February 8, 2024

Via Federal eRulemaking Portal at: https://www.regulations.gov

Internal Revenue Service
1111 Constitution Avenue, NW
Washington, D.C. 20224
Attention: Mr. Christopher A. Hyde, Office of Associate Chief Counsel
(Employee Benefits, Exempt Organizations, and Employment Taxes)

Re: SIFMA Comment on Internal Revenue Service Proposed Rule re:
Taxes on Taxable Distributions from Donor Advised Funds

Dear Mr. Hyde:

The Securities Industry and Financial Markets Association (“SIFMA”)1 appreciates the opportunity to comment on the Internal Revenue Service (“IRS”) proposed rule regarding Taxes on Taxable Distributions from Donor Advised Funds, REG-142338-07 (the “Proposal”).2 We respectfully submit the following comments for your consideration.

The Proposal provides guidance on the interpretation of key definitional terms used in the Pension Protection Act of 2006 (“PPA”),3 including what constitutes a “taxable distribution” from a donor advised fund (“DAF”). Under the PPA, a 20% excise tax is imposed on a sponsoring organization with respect to any taxable distribution paid from a DAF and a 5% excise tax is imposed on any fund manager that “knowingly agrees” to a taxable distribution.4

1 SIFMA is the leading trade association for broker-dealers, investment banks and asset managers operating in the U.S. and global capital markets. On behalf of our industry’s nearly 1 million employees, we advocate on legislation, regulation and business policy, affecting retail and institutional investors, equity and fixed-income markets and related products and services. We serve as an industry coordinating body to promote fair and orderly markets, informed regulatory compliance, and efficient market operations and resiliency. We also provide a forum for industry policy and professional development. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association. For more information, visit http://www.sifma.org.


The Proposal defines a “donor-advisor” as a person appointed or designated by a donor to have advisory privileges regarding the distribution or investment of assets held in a DAF. Under the Proposal, however, an investment advisor who provides investment management and advice with respect to both assets maintained in a DAF and the personal assets of a donor to that DAF (a “personal IA”) is also deemed to be a “donor-advisor” with respect to the DAF while serving in this dual capacity (regardless of whether the donor appointed, designated, or recommended the personal IA). Consequently, the payment of investment fees from DAF accounts which result in compensation to personal IAs who serve in this dual role would constitute a taxable distribution under Internal Revenue Code (“IRC”) §4966.5

SIFMA recommends that the IRS strike the Proposal’s new tax treatment of investment management fees paid from DAF accounts to personal IAs. In support of our recommendation, we respectfully submit the following legal, policy and practical points:

**Executive Summary**

1. The Proposal exceeds the IRS’s statutory authority.

2. The Proposal fails to provide underlying data or support and thus deprives the public of meaningful notice and opportunity to comment.

3. A personal IA does not meet the core definition of a donor-advisor, does not in fact act as a donor-advisor, and should not be treated as a donor-advisor under the Proposal.

4. A personal IA has two separate and distinct client/legal relationships: (1) the donor-client with respect to their personal assets, and (2) the sponsoring organization with respect to DAF assets, and owes each the legal obligation to disclose and manage potential conflicts of interest.

5. Professional management of DAFs should be encouraged and not punished with excise tax penalties.

6. The Proposal would benefit from additional revisions and clarifications (identified in the body of this letter).

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1. **The Proposal exceeds the IRS’s statutory authority.**

The Proposal seeks to amend tax regulations under IRC §4966 (Taxes on taxable distributions), including redefining the term “donor-advisor” to include a personal IA, who would then be subject to excise taxes on investment fees earned from DAF accounts. IRC

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5 Although the Proposal is limited to rulemaking under IRC §4966 (Taxes on taxable distributions), a personal IA who receives distributions from a DAF may also be subject to: (1) IRC §4958 (Taxes on excess benefit transactions) and/or (2) IRC §4967 (Taxes on prohibited benefits), both of which apply to a “donor-advisor” as defined in IRC §4966. See discussion in Section 1 infra.
§4966, however, *already* defines the term donor-advisor (within the definition of DAF) to mean:

“(any person appointed or designated by [a] donor)’ who “has, or reasonably expects to have, advisory privileges with respect to the distribution or investment of amounts held in such fund or account by reason of the donor’s status as a donor.”

The related IRC tax provisions rely upon this same statutory definition. IRC §4958 (Taxes on excess benefit transactions) cites to IRC §4966 for the definition of donor-advisor. IRC §4967 (Taxes on prohibited benefits), in turn, cites to IRC §4958 for the definition of donor-advisor. Thus, all roads lead back to the statutory definition of donor-advisor under IRC §4966. Moreover, the DAF-related statutory scheme reflects a clear congressional intent to distinguish between donor-advisors, on the one hand, and investment advisers, on the other hand.

Nothing in these statutory provisions suggests an express or implied delegation of authority to the IRS to define the term “donor-advisor” differently or more broadly than IRC §4966, as it has done in the Proposal. Nothing in the statute suggests congressional intent to delegate to the IRS authority to expand the universe of donor-advisors who are subject to IRC §4966’s excise taxes. If Congress had intended to delegate such authority, it would have done so. It did not.

The IRS is constrained by the statutory language of IRC §4966, including the definition of “donor-advisor.” The IRS is not free to alter or expand the definition of “donor-advisor” by regulation because the limitations of the statute prohibit it. All federal agencies, including the IRS, are bound by and subject to the limits of their grant of statutory authority. Accordingly, we recommend that the IRS’s expansion of the definition of donor-advisor to include personal IAs be stricken from the Proposal.

2. The Proposal fails to provide underlying data or support and thus deprives the public of meaningful notice and opportunity to comment.

The Proposal identifies the following four reasons/potential conflicts of interest for the new tax treatment of personal IAs (some of which allegedly inhibit DAF charitable distributions):  

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7 IRC §4958(f)(7).
8 IRC §4967(d).
9 See IRC §4958, Subsections (f)(1)(E) and (F), and (f)(7) and (8) (separately defining donor-advisors and investment advisers, and separately addressing their tax treatment in Subsections 4958(c)(1)(A) and (c)(2)(A)).
11 88 FR at 77926.
• The close relationship between the donor and his or her personal IA gives the donor influence over investment decisions with respect to assets held in the DAF (comparable to that of a donor-advisor);

• Personal IAs have an incentive to advise against distributions from the DAF to eligible charities because doing so would dilute the DAF’s assets under management (“AUM”) and thus, dilute the personal IA’s fees based upon the DAF’s AUM;

• Sponsoring organizations may allow appointment of a donor’s personal IA to act as an investment manager of DAF funds in order to incentivize investment advisers to encourage their clients to give to the firm’s DAF, rather than directly to a public charity; and

• A more than incidental benefit may occur if the personal IA charges donor-clients reduced fees to manage the donor’s personal assets because the personal IA also manages the assets that the donor contributed to the DAF.

The Proposal, however, provides no data or other empirical evidence to support any of these reasons/potential conflicts. Thus, the public is deprived of a meaningful opportunity to review and comment upon these stated reasons. If such data or evidence does exist, then the IRS should repropose and publish its data and evidence for public comment. If such data or evidence does not exist, then the IRS should set-aside the current Proposal and conduct further study to determine whether or not the assumptions that underpin its stated reasons are valid. In any event, we addresses below each of the IRS’s stated reasons in turn.

3. A personal IA does not meet the core definition of donor-advisor, does not in fact act as a donor-advisor, and should not be treated as a donor-advisor under the Proposal.

The Proposal defines the term “donor-advisor” in proposed regulation 26 CFR §53.4966-1(h) (Definitions – donor-advisor). With respect to personal IAs, the definition includes three relevant subparagraphs – (h)(1), (h)(2) and (h)(3).

(h)(1) In general.

Subparagraph (h)(1) defines a “donor-advisor” – consistent with the statutory definition discussed in Section 1 above – as a person appointed or designated or recommended by a donor to have advisory privileges regarding the distribution or investment of assets held in a DAF.

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12 See Portland Cement Assoc. v. Ruckelshaus, 486 F.2d 375, 393 (D.C. Cir. 1973), https://casetext.com/case/portland-cement-association-v-ruckelshaus (with respect to the standard for adequate notice, “[i]t is not consonant with the purpose of a rulemaking proceeding to promulgate rules on the basis of inadequate data, or on data that, to a critical degree, is known only to the agency.”).

First, a personal IA – by virtue of his or her role as an investment manager in the donor’s DAF – does not have *advisory privileges* regarding his or her donor-client’s DAF assets. Moreover, the donor does not have the ability to control, or unduly influence, his or her personal IA with respect to investment decisions about DAF assets, notwithstanding their relationship of trust and confidence with respect to the donor’s personal assets. The relationship between the personal IA and the donor-client with respect to personal assets does not create a relationship with respect to the donor-client’s DAF assets that, as the Proposal alleges, is “comparable to that of a donor-advisor.”

Second, a donor does not appoint or designate his or her personal IA to serve as an investment manager in the donor’s DAF. Rather, it is the sponsoring organization that owns and controls the DAF that appoints the personal IA as an investment manager of the DAF. The donor does not make, or take part in, the decision to appoint their personal IA as an investment manager of the DAF. This is true even if the donor recommends or suggests their personal IA for this role. The ultimate decision rests with the sponsoring organization.

Given that a personal IA has no advisory privileges regarding his or her donor-client’s DAF assets, and that a donor-client has no role in appointing his or her personal IA to serve as an investment manager in the donor’s DAF, a personal IA does not meet the core definition of a donor-advisor – as articulated in IRC §4966 – and incorporated in the proposed regulation under subparagraph (h)(1).

(h)(2) Person who establishes fund or account.

Subparagraph (h)(2) states that a “donor-advisor” also includes a “person … who establishes a fund or account and advises as to the distribution or investment of amounts in that fund or account…regardless of whether the person contributes to the fund or account.” This definition is overbroad.

In order for an investment adviser (“IA”) to “establish” a DAF account, the sponsoring organization must first decide and agree to establish the DAF account on its own system. The IA then separately establishes an investment advisory account on its own investment platform/system. These steps are wholly independent.

Subparagraph (h)(2) should be revised to clarify that an IA who merely assists clients in the application process, administrative set-up, and ministerial ongoing maintenance of a DAF account should not be thereby deemed a “donor-advisor” to the DAF. Likewise, an IA who thereafter provides only investment advisory services to the DAF should not be thereby deemed a “donor-advisor” to the DAF under subparagraph (h)(2).

Subparagraph (h)(2) should explicitly require that an IA retain *advisory privileges* with respect to distributions or investments of a donor’s assets in the fund in order to be deemed a donor-advisor. The definition in (h)(2) should draw a clear distinction between an IA who has *advisory privileges* (e.g., the ability to make grant recommendations to specific charities and in

14 88 FR at 77926. See discussion of a personal IA’s two separate and distinct legal obligations in Section 4 infra.
specific amounts, add successors to the DAF account, and add additional donor-advisers), on the one hand, versus an IA who merely provides investment advisory services to the DAF, on the other hand. As discussed above, these two functions are separate and distinct and the IRS should not conflate the two in a single definition.

(h)(3) Personal investment advisers.

Finally, subparagraph (h)(3) would treat a personal IA as a “donor-advisor” if he or she “manages the investment of, or provides an investment advice with respect to, both the assets maintained in a donor advised fund and the personal assets of the donor to that donor advised fund…regardless of whether the donor appointed, designated, or recommended the personal investment advisor.”15

As discussed below, a personal IA owes separate legal duties under the Investment Advisers Act of 1940 (the “Advisers Act”) to their donor-clients with respect to their personal assets, and to their sponsoring organizations with respect to DAF assets. The IRS should give deference to these long-established legal duties. As stated above, there is no reason to equate a “donor” who contributes assets to a DAF with the person who manages those assets. They are two entirely different legal statuses and roles and should not be treated the same.

For all the foregoing reasons, a personal IA does not meet the core definition of a donor-advisor, does not in fact act as a donor-advisor, and should not be treated as a donor-advisor under the Proposal. Accordingly, we recommend that the IRS strike subparagraphs(h)(2) and (h)(3) of proposed §53.4966-1(h).

4. A personal IA has two separate and distinct client/legal relationships: (1) the donor-client with respect to their personal assets, and (2) the sponsoring organization with respect to DAF assets, and owes each the legal obligation to disclose and manage potential conflicts of interest.

Under federal law, an investment adviser is a fiduciary.16 Under the Advisers Act, the fiduciary duty an investment adviser owes to his or her client comprises a duty of care and a duty of loyalty. The duty of care requires an investment adviser to provide investment advice in the best interest of his or her client, based on the client’s objectives. Under the duty of loyalty, an investment adviser must eliminate or make full and fair disclosure of all potential conflicts of interest which might incline an investment adviser – consciously or unconsciously – to render advice which is not disinterested such that a client can provide informed consent to the conflict.

An adviser’s fiduciary duty under the Advisers Act applies to all investment advice the investment adviser provides to clients, including advice about investment strategy, engaging a

15 The proposed regulation provides an exception for a personal IA who “is properly viewed as providing services to the sponsoring organization as a whole, rather than providing services to the donor advised fund.” See Section 6.a. infra for our recommendation that personal IAs who advise pooled assets in a DAF should satisfy this exception.

sub-adviser, and account type. In providing advice about account type, an adviser should consider all types of accounts offered by the adviser and acknowledge to a client when the account types the adviser offers are not in the client’s best interest.17

*The personal IA’s fiduciary duty to a donor-client.*

Thus, for example, if a personal IA advised his or her client to donate to a DAF which held its assets at the personal IA’s firm, rather than directly to a public charity, then that advice is legally required to be in the best interest of the client, and not place the interest of the personal IA above the interest of the client. Where the personal IA knows that he or she will be appointed by the DAF’s sponsoring organization to serve as an investment manager of the DAF – which represents a potential conflict of interest – then the personal IA would be required to disclose that fact to the client and obtain the client’s informed consent.

*The personal IA’s fiduciary duty to the sponsoring organization.*

In the role of investment manager of a DAF, a personal IA’s client is the DAF’s sponsoring organization. In managing and giving advice with respect to DAF assets, the personal IA owes a fiduciary duty to give advice that is in the best interest of the sponsoring organization. Needless to say, a personal IA may face potential conflicts of interest either between his or her own interests and those of a client, or among different clients.18

*These two separate fiduciary duties are well-aligned.*

Regardless, the personal IA’s interest is fully aligned with both the DAF’s sponsoring organization and the donor-client in terms of growing the DAF assets as much as possible for subsequent distribution. Personal IAs are often better equipped to grow the assets in a DAF account at a higher rate than investors. The larger the account balance, the more the donor and sponsoring organization can distribute to their favorite charities.

*The potential conflict to advise against distributions from the DAF.*

For personal IAs, one potential conflict of interest, as the Proposal points out, is that personal IAs may have an incentive to advise against distributions from the DAF because it would dilute the fees they earn from the DAF. As discussed above, personal IAs are required to disclose this potential conflict to their client and obtain the client’s informed consent. More importantly, personal IAs are legally obligated to not act in accordance with this potential conflict (i.e., to not give conflicted advice). If a personal IA violated this legal duty, then he or she would be subject to a Securities and Exchange Commission (“SEC”) enforcement action, disciplinary proceedings, and sanctions, and potential private civil liability as well.

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18 See Restatement (Third) of Agency, § 8.01 General Fiduciary Principle (2006) (“Unless the principal consents, the general fiduciary principle, as elaborated by the more specific duties of loyalty stated in §§ 8.02 to 8.05, also requires that an agent refrain from using the agent’s position or the principal’s property to benefit the agent or a third party.”).
As a practical matter, we have found no evidence that personal IAs are advising against distributions from DAFs. In fact, anecdotal evidence from our members suggests that personal IA advice against distributions is generally not occurring as contributions to DAFs versus distributions from DAFs have been nearly equal in recent years. But even if advice against distributions were occurring (and there is no evidence that it is), it is important to also note that the personal IA ultimately has no control or authority over the sponsoring organization decision-making in terms of the timing and volume of charitable distributions from the DAF.¹⁹

Yet, under the Proposal, the IRS treats this potential conflict presumptively as a fait accompli – a violation that has already occurred and that merits punishment via an excise tax penalty. This approach is unfair and inappropriate, particularly given that potential conflicts like these are regulated, examined for, enforced, and as appropriate, sanctioned under the SEC’s robust federal securities regulatory regime.

In addition, an IA subject to federal securities law is regulatorily obligated to establish policies and procedures, supervision, training, and oversight by a chief compliance officer, for all investment advisory accounts, including DAF assets at the firm (as well as the donor’s personal assets). These policies and procedures and oversight are subject to examination by the SEC. The existing IA regulatory regime fully safeguards against the potential conflicts of interest that concern the IRS and obviates the need for additional IRS regulation with respect to IAs.

5. Professional management of DAFs should be encouraged and not punished with excise tax penalties.

The Proposal takes issue with two alleged practices by sponsoring organizations and personal IAs. Specifically, the Proposal calls out: (1) sponsoring organizations for potentially incentivizing personal IAs to advise their clients to donate to the firm’s DAF by offering the role of DAF investment manager; and (2) personal IAs for potentially incentivizing their donor-clients to donate to a DAF with assets at the firm by offering reduce fees to manage the donor’s personal assets (because the personal IA also earns fees on DAF assets).

As discussed above, if a sponsoring organization’s offer of a DAF investment manager role creates a potential incentive for a personal IA to advise his donor-client to donate to a DAF with assets at the firm, then that would be a potential conflict that must be disclosed and consented to by the donor-client. Regardless, any advice from the personal IA to the donor-client to donate to the DAF must nevertheless also be in the best interest of the donor-client, as a matter of law.

With respect to a personal IA’s offer of reduced fees on personal assets (because the personal IA also earns fees on DAF assets), a number of our member firms report that personal IAs do not in fact charge reduced fees on the donor’s personal assets. Regardless, again, any advice from the personal IA to the donor-client to donate to the DAF must be in the client’s best

¹⁹ Sponsoring organizations likewise take their legal fiduciary duty and responsibilities to the DAF very seriously. Sponsoring organizations are likewise obligated to manage conflict of interest and act in the best interest of the DAF in managing contributions to and distributions from the DAF.
interest. Moreover, the personal IA would be left in essentially the same position as before their client’s DAF donation; they neither gain nor lose on fees.

Finally, it is important to recognize that the negotiation of the fee on the donor-client’s personal assets is separate and distinct from the negotiation of the fee for the DAF (which is negotiated with the sponsoring organization). One is not linked to the other, and thus, the personal IA does not receive a “more than incidental benefit” when these fees are separately negotiated with separate parties and the personal IA subsequently receives both types of fees.

Both of these potential conflicts are appropriately managed and disclosed under the personal IA’s fiduciary duty under the Advisers Act, and both generally benefit donor-clients and the public policy in favor of growing assets in DAFs for subsequent charitable distribution. It is in the best interest of all parties that DAF assets be managed by professional IAs in order to responsibly grow the assets available for donation to public charities.

Recognizing that IAs cannot reasonably be expected to work for free, the Proposal will likely chill the market by either effectively prohibiting traditional IA compensation structures or otherwise subjecting them to excise taxes. Consequently, we would reasonably anticipate a corresponding reduction in overall charitable contributions to DAFs and/or a reduction in the appreciation of DAF assets, ultimately reducing overall donations to public charities, which would be an unfortunate – and hopefully unintended – consequence of the Proposal.

6. The Proposal would benefit from additional revisions and clarifications.

SIFMA’s overarching and principled view is that personal IAs should not be treated as donor-advisors under the Proposal and thus, the IRS should strike the Proposal’s new tax treatment of investment management fees paid from DAF accounts to personal IAs. Regardless, if the Proposal nevertheless moves forward, we recommend the following additional revisions and clarifications:

a. Personal IAs who advise pooled assets in a DAF should be excepted from donor-advisor status under the Proposal.

Proposed regulation §53.4966-1(h)(3)(ii) provides an exception from donor-advisor status for personal IAs who are “properly viewed as providing services to the sponsoring organization as a whole, rather than providing services to the [DAF].” Personal IAs who advise pooled assets in a DAF do not provide service to the DAF as a whole; instead, they provide services equally across all the donors in the pool they advise. For that reason, we recommend that the exception in §53.4966-1(h)(3)(ii) be explicitly extended to include personal IAs who advise pooled assets in a DAF.
b. *IAs who serve as a portfolio manager of a client’s irrevocable trust assets (and who also advise the client’s DAF assets) are not personal IAs subject to the Proposal.*

IAs who serve as a portfolio manager of a donor-client’s irrevocable trust assets (and who also advise the donor-client’s DAF assets) are not personal IAs subject to the Proposal. This is so because the donor-client’s irrevocable trust assets do not constitute “personal assets of [the] donor.” By creating an irrevocable trust, the donor-client transfers all ownership and control of the assets into the trust and legally removes all of their ownership rights to the assets and the trust. The donor-client cannot change or terminate the irrevocable trust after its creation. Accordingly, the Proposal should clarify that portfolio managers of a donor-client’s irrevocable trust assets (who are not also advisers of the donor-client’s personal assets) are exempt from the definition of personal IA under the Proposal.

c. *The Proposal should clarify that only an individual person, and not an IA entity, can meet the definition of a personal IA.*

As discussed above, proposed regulation 26 CFR §53.4966-1(h)(3) defines a personal IA as “[a]n investment advisor defined in 4958(f)(8)(B) of the Code who manages the investment of, or provides investment advice with respect to, both the assets maintained in a donor advised fund and the personal assets of a donor to that donor advised fund.” (emphasis added). 26 USC §4958(f)(8)(B), in turn, defines an “investment advisor” as “any person (other than an employee of [the sponsoring] organization) compensated by such organization for managing the investment of, or providing investment advice with respect to, assets maintained in donor advised funds … owned by such organization.” (emphasis added)

Under our reasonable reading of the two definitions above, in order to meet the definition of personal IA, the same individual person who is compensated by the sponsoring organization for providing investment management services to the DAF must also advise the personal assets of a donor to that DAF. Under a strained and overbroad reading of these definitions, however, an IA entity that employs one individual who provides investment management services to the DAF, and employs a separate individual who advises the personal assets of a donor to that DAF, could be deemed a personal IA. The Proposal should clarify that only an individual person, and not an IA entity, can meet the definition of a personal IA.

d. *The Proposal should provide a one-year transition period and set the applicability date to be the subsequent tax year following the end of the transition period.*

If approved, the Proposal would apply “to taxable years ending after the date of publication” of the adopted rules in the Federal Register. This means that if the Proposal were adopted any time in 2024, then donor-advisors would be subject to the new taxes for all transactions that occurred in 2024. SIFMA believes that this would be unfair, difficult to comply with, and burdensome.
Accordingly, we request that the IRS provide a one-year transition period following adoption of the Proposal and change the applicability date to be the subsequent tax year following the end of the transition period. This will give stakeholders sufficient time to operationalize the new rules during the transition period, and pay any taxes that may come due in the following tax year.

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For all the foregoing reasons, personal IAs are not in fact, and should not be deemed by regulation to be, donor-advisors. SIFMA recommends that the IRS strike the Proposal’s new tax treatment of investment management fees paid from DAF accounts to personal IAs.

**SIFMA hereby requests a public hearing.**

If you have any questions or would like to further discuss these issues, please contact the undersigned at 202-962-7300.

Sincerely,

Kevin M. Carroll
Deputy General Counsel
SIFMA

cc: publichearings@irs.gov (Attention: Vivian Hayes)