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Donor Advised Funds

A Donor Advised Fund (DAF) is an investment account that is used for charitable giving and has many tax advantages, including tax-free growth of assets. DAFs are tax-exempt vehicles, sponsored by 501(c)(3) organizations such as community foundations, national charities and single-issue charities. The growth in Donor Advised Funds over the past few years has outpaced other charitable giving options such as private foundations, charitable trusts and direct giving. This is not surprising, as DAFs can be one of the most effective ways to make charitable gifts. For many clients, a Donor Advised Fund is ideal due to its simplicity, tax-efficiency, low fees and minimums, flexibility in gifting, etc.

Types of Donor Advised Fund Sponsors

- **Community Foundations** – Typically locally or regionally focused and may provide support in assisting donors with their charitable gifts based on their deep knowledge of local charities. These foundations may be smaller and thus may have higher minimums and fees or be unable to accept certain assets. The largest Charitable Foundations in Minnesota are the Minneapolis Foundation and the St. Paul & Minnesota Foundation.
- **National Charities** – These sponsors are not affiliated with a region or specific charitable purpose. Many of the largest charities are through financial service companies such as Fidelity Charitable, Schwab Charitable and Vanguard Charitable. They typically are low cost and have low minimums. However, they do not provide hands-on assistance in making charitable recommendations.
- **Single-Issue Charities** – These support specific institutions such as universities, religious organizations, United Way, The Sierra Club, etc.

Features of a Donor Advised Fund

- **Simplicity** – One tax receipt, no administration or legal assistance needed (unlike a trust and or a foundation).
- **No set up costs –** Set up costs for a trust or a foundation can be significant.
- **Low minimums** – Many national DAF have minimums of $5,000, other DAFs such as Community Foundations or Single-Issue Charities, may have $25,000-$100,000 minimums. Other charitable giving vehicles such as trusts or private foundations can have practical minimums of hundreds of thousands or millions of dollars.
- **Charitable tax deduction** – Contributions to a DAF are tax deductible in the year they are funded. A benefit of DAFs is that they allow the tax deduction to be separated from the charitable contribution which can be beneficial for several reasons.
- **Easy to contribute non-cash assets** – Some charities are only equipped to accept donations of cash; thus, a DAF can act as an intermediary for other kings of gifting. Many types of securities can be contributed to a DAF including cash, publically traded securities, mutual funds, private equity and hedge fund interests, real estate, cryptocurrencies, private business interests, etc.
- **Tax-free growth –** Assets can appreciate tax-free in a DAF, whereas private foundations and charitable trusts have different taxation rules.
- **Investment options** – Differ at each DAF, typically mutual fund and ETF options. Often investment options are limited rather than completely open.

- **Grants –** Can be basically made to any IRS qualified public charity. Minimum grant amounts differ among DAFs but can be as low as $50 for National Charities.
- **Flexible distributions –** DAFs do not have a mandatory distribution requirement by the IRS (unlike private foundations or charitable trusts). This allows flexibility in making granting decisions. However, the DAF sponsor may have minimum granting activity rules, often over multi-year periods.
- **Privacy –** Gifts can be made anonymously.
- **Legacy** – Donor advised funds can be used to promote and teach charitable values among family members and act as a legacy conduit. The sponsor on a DAF can often be transferable (ex. to heirs on death) to be managed by a successor. In addition, a DAF can be the beneficiary in a will or trust.
- **Portable –** Many DAFs allow for transfer of assets to another DAF sponsor.

Advanced Planning Benefits

- **Appreciated assets** – One of the large benefits of a DAF is that you can gift appreciated assets and avoid paying capital gains. For people in the higher tax brackets, this can be a considerable tax savings.
    - If appreciated assets are gifted, you can take a tax deduction up to 30% of AGI.
    - If cash is gifted, you can take a tax deduction up to 60% of AGI.
- **Concentrated stock positions** – Some individuals have concentrated positions, for instance in company stock. By gifting concentrated positions, you can diversify the portfolio.
- **Maximizing the tax deduction** – Standard deduction limits were raised as part of the Tax Cuts and Jobs Act of 2017, which reduces the benefit from annual charitable deductions. Instead of annual gifts, contributions can be bunched into a single year to maximize the tax benefits. Bunching can especially be beneficial in big income years or to offset income recognized due to a large Roth conversion.

Challenges of a Donor Advised Fund

- **Management fees** – The DAF sponsor charges an annual administrative fee, which is a drawback when compared to gifting directly. However, for the DAF admin fee you are essentially paying for all of the positive features such as its simplicity, tax-free growth, ability to contribute appreciated assets, etc.
- **Irrevocable gift** – While not necessarily a challenge, it should be highlighted that contributions into a DAF are irrevocable gifts to the sponsor firm. Therefore, after contributing into the DAF, the donor no longer has control of the assets. However, generally the DAF sponsor follows the donor's granting proposals.
- **Satisfying pledges** – Technically a DAF can satisfy a personal pledge; however, there are qualifications. The pledge has to be non-binding and the donor cannot receive any benefits due to the grant. The DAF sponsor cannot reference the pledge in its grant. The donor cannot claim an additional tax deduction since a tax deduction was already taken when assets were contributed into the DAF.
- **Charity events** – As mentioned above, the donor cannot receive any benefits or services from the grant and thus a DAF cannot be used to attend or sponsor a table at a charitable event or gala.

For many clients, donor advised funds may be the ideal option to implement their charitable plans. Donor advised funds, when combined with integrated financial, tax and estate planning can be a powerful tool. SilverOak can help determine which DAF matches client goals and needs. It is important to review charitable giving within the full context of a financial plan to ensure goals are being met efficiently, as there are many tax and estate planning considerations when implementing a charitable giving plan. Additionally, each DAF has different rules and procedures, so it is important to know the landscape. If charitable giving is one of your core values, it would be a privilege to help you make a meaningful difference in the causes that you care most about, either during your life or at your passing. Speak with your SilverOak advisor if you'd like to learn more.

Disclaimer:

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Investment decisions should be made based on an investor's specific circumstances taking into account items such as, risk tolerance, time horizon and goals and objectives. All investments have some level of risk associated with them and past performance is no guarantee of future success.