**Testimony of**

**William C. Daroff**
**Vice President for Public Policy &**
**Director of the Washington Office of**
**The Jewish Federations of North America**

**House Ways and Means Subcommittee on Oversight**

**Hearing on**

**Tax-Exempt Organizations**

**May 16, 2012**

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The Jewish Federations of North America applauds the House Ways and Means Subcommittee on Oversight for holding the first in a series of hearings focusing on issues related to tax-exempt organizations, including recent efforts by tax-exempt organizations to design and implement good governance standards, taxpayer experiences with the newly-redesigned Form 990, and recent legislative changes to the tax code dealing with tax-exempt organizations.

**Background**: The Jewish Federations of North America ("JFNA") is the national organization that represents and serves over 150 Jewish federations and 300 independent Jewish communities in more than 800 cities and towns across North America. In their communities, the Jewish federation and Network volunteers (collectively, the "JFNA System") are the umbrella Jewish fundraising organizations and the central planning and coordinating bodies for an extensive network of Jewish health, education and social services. With thousands of affiliated agencies and schools, the JFNA system is one of the United States' largest and most effective social service providers, serving well over one million clients each year in both the Jewish community and the general population.

Collectively, the JFNA system raises approximately $2.5 billion each year, roughly $1 billion through an annual fundraising campaign and $1.5 billion from planned giving activities. The vast majority of the $1.5 billion raised through planned giving represent contributions to donor advised funds and supporting organizations, often referred to as “participatory funds.” These funds are critical fundraising tools for the JFNA system, comprising approximately 60 percent of the over $12 billion in endowment assets held by federations. Annual grants and distributions from such donor advised funds and supporting organization represent 80 percent or just over $1 billion of the $1.25 billion in grants made annually from federation endowment assets. Annual distributions from the federation donor advised funds and supporting organizations normally range from 15 to 20 percent of their combined assets at the prior year-end. In addition, as discussed below, participatory funds provide the JFNA system with the opportunity to regularly interact with donors to strengthen our overall philanthropic mission.

**Good governance and Transparency**: JFNA firmly believes that good governance policies and ethical practices represent bedrock principles that are essential if nonprofit organizations are to demand public confidence in their operation. We have long advocated for the establishment of good governance procedures through prudent self-regulation rather than the imposition of government mandates of rigid, one-size-fits-all standards.  Boards of charitable organizations must institute and maintain policies and procedures to ensure that it manages and invests its funds responsibly. Federation boards of directors and investment committees fulfill a duty of care to make sure that endowment assets are invested wisely and prudently. Along with concomitant duties of loyalty and to minimize costs, investment committee members have fiduciary responsibilities to investigate asset management decisions and develop strategies appropriate for the fund and charity.

Federations follow established good governance procedures that insure proper stewardship of the funds raised within our communities. Such stewardship reaches all levels of operation and includes formalized mission statements, well articulated roles and responsibilities for boards of directors, officers and other key personnel, rigid conflicts of interest policies, preparation and review of tax and accounting forms and statements, among others. We take pride in the system-wide training offered by JFNA to federations in various aspects of operations including implementation of investment procedures that develop asset allocation strategies, prepare and maintain investment policy statements, implement investment strategies, monitor and supervise implementation and apply procedures to control and account for expenses. A variety of governance policies are documented, reviewed and substantiated on a regular basis, by both internal committees and independent outside auditors. Such periodic review includes verification of adherence to written policies and procedures related to investment allocation, conflicts of interest, organizational changes, and due diligence questionnaires, among others. In sum, federation internal governance procedures and oversight are designed to avoid conflicts of interest and ensure transparency in order to preserve financial resources and trust for our community today and in the future.

**The Jewish Federations and the Form 990**: In the fall of 2007, JFNA provided extensive comments to the IRS regarding the redesign of the Form 990. We applauded the IRS attempts to revise the form to increase transparency of nonprofit organizations through promoting compliance with the tax law and regulations and minimizing reporting burdens where possible. Although we supported the underlying principle that the Form 990, unlike other tax reporting forms, needs to provide meaningful information on the operations and structure of tax-exempt organizations, especially for those with detailed compensation arrangements, related entities, and complex transactions, we did express concern that many tax filers within the JFNA system would face increased reporting and compliance burdens because their size, structure and breadth of activities would require the completion of several of the detailed new schedules that accompany the new core form. In addition, smaller federations and agencies within the system would find that the new form would greatly increase the cost of compliance and add burdensome recordkeeping and data collection requirements. We urged that the IRS carefully balance the benefits from increased transparency that can be achieved through voluntary compliance with the costs from expanding reporting requirements that will be imposed on the nonprofit sector.

As noted above, our comments on the revised Form 990 emphasized our commitment to good government policies implemented through a self-regulatory approach. Specifically, in regard to the governance questions added to the Form 990, JFNA noted that the instructions to form began with the statement that "(a)ll organizations must answer each question in section III even though certain policies and procedures may not be required under the Internal Revenue Code." JFNA has actively supported "good governance" measures for nonprofit organizations for many years and was a major participant in the important work of the Panel on the Nonprofit Sector, organized in response to the recommendations of the Senate Finance Committee staff. Our comments to the IRS reflected our belief that to the extent that certain practices are mandated by federal or state law, it is appropriate that such practices "must" be followed by tax-exempt organizations. To the extent that such practices are recommended to advance ethical and effective behavior, it is appropriate that such principles "should" be followed by such organizations. We suggested that the IRS make clear that certain governance practices and policies listed on Form 990 represented recommendations and were not required by the tax code. We also noted that certain questions that asked for simple "yes" or "no" responses needed to be expanded to provide supporting explanations that could provide the user with a better understanding of the reporting organization's response and behavior.

In summary, JFNA believes that the new Form 990 does provide both the IRS and the general public with additional useful information as the overall operations of tax-exempt organizations. It should be noted, however, the overall compliance burden and related professional costs for preparation and review have risen significantly for virtually every organization within the JFNA system. Because of the added complexity of data collected, as well as the sensitivity of matters contained on sections of the revised form, many federations have created separate committees tasked with a detailed review of the new Form 990. We continue to work with the IRS to refined portions and schedules of the Form 990. For example, we recently raised the question of duplicative reporting of foreign grants by domestic organizations that make non-earmarked grants to other domestic organizations that can ultimately be granted overseas with the IRS. We appreciate the cooperation that we have received from the agency in consideration of our ongoing to minimize unnecessary or burdensome reporting on tax-exempt organizations.

**Recent legislative changes on tax-exempt organizations:** The Pension Protection Act of 2006 ("PPA") provided significant new rules for donor advised funds and supporting organizations. As noted above, these participatory funds are essential fundraising tools for the JFNA System and have been a vital source of the health, education and social service programs of agencies of our agencies. In addition to providing financial resources for critical human services in the local Jewish and general communities, these charitable vehicles also advance the values and goals of the JFNA System through nurturing relationships between Jewish philanthropists and federation lay and professional leadership, building leadership and social capital in the Jewish community, establishing priorities that consider the future needs of the Jewish community, and reinforcing the positive perception of the federation as a philanthropic partner within the larger community.

Many of the provisions contained in the PPA provided needed statutory definitions and operational rules for participatory funds as well as a penalty tax framework that can be applied to discourage unwarranted acts of self-dealing. However, JFNA continues to believe that it is in the public interest to provide incentives for donors to contribute assets to vehicles in which a public charity maintains ultimate supervision and control, such as is the case with participatory funds.

We are exceptionally proud that agencies within the JFNA System employ the highest ethical standards of self-regulation in governance and operation of participatory funds and regularly share expertise with other charities and policy makers outside the Jewish community on a variety of charitable giving issues. To help federations meet these high standards, appropriate rules and best practices were set forth in two separate JFNA publications, Donor Advised Funds: A Guide for Jewish Federation Endowment Professionals, and Handbook on Supporting Foundations, for use by the JFNA System. These publications have been revised to reflect the new requirements of the PPA.

JFNA believes that well-administered donor advised funds and supporting organizations that have policies and procedures in place to assure that qualified grants are made and impermissible material benefits to donors are not present greatly adds to overall tax administration. This oversight function performed in federation planned giving and financial departments throughout the country is an important component of the overall tax compliance system that operates in concert with the goal of furthering philanthropic endeavors.

We need to note however, that this oversight function does not come without cost. Virtually every federation now faces increased costs in administering their grant-making function from participatory funds. To prevent an unwanted chill on the philanthropic endeavors of donor advised funds and supporting organizations, it is essential that charities that administer such funds not be burdened with unnecessary procedures and requirements when they accept gifts, approve grants or make distributions in the normal course. In this regard, we have met with representative from the Treasury Department and the IRS on several occasions to urge that rules and regulations interpreting the PPA provide bright-line tests for donor advised funds that could be easily understood by donors and readily administered by fund managers and grant recipients. This clarity would improve compliance as well as foster philanthropy. For example, we continue to urge that Treasury and the IRS make it clear that donor advised funds are not permitted to make a grant if the donor to the donor advised fund is receiving more than an incidental benefit in return for such grant and that an impermissible benefit for purposes of the donor advised fund provision is the same as a benefit that would preclude a donor to a public charity from meeting the definitional requirement for a charitable deduction under Internal Revenue Section 170 for such contribution.

**Summary**: JFNA supports the efforts of the Subcommittee on Oversight to assure that tax-exempt organizations fulfill their mandate to the public. We support efforts to assure that such organizations meet the highest standards of good governance and transparency. We will continue to work with the IRS to balance the goals of increased reporting without imposing unnecessary or “one-size-fits-all” rules as it pertains to the Form 990. In addition, we will continue to work with the Treasury and the IRS to assure that the implementation of rules interpreting the PPA permit participatory funds such as donor advised funds and supporting organizations to continue to be vibrant vehicles for philanthropic giving.

I thank the committee for the opportunity to present this testimony. If you have any questions regarding this submission, please feel free to contact William C. Daroff, Vice President for Public Policy and Director of the Washington Office at 202-736-5868 or william.daroff@jewishfederations.org or Steven Woolf, senior tax policy counsel at 202-736-5863 or steven.woolf@jewishfederations.org