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New Regulations Make Important Changes for Private Foundations That Make Grants to Foreign Charities - an Affidavit Alone Won't Do It

Most foreign charities do not have determination letters from the IRS recognizing their status as tax exempt. However, private foundations have long been able to make grants to a foreign organization that is determined in good faith to be equivalent to a U.S. public charity (in a so-called equivalency determination).

Until recently, regulations provided that an equivalency determination is made in good faith if it was based on an affidavit of the grant recipient or on an opinion of counsel that the recipient is equivalent to a U.S. public charity. Many foundations have relied on the affidavit route, which provided a relatively inexpensive and easy process for a grant to a foreign school, hospital or charity with broad public support. Proposed regulations issued in 2012 were intended to facilitate foreign grants by expanding the class of advisors whose advice may be relied on to include "qualified tax practitioners," including CPAs and enrolled agents, as well as lawyers. The final regulations published by the IRS on September 23, 2015, make changes along these lines but also include significant additional changes.

The major new change is to eliminate the reliance on an affidavit of the recipient as the *sole* basis for making the determination (although these affidavits may still be used as *part* of the determination). However, there is no requirement that a private foundation obtain written advice from a qualified tax practitioner. In fact, the regulations provide that:

[G]rantee affidavits remain a cost-effective way of obtaining information relevant to making good faith determinations, and foundations may continue to rely on them when making determinations *to the extent reliance is reasonable and appropriate under the facts and circumstances*

The regulations cite as an example that *"a foundation manager with understanding of U.S. charity tax law may under the general rule make a good faith determination that a foreign grantee is a qualifying public charity based on the information in an affidavit supplied by the grantee."*

This does not mean a foundation can rely on an old affidavit or written advice. The regulations require that advice be "current" - meaning that there has not been any change in the law underlying that advice and that the factual information on which the advice is based is from the grantee's current or prior year. For advice on whether a foreign organization gets enough public support over a five-year period to be deemed equivalent to a public charity, information can be relied on for the two years following that period.

To provide time to transition to the final regulations, there is a 90-day period during which private foundations may make distributions to foreign organizations based on the old rules set forth in the proposed regulations. In addition, a private foundation that makes a grant to a foreign organization pursuant to a written commitment made before September 25, 2015, will be compliant so long as the grant is fully distributed to the grantee within five years.

The Bottom Line

Private foundations that have relied solely on affidavits of the recipients in making equivalency determinations will need to consider how to make these determinations after the transitional period. Going forward, the affidavit alone will not be enough. Additional steps, depending on circumstances, may include hiring a qualified tax practitioner to provide an equivalency opinion, obtaining information from a repository such as NGO source or, in appropriate instances, making determinations without opinions, but documenting the analysis in writing.

Although the standards for what is needed beyond an affidavit are not clear, it is apparent that something in writing setting out why the affidavit can be relied on is now prudent for any equivalency determination.

We are happy to help you with equivalency determinations under the new regulations.

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