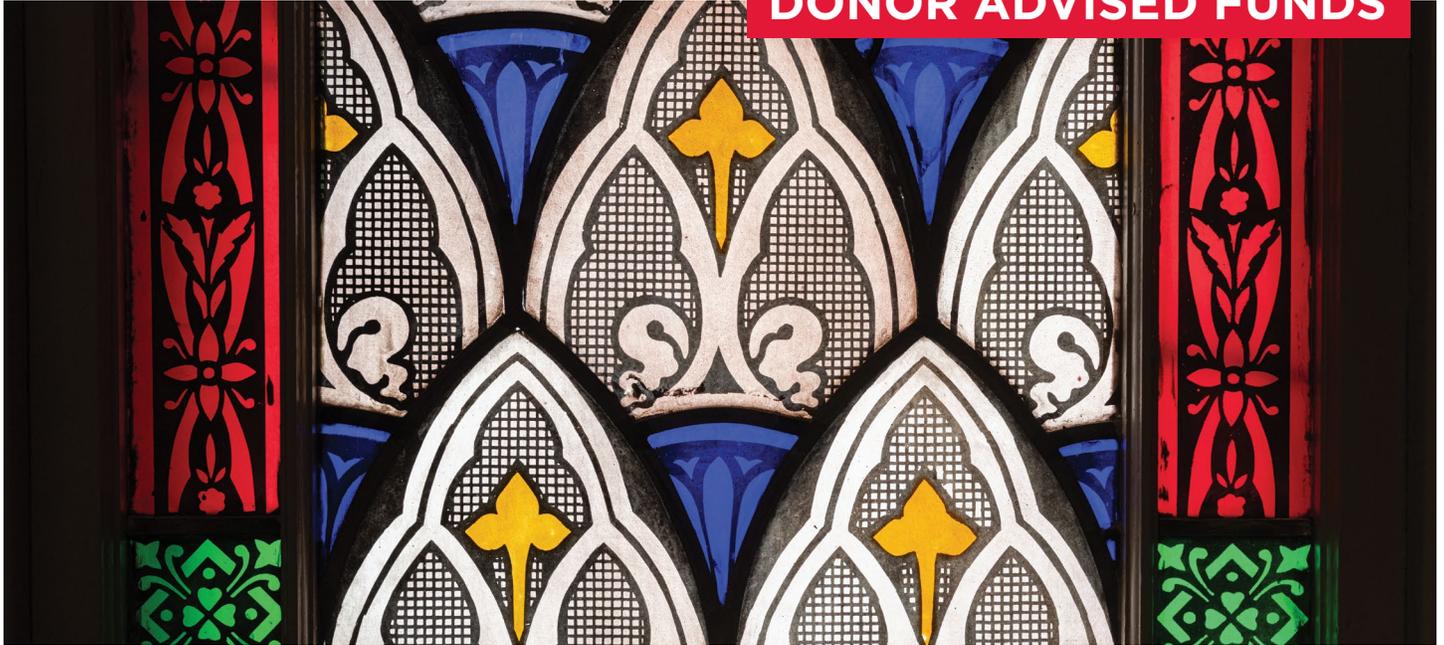


DONOR ADVISED FUNDS



Congress Creates a Powerful Tool for Philanthropy

No doubt giving through donor advised funds (DAFs) is a growing phenomenon in the United States. In the pre-DAF era, philanthropists had reasons for creating private foundations (aka family foundations) to attain privacy, control, tax efficiency; consolidate giving; and involve multiple family members or generations in the giving decisions about family wealth.

All those reasons still exist (and so do private foundations), but today one can achieve all the same benefits at significantly lower cost and complexity, with even greater tax benefits, by opening a DAF. Given their rising popularity among donors at every level in every part of the country, it's worth examining how DAFs work and how to maximize giving through them.

What Are DAFs?

When the IRS first defined DAFs through the 2006 Pension Protection Act, they already had been in existence for 75 years. The New York Community Trust started the first one in 1931, followed by multiple community foundations and Jewish federations, and in 1987 the National Foundation was the first stand-alone DAF to receive a 501(c)(3) designation (followed by Fidelity Charitable in 1991 and Vanguard Charitable in 1997). Despite this long history, today DAFs are the fastest growing type of charitable gift vehicle in the U.S.

DAFs are accounts hosted by a 501(c)(3) charity, opened by an individual with donated assets above a minimum amount. The donor subsequently recommends (i.e., "advises") that grants be

made out of the DAF to other 501(c)(3) charities named by the donor.

The donor receives full tax credit for the gift to the DAF, just like a completed gift to any other 501(c)(3), but later can recommend grants to one or multiple charities. Unlike private foundations, no rules currently exist requiring minimum charitable distribution of DAF funds.

Why Do Donors Open DAFs?

DAFs mimic many of the benefits of a private foundation, but with much lower startup and operating costs, lower requirements for recordkeeping and grant reporting, no minimum distribution requirements, AND higher and more favorable deductibility of donated assets.

Features common to most DAFs:

- Most DAF minimums are \$5,000 or \$10,000 to open.
- DAFs accept cash, stock, and non-cash assets.
- Donor-advisors have online access to make grant requests and research charities.
- Donor-advisors can name additional and successive donor-advisors.
- Donor-advisors can remain anonymous to the charities they support if desired.
- DAFs are professionally managed and the investments grow free of taxes.

Who Gives Through DAFs?

Multiple studies in recent years provide insight about existing DAF donors:

- The overwhelming majority (94 percent) of 15,300 surveyed DAF donors are repeat donors who grant to the same charities more than once, and among that group 47 percent grant the same amount every year.
- DAF donors are involved: 73 percent report being somewhat or very involved in the charities they support, with 6 percent reporting they became more involved after opening a DAF.
- DAF donors are strategic: 61 percent report being somewhat or very strategic with their philanthropy, with 18 percent reporting becoming more strategic after opening a DAF.

There's no question that DAFs cause donors to be more thoughtful in how their philanthropy is distributed, and promote long-term relationships between donors and the charities they most wish to support.

Can DAFs Be Used to Make or Pay a Pledge?

Yes, if three conditions are met.

Ever since the IRS first wrote comprehensive rules governing DAFs in 2006, confusion has prevailed over the question of DAFs making payments on a pledge recorded in the donor's name. The root of the problem is the severe IRS penalty imposed on donor-advisors and DAFs if a grant is made that results in "more than an incidental benefit" to the donor-advisor. The IRS might consider a DAF payment on a pledge obligated by another party (the donor-advisor) a personal benefit.

Fortunately, in December 2017 the IRS proposed clarifying rules over DAFs and pledge payments. Although not yet law, the notice (2017-73) provides that donor-advisors and DAF sponsors may immediately rely on it for guidance relating to DAF pledges. The IRS will not impose penalties for fulfilling a personal pledge with a DAF if:

1. When making the grant, the DAF makes no reference to the existence of the pledge.

2. The donor-advisor nor anyone else receives directly or indirectly any other benefit besides the pledge payment.
3. The donor-advisor does not claim a charitable deduction for the grant, even if the charity mistakenly provides a tax receipt to the donor.

DAF donors wishing to pledge a gift have several options.

- 1) Donor-advisors can **ask the DAF to sign the pledge**, which most will do if the DAF account already has the funds in it.
- 2) If the donor-advisor signs the pledge without the DAF, **the donor-advisor must omit any reference to the pledge when making the grant request** with the DAF.
- 3) Finally, the donor-advisor can sign a **non-binding giving plan** or gift intention document that presents no problem for a DAF to fulfill since there is no legal obligation to do so.

Where Can One Open a DAF?

At last count, there were 979 DAF sponsoring organizations holding 285,000 accounts worth \$90 billion. The three most common places to find a DAF program are:

1. Community foundations, such as the Baltimore Community Foundation and The Associated: Jewish Federation of Baltimore
2. National charities, such as National Philanthropic Trust and the Schwab Fund for Charitable Giving
3. Single-issue charities, such as Feeding America and Boys and Girls Clubs of America

Like a majority of 501(c)(3) charities, the University of Maryland Baltimore Foundation does not have its own DAF, but *gifts from DAFs are essential to our annual support* and we welcome the opportunity to work with existing DAF holders as well as those considering DAFs among other giving options.

This publication is not intended to provide legal, tax, investment, or other professional advice, and should not be relied upon for such advice. In advance of any charitable gift plan, we encourage you to seek the advice of legal, tax, and investment professionals.

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