Global Center for Excellence in Philanthropy

President's Fiscal Year 2025 Budget would add restrictions to what payments are qualifying distributions for Private Foundations with annual payout requirements.

On March 11, 2024, the Treasury Department released the General Explanations of the Administration's Fiscal Year 2025 Revenue Proposals ("Green Book"), which provides the Treasury Department's explanations of the revenue provisions in the President's budget blueprint proposal ("budget blueprint"). The budget blueprint renews proposals from last year that would limit the use of donor advised funds (DAFs) to avoid a private foundation payout and a new provision that would exclude payments to most disqualified persons from counting toward the private foundation payout requirement.

Distributions to DAFs

Currently, DAFs are not required to distribute amounts held within a particular period while private non-operating foundations are annually required to distribute at least 5 percent of the average fair market value (with some modifications) of their non-charitable use assets determined for the preceding taxable year. This 5 percent distribution amount for private foundations must consist solely of qualifying distributions.

Private foundations that are donors to DAFs or persons appointed or designated by the private foundations as donor-advisors have continuing advisory privileges with respect to the DAFs. These privileges could provide a private foundation with the continued ability to direct amounts that have been used to satisfy its requirement to distribute the amounts outside of its control. The Green Book calls this result "not appropriate" and states "(t)his use of DAFs can subvert the goal behind requiring minimum distributions, by reducing the current charitable use of the associated funds."

The proposal clarifies that a distribution to a DAF can only be counted as a qualifying distribution if the distributed funds are spent by the DAF as a qualifying distribution by the end of the taxable year following receipt and the private foundation maintains adequate records showing that the DAF made the qualifying distribution within the required time frame. So, a private foundation could treat its DAF distribution as a qualifying distribution to find out later that it doesn't qualify because the DAF didn't redistribute it in time (or at all). The budget blueprint appears to reflect the belief that as a DAF donor, the private foundation's advisory privileges can and will direct the DAF's timely redistribution of amounts the private foundation has already treated as a qualifying distribution.

Such a provision would bring private foundation distributions to DAFs in line with private foundation distributions to other private non-operating foundations or certain charitable organizations (tax-exempt pursuant to Internal Revenue Code section 501(c)(3)) that the private foundation controls. While the consequences in this case are not clear, it stands to reason that a failed redistribution by the DAF will be treated the same as a failed redistribution by other private nonoperating foundations or controlled charitable organizations.

In those cases, should the donee or recipient of the distribution not redistribute all the funds by the close of the year the distribution was received, the private foundation would increase its required minimum distribution for this un-redistributed amount for the year beginning after the close of the donee organization's tax year during which the amount should have been redistributed.

Payments to most disqualified persons

Qualifying distributions can include reasonable and necessary administrative expenses paid by the foundation to further its charitable purposes. Such administrative expenses can include compensation to, or reimbursement of expenses incurred by, disqualified persons when the compensation or expense reimbursement doesn't constitute a prohibited act of self-dealing under Internal Revenue Code section 4941. The Green Book states that some private foundations meet their entire distribution requirement by hiring family members. It further states that "(a)llowing payments to disqualified persons to count towards a private foundation's payout requirement does not meet this intent to directly further charitable purposes."

Under the proposal, "paying compensation or reimbursing expenses by a private foundation to a disqualified person (other than a foundation manager of such a private foundation who is not a member of the family of any substantial contributor) is not a qualifying distribution that satisfies the payout requirement." These payments could still be made, again, assuming that they are not prohibited self-dealing, but they wouldn't be included as qualifying distributions towards the required payout.

It is important to note that the Green Book is not proposed or actual legislation, and it is uncertain at this time how likely it is that any of the specific provisions may be enacted, especially give the disparate tax legislative agendas of Democrats and Republicans in Congress. Deloitte summarized the other provisions of the Green Book: *"Biden doubles down on corporate, high-wealth tax increases in FY 2025 budget blueprint".*