circumstances.<sup>221</sup> The IRS should go a step further and propose that DAFs, regardless of circumstance, be removed from its list of qualifying distributions.<sup>222</sup> A narrow ban on such grantmaking serves several purposes. It directly addresses the payout-related harms engendered through the current practice—the substitution of DAFs for working charities—and would ensure that more working charities receive annual donations from private foundations. This narrow change also has a built-in argument in its favor: it is simply requiring that private foundations more fully comply with the spirit of the 1969 Act. Congress, after all, already *passed* legislation to ensure that five percent of private foundations’ funds would be redistributed to serve the public good. The Congress in 1969 could not have foreseen the rise and opportunity presented by DAFs, and this regulation creates a return to the status quo.

Because it would not be imposing any extra regulations on private foundations, it would likely be more politically feasible than more substantial regulations geared towards DAFs.<sup>223</sup> Even some members of the private foundation community acknowledged that, in some instances, foundation-to-DAF grants breach the public trust and should be prohibited.<sup>224</sup> A prohibition on putting DAF grantmaking towards their annual payout requirement only

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*Did We Get Them and Do They Meet Current Needs?*, 17 PITT. TAX REV. 247, 295 (2020) (noting, briefly, how private foundations should be disallowed from donating to DAFs).

221. I.R.S. Notice 2017-73 14 (2017). In its request for comments, the IRS noted that private foundation-to-DAF transfers could still 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.” *Id.*

222. *Qualifying Distributions—In General*, IRS (Sept. 23, 2021), <https://www.irs.gov/charities-non-profits/private-foundations/qualifying-distributions-in-general> [<https://perma.cc/ML73-CG34>].

223. *But see* Fishman, *supra* note 220 (“DAFs are often essentially checking accounts. Assets entering a DAF should be distributed within five years. The rules relating to contributions of non-cash appreciated assets need to be tightened and overseen more closely by the IRS. This may mean lengthening the period before the full deduction benefits are granted to the donor.”).

224. Olsen-Phillips, *supra* note 138 (“Comments from the Community Foundation Public Awareness Initiative also generally opposed tighter rules, although it added that if a foundation were making grants to a donor-advised fund and those funds then sat ‘dormant,’ that would be ‘an abuse of the public trust and a loophole that should be closed.’” (citation omitted)).

disincentivizes DAF grantmaking that aimed to help foundations *meet* this requirement—rather than grantmaking going towards DAFs for other reasons.<sup>225</sup>

Further, this narrow change builds in compromise and reflects the considerations of private foundations. There are several valid reasons why private foundations might wish to utilize DAFs, such as when smaller foundations wind down their efforts, endeavor to give thoughtfully, or when militated by safety concerns.<sup>226</sup> For example, Professor Daniel Hemel argues that delaying payouts to charities is not necessarily a net-negative: “[I]f the alternative is that you rush your decision and give this year to a charity that might not make the best use of the funds, then DAFs don’t seem so terrible from a public policy perspective.”<sup>227</sup> By only regulating a small subset of private foundation-to-DAF regulations, this solution threads the needle between mitigating wealth warehousing concerns and allowing flexibility for private foundations.

This change will require greater IRS oversight of private foundations. This may present challenges for the agency, which—as noted by Professor James Fishman—“has been under siege by certain elements of Congress, its budget cuts, and its resources incapable of the necessary scrutiny of the nonprofit sector.”<sup>228</sup> Concrete data on the agency’s oversight limitations is scarce, but

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225. Such regulation may also help to legitimize DAFs. As previously discussed, several scholars argue that the regulations created by the 1969 Act played a role in legitimizing private foundations and shoring up public trust. This legitimization is largely proved by omission, as private foundations have largely avoided the same kind of congressional backlash that they received in the leadup to the 1969 Act. *See* Fishman, *supra* note 220, at 283; Hackney, *supra* note 29.

226. Debi Ghatge, *The Philanthropy Roundtable Urges Congress NOT to Force More Giving from Donor-Advised Funds and Foundations*, PHILANTHROPY ROUNDTABLE (Oct. 5, 2020), <https://www.philanthropyroundtable.org/home/blog/post/roundtable/2020/10/05/the-philanthropy-roundtable-urges-congress-not-to-force-more-giving-from-donor-advised-funds-and-foundations> [<https://perma.cc/Y4XG-7XFW>] (“DAFs also protect the safety of private foundation staff, family members, and grantees who are targets of violence here and abroad. For example, we know of an East Coast family foundation that gives to a DAF to support anti-terrorist organizations, some of which have had fatwas issued against them. Giving through a DAF protects this family foundation from that violence.”).

227. Carl D. Holborn & Britany E. Morrison, *Can Private Foundations Make ‘Qualifying Distributions’ to Donor-Advised Funds?*, 31 TAX’N EXEMPTS 3, 7 (2019).

228. Fishman, *supra* note 220, at 280. Some have even suggested decoupling oversight of exempt organizations (including 501(c)(3) charities, like DAFs, and private foundations) from the IRS altogether. *See, e.g.*, Lloyd Hitoshi Mayer, *The Better Part of Valour Is Discretion’: Should the IRS Change or Surrender Its Oversight of Tax-Exempt Organizations?*, 7 COLUM. J. TAX. L. 80, 115–17 (2016).

some scholars suggest that exempt organizations' noncompliance "may be relatively widespread."<sup>229</sup> Reform to the IRS's oversight of private foundations must take the agency's limitations into account; the narrow proposal suggested above likely would not substantially impact the day-to-day operations to the IRS.

This federal reform is crafted to address payout challenge posed by private foundations' use of DAFs. The next Section proposes a solution to address the other harm created by private foundation-to-DAF grantmaking—avoidance of the disclosure requirements.

#### B. EMPOWERING STATE ATTORNEYS GENERAL WITH GREATER OVERSIGHT

While the IRS oversees tax reporting activity for both charities and private foundations, the day-to-day aspects of philanthropy regulation often occurs at the state level. Individual states' oversight of charities and private foundations varies wildly,<sup>230</sup> but at a basic level, each state attorney general is empowered with the *parens patriae* duty to enforce the public interest.<sup>231</sup> This plays an important role in preserving accountability. In order to address the transparency concerns created by private foundation donations to DAFs, state attorneys general should play a greater role in preserving public (or, at the very least, governmental) accountability over which charities receive private foundations' funds.

State attorneys general are endowed with substantial common-law powers over charities.<sup>232</sup> These offices wear many charities-regulating hats, including "educating fiduciaries and staff[] in meeting their legal obligations and improving charity governance, . . . [and] rectifying self-dealing and other breaches of fiduciary duty by charity insiders."<sup>233</sup> But despite these broad powers, state attorneys general and their charities divisions face challenges in fulfilling the

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229. Mayer, *supra* note 228, at 95.

230. Lott et al., *supra* note 208, at 8.

231. Evelyn Brody, *Whose Public? Parochialism and Paternalism in State Charity Law Enforcement*, 79 IND. L.J. 937, 943 (2004). State attorneys general possess broad *parens patriae* (literally, the "parent of the country") powers to sue entities and recover damages relating to behavior that threatens the state or its citizens. See Richard P. Ieyoub & Theodore Eisenberg, *State Attorney General Actions, the Tobacco Litigation, and the Doctrine of Parens Patriae*, 74 TUL. L. REV. 1859, 1863-64 (2000).

232. Some have even described state attorneys general powers in this arena as "unfettered." See Ellen P. Aprill, *What Critiques of Sarbanes-Oxley Can Teach Us About Regulation of Nonprofit Governance*, 76 FORDHAM L. REV. 765, 785 n.167 (2007).

233. Brody, *supra* note 231, at 947.

extent of their oversight capabilities—namely, staffing shortages and perennial underfunding via state legislatures.<sup>234</sup>

To foster greater oversight of private foundation-to-DAF grantmaking, state legislatures should grant state attorneys general the authority to inspect private foundations' annual DAF donation reports. Such an enactment bears similarities to the IRS oversight originally granted by the 1969 Act, which opened private foundations' yearly grantmaking activity to the IRS.<sup>235</sup> It cracks open the black box between the private foundation's grant to a DAF and the eventual disbursement. Further, it provides state attorneys general—who carry broad enforcement authorities—the ability to pinpoint and investigate any misuse of charitable funds.

Allowing state attorneys general the authority to inspect these sheets would not pose a substantial administrative burden for DAF sponsors or private foundations. Private foundations that operate DAF accounts have easy administrative access to such information via their chosen DAF sponsors. In a series of interviews the Minnesota Council of Nonprofits conducted with the five largest NSOs, they confirmed the availability of easily accessible annual grantmaking documentation from a DAF donor's account.<sup>236</sup> State legislation requiring that private foundations file the list of annual grantmaking from their DAF accounts with state attorneys general would impose a minimal burden on both the private foundation and the DAF sponsor, as it requires no additional forms to fill out and only asks that the foundations file readily-available information. Further, the amount of unaccounted for charitable money involved—in the billions—outweighs any potential the administrative costs. Ensuring that the public benefits from private foundation giving—as was intended by the 1969 Act—outweighs the administrative inconvenience engendered through additional state attorney general oversight.

With statutory expansion of their monitoring capabilities, states are better candidates for oversight than the IRS. As previously noted, while the IRS controls federal tax reporting for both private foundations and charities, the agency continually experiences resource shortages and budget cuts.<sup>237</sup> The Exempt Organization

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234. Aprill, *supra* note 232, at 786.

235. The Tax Reform Act of 1969, Pub. L. No. 91-172, § 101(e)(3), 83 Stat. 487, 521-24 (1969) (adding I.R.C. § 6104(d) and requiring private foundations make annual reports available for inspection).

236. Aanestad et al., *supra* note 23, at 10.

237. See Fishman, *supra* note 220, at 280; see also Paul Kiel & Jesse Eisinger, *How*

division, which oversees private foundations and DAFs, perennially feels the brunt of these burdens.<sup>238</sup> IRS involvement is necessary to amend the organizations eligible for qualifying distributions under I.R.C. § 4942, but leaving day-to-day oversight to the short-staffed agency would likely result in little meaningful oversight.<sup>239</sup>

Further, some states have already taken charge on meaningful DAF regulation.<sup>240</sup> As previously mentioned, a 2019 bill in California attempted to shed light on DAF transparency issues. The legislation would have required that California-based DAFs report individual funds' asset size and annual grantmaking.<sup>241</sup> This legislation would not have addressed the donor anonymity issue posed by private foundation-to-DAF donations, but it would have shed light on fund-level payout rates.<sup>242</sup> Despite support from CalNonprofits, the bill received substantial pushback from NSOs and community foundations and eventually stalled in the California legislature.<sup>243</sup> Although the California legislation failed to pass this legislation, it signaled an openness and desire for state legislators to tackle the DAF issue.

#### CONCLUSION

The growing popularity of DAFs—and their lack of regulation and public oversight—presents a troubling opportunity for private foundations to subvert the 1969 Act's goals, which put in place

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*the IRS Was Guttled*, PROPUBLICA (Dec. 11, 2018), <https://www.propublica.org/article/how-the-irs-was-guttled> [<https://perma.cc/NKP4-RCNS>].

238. Kiel & Eisinger, *supra* note 237.

239. Cf. Marion R. Fremont-Smith, *The Search for Greater Accountability of Nonprofit Organizations: Recent Legal Developments and Proposals for Change*, 76 *FORDHAM L. REV.* 609, 609 (2007) (“[S]ome scholars are suggesting that all regulation be removed from the IRS or that some of its powers be transferred to an agency more suited to regulate tax-exempt entities, as the IRS’s principal focus is tax collection.”).

240. A potential criticism of the state-led approach is the patchwork nature of state charities regulation. Some states, like California, employ nearly seventy full-time attorneys in their charities divisions; in other states, an assistant attorney general assigned to the charities division may split their time with the consumer protection division. Lott et al., *supra* note 208, at 8. But this approach also places the onus on states who *do* desire to pass DAF-focused legislation, rather than waiting for the IRS to consider the issue. Further, active state charities regulation tends to be focused around certain states; private foundations tend to have active footprints across these states—which include California, New York, and Connecticut. See Aprill, *supra* note 232, at 786. This solution takes an incremental approach, rather than a full-throated IRS overhaul, that may be more politically feasible in the short-term.

241. Cantor, *supra* note 121.

242. *Id.*

243. *Id.*



minimum standards for disbursement of charitable funds and public (as well as governmental) accountability. While the available evidence suggests that the number of private foundations that take advantage of DAFs' favorable regulatory structure remains small, this number seems to be growing—and the amount of philanthropic dollars involved is considerable. In the face of growing wealth inequality, more private foundations appear to be taking advantage of DAFs to fulfill the IRS's five percent annual payout requirement, which allows private foundations' wealth to remain warehoused indefinitely. Further, charitable giving through DAFs allows private foundations to avoid public scrutiny, which prevents public oversight. Private foundations receive substantial tax benefits for their philanthropic mission, and by increasingly utilizing DAFs, they are failing to abide by the spirit of the rules put in place to prevent misuse and benefit the public.

This Note names the harms created by private foundation-to-DAF grantmaking—including billions in delayed payouts to working charities and a disturbing decline in philanthropic transparency—and advocates for a new regulatory regime to address the private foundation-to-DAF problem. It proposes two remedies: one directed towards the Treasury and the IRS, and one directed towards state attorneys general. This dual-pronged proposal acknowledges the federalist system that oversees charities regulation and provides multiple opportunities for increased accountability. Ultimately, this solution puts forth narrowly tailored, incremental proposals to reinvigorate the spirit of the 1969 Act and to prevent private foundations from abusing DAFs as a loophole to avoid annual payout requirements and governmental scrutiny. Further, reform can play a crucial role in building public trust in private foundations and potentially in legitimizing DAFs. By imposing oversight and regulatory standards on private foundation-to-DAF transfers, the federal government and states can reinstate philanthropic legitimacy in such activity and promote public trust.