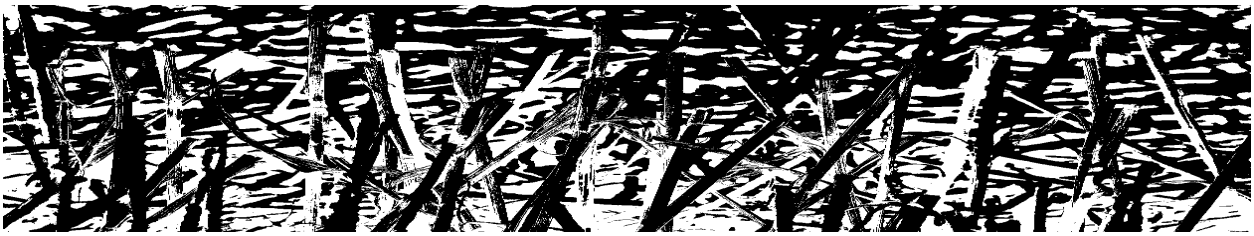

Jack Straw Fortnightly*

wabbit season

A panel of the 9th Circuit federal appeals court heard oral argument last Monday in *Pinkert v. Schwab Charitable*, a case we covered in some detail last August in Jack Straw four comma six, with links to the pleadings and the briefing on motions to dismiss, and again in four comma nine and five comma two, with links to the briefs on appeal.

Pinkert is a sort of sequel to *Fairbairn v. Fidelity Charitable*, which Jack covered in three comma three and again in three comma nine.

A sequel in the sense **that a contributor to a donor advised fund** is again arguing that she **has some kind of retained property interest** in the fund **that should give her standing to sue** the fund sponsor for mismanaging the investment of fund assets.

We will not go into a lot of detail this time around. Jack's take has been that these folks are playing with fire: if the courts were to determine **that a contribution to a donor advised fund is subject to a condition subsequent**, IRS should disallow the claimed charitable deduction altogether.

But a couple of things did strike Jack as interesting during last Monday's argument.

One, the lawyer for the plaintiffs/appellants said more than once that the tax Code "requires" that a fund sponsor extend advisory privileges to the contributor or her designee, and specifically at time stamp 11:04 she argued that if Schwab Charitable did not provide the contributor "meaningful" advisory privileges, **it would lose its status as an exempt donor advised fund.**

This argument was also advanced in their opening and reply briefs, and for some reason not directly challenged by Schwab Charitable in its response brief nor at oral argument.

But Jack wants to say this is pretty much an inversion of what section 4966(d)(2)(A)(iii) actually says, which is that if a fund sponsor does extend advisory privileges, then we have this creature called a "donor advised fund," which is subject to excise taxes on any distributions it might make other than to a (b)(1)(A) charity unless it exercises expenditure responsibility.

Oversimplifying somewhat, but the point being that the purpose of sections 4966 and 4967 is not to create a new species of exempt entity but **to identify an existing form as a disfavored stepchild** of the sector, grudgingly acknowledging that a fund sponsor might actually listen to a contributor or her designee in making grants, but imposing specified restrictions if they do.

If Schwab did not extend advisory privileges, you would have maybe a designated fund or a field of interest fund, which would be subject to less regulatory restriction, but the fund would not "lose its exempt status."

bundle of sticks

Anyway, the issue on which this case will be decided is standing. Does a contributor to a donor advised fund have a legally cognizable interest in the fund that would allow her to sue the sponsor for mismanaging fund assets, yes or no.

And the theory here is that the "robust" advisory privileges in fact extended to the plaintiffs, while not a "property" interest in any traditional sense, do confer "reputational" or "expressive" interests that may be impaired by mismanagement of the fund, which they should have standing to protect.

Near the start of the respondent's argument, at time stamp 13:38, the judge who was chairing the panel lobbed what seemed like a softball to the lawyer for Schwab Charitable, asking **whether this "reputational, expressive" stuff had even been pleaded** below.

To his credit, the respondent's lawyer argued that **even if it were adequately pleaded there would be no standing**. But he did say he didn't think it had been pleaded, and he did not say why. And on rebuttal, the lawyer for the Pinkerts did not pick up this thread.

Jack says it would be a mistake for the panel to decide this case on that technicality, because

> (a) the plaintiffs would simply be given leave on remand to amend their complaint, and we would be back here in another year or two, and
>
> (b) there really is no question that the amended complaint does allege "reputational" and "expressive" interests, which are after all kinda the entire point here.

And then at the very close of her rebuttal argument, at time stamp 28:25, the lawyer for the Pinkerts conceded that

> if her client's standing were premised on the idea that because of Schwab Charitable's mismanagement he would have to make additional contributions to the fund in order to realize his "reputational" or "expressive" objectives, and
>
> if he had not in fact yet made additional contributions,

he would not have standing because his injury would be "speculative."

This Jack says was an unforced error.

And again, if the case is decided on this ground, Jack says this would be a mistake.

meanwhile

The DOJ has amended its complaint in *Eickhoff*, correcting the mistaken allegation, which had been repeated multiple times in the complaint as initially filed, that a qualified charitable remainder trust is required to file not only a 5227 but also a 1041.

Your correspondent had communicated with the DOJ lawyers on the subject, and is here taking credit for their having corrected this error in the amended pleading, which now states that **a nonqualified split interest trust would be required to file a 1041 rather than a 5227.**

We wrote up the initial complaint last month in Jack Straw five comma four, suggesting at the time that this case almost certainly grew out of the facts underlying an advice memo we covered almost two years ago in three comma seven.

At issue here is a flawed strategy to "trap" realized gains inside what purports to be a charitable remainder annuity trust. We refer the reader to our previous coverage for details.

and now these words

Jack would like to take a moment here to thank Peter J. Reilly, an accountant who has a regular column in Forbes, for giving this newsletter a shout out in his March 22 column on the decision of the 6th Circuit federal appeals court in *Oakbrook Land Holdings*.

Mr. Reilly mentions your correspondent alongside three other well respected commenters with whom Jack would be hesitant to claim anything like parity.

And he finds a succinct pull quote. Again many thanks, Peter.

and these

This is as good a place as any to also mention that your correspondent had an article placed in the most recent issue of the quarterly Journal of the bar association of metro St. Louis metro bar association,

concerning a Missouri statute drafted some years ago by a committee of the state bar to enable a trust beneficiary to test the water before committing to a petition or motion that might trigger an *in terrorem* clause, forfeiting her interest in the trust,

and how that statute has fared in five different cases reviewed by various state appellate courts.

The article expands considerably on the writeup in Jack Straw three comma four on the Missouri state supreme court's mishandling of a collusive lawsuit that was apparently intended to highlight shortcomings in the statute.[1]

A .pdf of the article as printed is linked to a blog post on your correspondent's website, with some mild complaining about the vagaries of editing for publication, together with the original typescript.

We now return to our regularly scheduled programming.

a hill of beans

The so-called "secure two point oh" bill, H.R. 2954, has cleared the House on a nearly unanimous vote, with five Republicans dissenting, only one of whom goes on record to explain why.

Tucked away in this bill is an extremely modest incentive for charitable giving, which may be a toehold for eventually enacting something like the so-called "legacy" IRA.

Section 310 of the bill would amend Code section 408(d)(8) to allow up to $50k of what would otherwise be a "qualified charitable distribution" from a traditional IRA to be directed instead to what is referred to as a "split interest entity," by which is meant either a charitable remainder trust or a gift annuity.[2]

But **only once**, and **only if the QCD is the only source** of funding for the remainder trust or the gift annuity. And **only if the payout is at least five pct.**, and **only if the entire payout is treated as ordinary income**.

There is a modest revenue estimate attached to this provision, a few hundred million in early years, almost nothing in outlying years,

but Jack wonders whether there is any market for this at all.

No one, says Jack, would set up a remainder trust to hold only $50k. And probably very few charities would issue a gift annuity for that amount. The costs of administration are just too high.

There is also provision for **adjusting the existing $100k limit on outright QCDs for inflation** from 2021, which is at least something.

gimme back my papers

In our last issue, five comma four, we speculated that the March 03 decision of the 6th Circuit federal appeals court in *Mann Construction*,

invalidating an IRS Notice that had listed a transaction as "abusive" without affording an opportunity for public comment, might not bode well for the IRS in *CIC Services*,

which was on remand to the eastern district of Tennessee from the Supreme Court having reversed both the 6th Circuit and the trial court on the question

whether a suit challenging the validity of Notice 2016-66, dealing with microcaptives, was barred by the anti-injunction act.

We did not have to wait long, contra Jack's prediction in four comma nine that with the filing of an amended complaint last November it would be "awhile before we see a substantive result."

On March 04, the court invited supplemental briefing on the question what effect *Mann Construction* might have on the pending case. IRS filed a response, arguing

(a) that the court should not "rush to apply" that decision while it was still subject to possible motions for rehearing,[3] and

(b) that technically the validity of the Notice listing the

transaction at issue in *Mann Construction* was no longer at issue when that case went up on appeal, so the statement in the appeals court opinion that it "must set aside" the Notice is dictum.[4]

What IRS did not argue, as Jack had suggested in each of the newsletters linked above that it might, is that there is a difference between

a Notice "identifying" a transaction as "of interest" in order to facilitate information gathering to support possible, eventual formal guidance, and

a Notice "listing" a transaction as "abusive" in order to identify audit targets.

The latter is clearly "legislative," and arguably requires an opportunity for public comment. The former not so much.

As Jack argued in four comma nine, "[w]ith the enactment of section 6707A(c)(1) in 2004, Congress expressly empowered IRS to make these inquiries."

One might in theory argue this was an improper delegation of legislative authority, but no one has been making that argument.

In any event.

In filing its amended complaint last November, the taxpayer expanded its prayer for relief to include not only a declaration that the Notice was invalid but also an injunction

preventing IRS from using any of the information it had gathered from participants and material advisors while the Notice was in force, and

requiring the agency to "destroy or return" these materials to those who had submitted them.

In its final judgment on March 23 vacating the Notice, the trial court granted this additional relief in part. While the court declined to enjoin IRS from using information it might also have acquired from other sources, it did require the agency

[to] return all documents and information produced pursuant to the Notice to taxpayers and material advisors.

IRS has filed a motion to reconsider this aspect of the ruling, arguing that the court had actively discouraged the parties from briefing the issue pending a determination of the validity of the Notice itself, and also a motion to stay the injunction pending resolution of the motion to reconsider.

Jack does expect to see another appeal in *CIC Services*, but he is not optimistic the 6th Circuit will give IRS a favorable ruling or that the Supreme Court will again grant cert.

let's go crazy

The 7520 rate for May is up eighty basis points from April to three point zero percent. A hundred forty basis points from the February rate of one point six.

Leverage for remainders after a fixed annuity is dwindling fast. Anyone wanting to take advantage of the two-month lookback for a charitable gift of a lead interest

will need to close the transfer within the next few days.

Jack again reminds the eager planner that **there is a tradeoff between the larger deduction for a gift annuity and the exclusion ratio** on the payout.

(non)compliance strategy

In a field advice memo released March 18, numbered 20221101F, a lawyer in the TE/GE Division advised an area manager for EO Examinations that an org that was filing the "e-postcard" year after year,

despite the fact it was not eligible because it "normally" had gross receipts of more than $50k,

would be subject to automatic revocation after three years of in effect not filing information returns, **without the notice otherwise required, and without recourse to the Appeals Office,**

unless TE/GE and Appeals were to adopt an informal policy to allow Appeals to reconsider the examiner's determination of gross receipts.

The memo describes the filing of "e-postcard" by an apparently ineligible org as a "compliance strategy," as though this were being done intentionally to avoid making disclosures that would otherwise be made on a 990 or 990-EZ.

lorem ipsum

[1]

And concludes that a revision to the statute may in fact be indicated, but ironically largely because the courts handling *Knopik* screwed up.

Your correspondent has submitted a proposed revision to the probate and trust law committee of the state bar, which may take it up at its semi-annual meeting on May 03.

[2]

Not a pooled income fund, which cannot be expected to pay five percent. And of course Jack would quibble that a gift annuity is not a "split-interest entity."

[3]

The time for filing such motions has since elapsed.

[4]

Jack is all about procedural niceties, but even he is not persuaded by this argument. The substantive relief granted the taxpayer in *Mann Construction* logically depends on the invalidity of the subject Notice.

If the DOJ had wanted to clarify this matter, it should have filed a motion for rehearing. Which would have been denied.

Jack says, facts are never what they seem to be