WHAT GIFT PLANNERS NEED TO KNOW ABOUT DONOR ADVISED FUNDS

PG CALC WEBINAR

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I. Donor Advised Fund Basics

A. Working Definition and Characteristics

As its name suggests, a donor advised fund (DAF) is in the nature of an account maintained by a public charity to which a supporter of the charity has made a contribution with the understanding that the contribution is to be credited to the account – and with the further understanding that the supporter will have certain advisory rights (as detailed below) vis-à-vis the account. Not surprisingly, the supporter is known as the "donor" and the charity serves as the "sponsor" of the DAF.

Indeed, the DAF itself is not a separately existing legal entity. Thus, whenever a contribution is made to establish a new DAF or augment an existing DAF, the contribution is made *to* the sponsoring charity *for* the DAF.

The advisory rights associated with a DAF take two general forms. First, the donor will *always* be able to make recommendations to the charity regarding distributions from the DAF. The recommendations will typically address when the distribution is to be made, how much is to be distributed, how the distribution is to be used, and the identity of the recipient, recognizing that it will almost always be another public charity although – depending on the sponsor's policies – it could be an organization that does not qualify as a public charity under U.S. tax law. *Less often*, the donor will be able to make recommendations as to how assets attributable to the DAF are to be invested or to be managed in other respects.

Any recommendation the donor makes must ultimately not be binding upon the sponsor, as the sponsor will need to determine to its own satisfaction that the advice being provided by the donor is sound. That being said, charities sponsoring DAFs typically carry out the recommendations of donors. In part this is because if a sponsor declines to do so in any case other than one in which the donor's recommendation is plainly unacceptable, the sponsor risks alienating not only the donor in question, but also other donors and potential donors who may decide that the sponsor is not sufficiently accommodating.

A DAF can continue to exist for as long as the policies of the sponsor permit it to do so. Sometimes this can be for a period of years, sometimes for the lives of the donor or one or more other persons, or sometimes for a combination of the two. In other instances, a DAF might terminate when it no longer holds any assets, when the value of its assets dips below a certain amount, or when other conditions are met. Some sponsors will even allow a DAF to last conceivably forever. The sponsor's policies will also determine how any value remaining in a DAF upon termination is to be distributed. Often this is accomplished through a beneficiary designation such as might govern a life insurance policy or a qualified retirement plan.

B. More about Donors/Advisors

While normally the donor who establishes a DAF will also be the one to exercise the advisory rights, many variations on this standard arrangement are possible. For one thing, there could be more than one donor, say a married couple or several members of a particular family. In such an instance either all or fewer than all of the contributors might have advisory rights, although whenever two or more parties have advisory rights the sponsor will usually insist that the advisors act in concert or through a spokesperson.

Even though most DAF donors are individuals, a DAF can be established by or supplemented with contributions from one or more entities, such as corporations, partnerships, or trusts. One possibility is for a charity that is distinct from the sponsor – yet eligible to receive distributions from a DAF maintained with the sponsor – to establish a DAF to which supporters of the non-sponsor charity could make contributions. Nevertheless, the donor charity, rather than any of the other contributors, would retain the advisory rights with respect to the DAF.

The opposite also occurs sometimes: a donor establishes a DAF but then allows one or more other parties to exercise some or all of the advisory rights, either initially or at some point in the future. In fact, it is quite common for an individual to establish a DAF and then designate surviving family members to take over as successor advisors upon the donor's death.

In short, not all DAF donors are advisors and not all DAF advisors are donors. Still, to the extent a donor that establishes a DAF gives up any of the available advisory rights, the donor will at least be the one to select the holder of those rights.

C. More about Sponsoring Charities

DAFs were first established with traditional community foundations, i.e., organizations that exist either exclusively or primarily to serve the charitable needs of a particular geographic area, whether a city, a county, a region within a state, or an entire state (or group of states). There are now approximately 750 such foundations throughout the country.

Similar to traditional community foundations are hundreds of charities, many of which sponsor DAFs, that exist to channel support to other charities that are engaged in specific charitable endeavors or that uphold certain doctrines or principles. Examples include the nation's many local Jewish federations, as well as numerous other charities that gather contributions from persons with a specific religious heritage and make distributions to charities with the same heritage. Another example would be Pride Foundation, which is based in Seattle and serves donors and charities seeking to advance the cause of gay, lesbian, bisexual, and transgender individuals.

During the last couple decades, the most notable among charities sponsoring DAFs are the approximately four dozen affiliated with investment firms, such as Fidelity Charitable, Schwab Charitable, and Vanguard Charitable. Some larger banks, such as Bank of America and Wells Fargo, also have related foundations that maintain DAFs. Contributions from donors are facilitated by the fact that they tend to be clients of the for-profit entity in question. The charities maintaining the DAFs affiliated with for-profit entities generally do not favor one type of charity over another with regard to distributions. So long as recipients are public charities, they can have any sort of mission and be located anywhere in the country. Much the same approach to distributions is taken by the National Philanthropic Trust, although it is not affiliated with any investment firm or bank.

Finally, a largely unknown number of run-of-the-mill public charities, such as universities and hospitals, sponsor DAFs. These charities are more likely to require that distributions from DAFs go to charities with missions related to those of the sponsors themselves. Others will mandate that a portion of what is distributed remain with the sponsor, albeit to be used in a manner specified by the advisor to the DAF.

D. Statutory Definition and Related Issues

Only when the Pension Protection Act of 2006 became law did the Internal Revenue Code (IRC) begin to contain any explicit mention of DAFs. They are addressed primarily in IRC Chapter 42, which pertains to "private foundations and certain other tax-exempt organizations." There are two sections applicable solely to DAFs: Sec.4966, which provides for taxes on certain DAF distributions, and Sec. 4967, which imposes taxes on "more than incidental benefits" received by advisors and other persons defined in IRC Sec. 4958(f)(7). More about these taxes can be found later in this paper. At this point, what is most significant about the IRC's treatment of DAFs is the definition of a DAF found in IRC Sec. 4966(d)(2)(A):

(A) IN GENERAL.–Except in subparagraph (B) or (C), the term "donor advised fund" means a fund or account–

(i) which is separately identified by reference to contributions of a donor or donors,

(ii) which is owned and controlled by a sponsoring organization, and

(iii) with respect to which a donor (or any person appointed or designated by such donor) has, or reasonably expects to have, advisory privileges with respect to the distribution or investment of amounts held in such fund or account by reason of the donor's status as a donor.

In simplest terms, the exceptions in subparagraphs (B) and (C) pertain to funds that support a single charitable purpose or a single charitable or governmental entity or that make distributions as determined by a committee, so long as the committee meets various requirements.

Some commentators have identified shortcomings in the statutory definition. One criticism is that IRC Sec. 4966(d)(2)(A)(i) is vague as to what constitutes adequate identification with a donor or donors. While some donors name their DAFs after themselves or their families, other donors, particularly if they seek anonymity, consciously choose names that do not reveal their identities. In addition, the phrase "donor or donors" begs the question of whether there is a limit to the number of donors which, if exceeded, makes the fund or account no longer a DAF. Conversely, even if there are many donors, a smaller "cartel" of them, or perhaps even a single donor, might in fact exert disproportionate influence in the exercise of advisory rights.

Another inadequacy articulated by those who have analyzed IRC Sec. 4966(d)(2)(A) is that subparagraph (iii) allows for a fund or account to be a DAF if an advisor has rights solely with regard to determining the dollar amount to be distributed or invested but not to determining matters such as the timing of a distribution, its specific recipient, or the way in which the recipient is to use the distribution. They contend that the statute should be clarified to provide that a fund or account is a DAF only if advisory rights extend to all relevant matters.

Thus, while the statutory definition of a DAF is mostly consistent with the working definition and characteristics presented at the beginning of this paper, what might be a DAF in one person's eyes might not be DAF in another's eyes. In particular, some DAF sponsors and their supporters might regard as DAFs accounts or funds that fail to meet the statutory definition, although conceivably the opposite could be true as well.

II. DAFs in Context

A. Facts and Figures

DAFs have become extraordinarily popular in the last two decades, and they are likely to remain thus indefinitely. Whereas reports published by the Internal Revenue Service (IRS) are a source of helpful statistics on some gift arrangements of interest to gift planners, such as charitable remainder trusts and pooled income funds, the IRS does not publish statistic as to others, such as charitable gift annuities or retained life estates. Likewise, when it comes to information about DAFs, the IRS has little to offer, aside from the aggregated information each sponsor provides when it files its Form 990 annually. Instead, better sources of information are individual DAF sponsors (recognizing that their information will usually pertain only to their DAFs) and "trade groups" such as the Council on Foundations or regional associations of grant makers. Fortunately, however, each year the National Philanthropic Trust attempts to collect and then publish information on DAFs nationwide. Its most recent report was made available on November 12, 2013. Its next report is expected to be released during the first half of November 2014.

According to the 2013 report (which reflects data effective as of fiscal years ending in 2012 with regard to approximately 1,000 sponsors), 201,631 DAFs held assets worth $45.35 billion. In 2012, a total of $13.71 billion (i.e., 4.3 percent of all charitable giving for the year) was contributed to sponsors to augment existing DAFs or establish new ones. In fact, over 13,000 DAFs were created in 2012. Distributions from DAFs totaled $8.62 billion, which put another way, was 16 percent of the value of DAF assets.

A report issued in June of 2014 by Fidelity Charitable, which sponsors the country's largest DAF program, reflects how quickly such a program can grow. The charity did not even exist until 1991, but it now administers over 63,000 DAFs holding assets of more than $12 billion. Distributions from those DAFs in 2013 totaled more than $2.1 billion.

What, then, accounts for the ongoing popularity of DAFs? Not surprisingly, they meet significant needs on the part of both donors and the many charities that sponsor DAFs. Of course, not everyone in the wider charitable community has high regard for DAFs, at least as they now exist, and their concerns will receive some attention toward the end of this paper. For the time being, however, the appeal of DAFs will be probed in a bit more detail.

B. Why Donors Like DAFs

1. A DAF is a realistic alternative to a private foundation.

True, many DAF donors are not wealthy enough to consider even for a moment establishing their own private foundation. (Note: On the one hand, a private foundation can do direct charitable work in a manner similar to that of a public charity, in which case it is regarded by the IRS as a private *operating* foundation and is effectively treated in some respects as though it were a public charity. The vast majority of private foundations do not conduct any of their own activities but instead by and large simply make grants to public charities. They are regarded by the IRS as private *non-operating* foundations. As used in this paper, “private foundation” refers to this latter type.) Moreover, there is debate about what level of funding is realistic before a donor should begin thinking about establishing a private foundation. Whatever the threshold, a donor weighing whether to set up a private foundation will often identify three options: continue making gifts to charities directly, establish a private foundation, or settle for something in between.

Indeed, there is a continuum that runs from making nothing but unrestricted gifts to public charities at one end to channeling all philanthropy through a private foundation at the other. Points along the continuum include attaching restrictions to gifts, which represents a step away from unrestricted giving, or setting up a supporting organization, which, like a private foundation, is a separate legal entity, albeit one treated by the IRS as a public charity. Somewhere in the middle of the continuum sits the DAF. To many donors, it compares favorably not only with private foundations, but with other choices along the continuum, especially when a donor determines that the *influence* afforded by a DAF is an acceptable substitute for the *control* over investments and distributions afforded by a private foundation. Moreover, this can be so even for a donor with tens of millions of dollars to contribute.

2. Establishing a DAF, as well as maintaining it, is simple and inexpensive and takes relatively little time.

As discussed later in this paper, sponsoring charities vary with regard to the policies applicable to their DAFs. With this understanding, many sponsors will nevertheless allow donors to establish a DAF with fairly small amounts, sometimes as little as $5,000, and will often permit supplemental contributions of even lower amounts. Furthermore, standardizing of the documentation needed to establish a DAF means that this aspect of the process can be completed in less than an hour (including even the time needed by the donor to actually read and comprehend what’s being signed!).

Once a DAF is in existence, the sponsoring charity handles all associated investment management, record keeping, and legal compliance. The charity charges the DAF a fee each year for this administrative work, but such fees are typically quite modest as a percentage of the DAF’s value. Many sponsors, particularly those affiliated with for-profit entities, have streamlined the process of providing recommendations to the point where everything either can – or must – be done online.

By contrast, a donor wishing to establish a private foundation will need to spend several thousand dollars in legal fees to have the constituting documents drawn up and submitted to the IRS. Thereafter, the foundation must bear the expenses associated with all aspects of administration, regardless of whether they are outsourced or handled internally.

3. A DAF can perpetuate a donor's legacy.

Part of the appeal of a private foundation is that the donor can create a way for members of subsequent generations to have a hand in the philanthropic impact the donor seeks to make, both during the balance of the donor's life and beyond. In addition, because the foundation will usually bear the donor's name (or at least the family name), as the decades go by the foundation can be expected not only to have a continuing philanthropic impact, but also to shine – it is hoped – a favorable light upon the donor and his or her progeny, whether such progeny are actively involved with the Foundation or not.

To the extent a sponsoring organization permits a DAF's initial donor to appoint subsequent advisors, the same benefits to be derived by someone who establishes a private foundation can be derived by the initial DAF donor, if only for as long as members of the next generation are living. Some sponsors will even allow the name of a DAF to include the word "foundation," meaning that Mary Smith's DAF could be called "the Mary Smith Foundation" despite the fact that it is not a private foundation.

Note: Some of the same legacy benefits are available when a donor simply establishes a named endowed fund with a public charity. Thus, the importance of legacy objectives in relation to a donor's many other objectives will need to be taken into account in suggesting avenues for the donor to pursue.

4. A DAF can protect the donor's anonymity.

Just as some donors crave having their name attached to their philanthropy, others long to be anonymous. Once again, because the name of a DAF can be anything (within reason) a donor might dream up, all the recipient of a DAF distribution will know is the name of the DAF and the name of the sponsoring charity. The sponsor does not need to report to the IRS, or to anyone else, the identity of any donor to any DAF. This contrasts with what a private foundation must do each year: file with the IRS a Form 990-PF that will be accessible to the public and will set forth the names of individuals involved with the foundation as primary donors and as members of its governing board.

5. With a DAF, a donor can give now but determine later the ultimate charitable beneficiaries of the gift.

Whereas a private foundation must distribute each year five percent of its assets, in any given year a DAF does not have to make any distributions. Obviously, if several years went by without a DAF recommending distribution of so much as a dollar, there would be cause for concern, and some sponsors have policies in place to ensure that distributions are eventually made. Typically, though, a donor will – for tax reasons – contribute to his or her DAF toward the end of one calendar year and then early in the following year recommend significant distributions, perhaps in an amount equal to the contribution made in the immediately preceding year. When this is done, the charitable impact is delayed, but only modestly. Furthermore, the quality of a donor's philanthropy can be enhanced when he or she has the opportunity to do research and make considered decisions without having to worry about a tax deadline.

6. For tax benefits in general, (almost) nothing beats a DAF.

Because DAFs can be sponsored only by public charities, contributions of long-term capital gain property to a sponsoring charity result in a deduction based on the asset's fair market value. With a private foundation, this treatment is available with only one type of long-term capital gain property: publicly-traded securities. Otherwise, the deduction resulting from a gift of long-term capital gain property to a private foundation is going to be a function of the property's cost basis, which might be as low as zero in the case of privately-held stock in a company the donor founded.

Once the amount of a deduction is determined, a donor must determine how much of the deduction can actually be claimed in the year of the gift plus any applicable carry-over years. The deductions associated with gifts of cash and ordinary income property to a public charity can be claimed up to 50 percent of the donor's adjusted gross income (AGI), with the deductions for gifts of long-term capital gain assets eligible to be claimed up to 30 percent of AGI. When such gifts are made to a private foundation, however, the limits are 30 percent of AGI and 20 percent of AGI, respectively.

In addition, a private foundation must pay a tax equal to two percent of its assets each year, although many foundations are able to take advantage of IRC provisions that reduce the tax to one percent. Neither a DAF nor its sponsoring charity needs to pay any such tax. In only one respect are DAFs in the same camp as private foundations: when it has been in effect in years past (and as provided for in legislation pending in both houses of Congress), the so-called IRA charitable rollover option available to certain donors has precluded distributions not only to private foundations and supporting organizations, but also to public charities to the extent the distribution would be added to a DAF.

7. DAFs afford donors a very convenient way to support multiple charities.

In lieu of writing checks or otherwise making individual gifts to individual charities, a donor can make a single gift for his or her DAF and then provide at one time a set of recommendations as to how distributions from the DAF are to be made. This makes less work for the donor and simplifies his or her record keeping for tax purposes. Some sponsors even permit donors or other advisors to make standing recommendations as to distributions they would like to see repeated at set intervals that could stretch over a number of years.

B. Why Sponsoring Charities Like DAFs

1. DAFs help charities fulfill their missions.

Especially for a traditional community foundation, a frequent aspect of the organization's overall mission is something to the effect of "increasing philanthropic activity" within the community served (whether that community is geographic or defined in religious or other social terms). Allowing DAFs to be established increases the philanthropic options offered to the community and arguably increases the flow of charitable dollars available to the community, in that some donors might not have given as much – or given at all – had a DAF not been possible. Despite the fact that their philanthropic impact is more diffuse, sponsoring charities affiliated with for-profit entities are also helping to make charitable giving more appealing to a certain group of potential donors, i.e., the clients of the related for-profit entities. As for those public charities such as educational, health care, or environmental organizations that offer DAFs, dollars are attracted to a particular type of charitable activity in general and, to the extent the sponsoring charity requires that at least some of what is distributed be used "in house," some of the dollars attracted are made available to the sponsor directly.

Of course, depending on its cost structure and the fees it charges DAFs, a sponsor can not only cover the expenses attributable to administering its DAF program with those fees, but actually use any excess to fund other aspects of its operations. This is very much a reality for many traditional community foundations, which often receive little direct financial support that can be used to cover the costs of operating the foundation, whether in general or with respect to activities such as conducting research, convening conversations among stake holders with regard to certain issues facing the community, etc.

2. Offering DAFs can make a charity "competitive."

Although related to the first reason sponsoring charities like DAFs, this second one is ultimately distinct. The notion is that all public charities exist in something of a market for garnering charitable dollars from potential DAF donors. Every such charity is eligible to receive distributions from DAFs maintained by other public charities. In this way, a charity garners some of the market's dollars indirectly. If instead the same charity is willing and able to offer DAFs to donors on its own, it stands to garner some of the market's dollars directly, even as it also hopes to garner some indirect dollars.

In essence, each sponsor is trying to exploit perceived advantages its DAFs may have over DAFs sponsored by other public charities in the minds of certain donors. In making its case, a sponsor is effectively saying something like, "If you establish a DAF with our organization, you will be [pick one: contributing to the welfare of the Anytown metropolitan area/serving God with your earthly wealth/honoring your alma mater/stretching your charitable dollars as far as possible by virtue of our low fee structure]." Different donors will have different motivations and objectives, but a given potential DAF donor with an affinity for a given charity the donor knows offers DAFs may be somewhat more inclined not to establish a DAF elsewhere.

III. Establishing and Maintaining a DAF

A. What's Mandatory

As noted earlier in this paper, there are certain taxes that apply to a DAF as well as to the donor and other parties that have a relationship to the DAF. Fortunately, all such taxes can be avoided if proper care is taken.

1. Taxable Distributions

IRC Sec. 4966(c) defines a taxable distribution as a DAF distribution made to an individual or to any other "person" (i.e., an entity) if the distribution is not for a charitable purpose (as defined in IRC Sec. 170(c)(2)(B)) or if the sponsor does not exercise "expenditure responsibility" with respect to the distribution. The elements of expenditure responsibility are set forth in IRC Sec. 4945(h) and basically require that a charity making a distribution monitor how the recipient uses the money.

If a taxable distribution is made, the sponsor will owe a tax of 20 percent of the amount distributed. Any "fund manager" that agrees to the making of a taxable distribution will owe a tax of five percent of the amount distributed. Because a fund manager might be an officer, a director, a trustee, or possibly even an employee of the sponsor, it is quite possible that multiple individuals will be responsible on a joint-and-several basis for paying the five-percent tax, although the total amount of the tax paid by all relevant fund managers together cannot exceed $10,000.

2. Prohibited Benefits

If a DAF donor, advisor, or "related person" (as defined in IRC 4958(f)(7), a "related person" includes not only certain family members identified there and in IRC 4946(d), but also potentially numerous individuals involved in operating the DAF sponsor or certain other entities) receives, directly or indirectly, "more than incidental benefit" from a DAF distribution made as the result of advice given by the individual, IRC Sec. 4947(a)(1) imposes on such person a tax of 125 percent of the value of the benefit. In addition, IRC Sec. 4967(a)(1) imposes a tax of 10 percent of the benefit on any fund manager who knew the benefit would be conferred but agreed to the distribution anyway. As with the prohibited distributions tax, there is joint-and-several liability and a $10,000 limit on the tax paid by fund managers as a group.

In trying to determine what constitutes a benefit that is more than incidental, it can be helpful to refer to IRC Sec. 170(a), along with the related Treasury Regulations and case law, which together describe what sorts of benefits do and do not require a donor who makes any sort of charitable gift to reduce his or her deduction if the gift resulted in a benefit provided by the charity. Making the necessary determination is entailed in potentially numerous circumstances but two in particular.

One is the extent to which, if at all, it is permissible for a distribution from a DAF to be part of a "bifurcated" transaction. This issue will arise if in connection with a distribution the donor becomes entitled to attend an event put on by the recipient charity. Assuming the price for the event is partly a charitable contribution and partly to cover the cost attendance at the event, if the DAF distribution covered both parts, the cost of attendance would constitute more than an incidental benefit. Nevertheless, some feel it is permissible for the donor to recommend a DAF distribution equal to the amount of the charitable contribution, with the donor then paying personally the amount associated with the cost of his or her attendance. Others take the more conservative approach that this should never be done because it is too much like what would clearly be an impermissible instance of self-dealing in the case of a distribution from a private foundation.

The other significant way in which a taxable distribution might occur is in the context of a pledge the donor has made to a public charity if the donor then recommends a DAF distribution in an amount that fulfills all or a portion of the pledge. Much depends on whether the pledge is legally binding on the donor, for if it is not, then the IRS will be unlikely to prevail in imposing the tax. If, however, the pledge is binding and if the IRS analogizes satisfaction of the pledge by means of a DAF distribution as being tantamount to what would clearly be an impermissible instance of self-dealing were the distribution made from a private foundation, the DAF taxable distribution tax might be applicable.

3. Excess Business Holdings and Excess Benefit Transactions

Part of what the Pension Protection Act of 2006 accomplished was to extend to DAFs the imposition of taxes imposed by IRC Secs. 4943 and 4958 that were already applicable to private foundations. The former concerns investments a DAF continues to hold beyond a particular period of time (depending on various conditions) in corporations or other business ventures in which the donor or any of a number of other persons related to the donor own more than a 20-percent or a 35-percent (again, pursuant to various conditions) controlling interest. If ownership of more than the applicable percentage continues for more than the applicable period of years, a tax is imposed at a rate as low as 10 percent or as high as 200 percent of the amount of the excess.

Under Sec. 4958, a separate tax applies to an excess benefit (which is to be distinguished from an excess distribution, discussed earlier in this paper) received by a DAF donor or certain other disqualified persons in connection with each of the following types of transactions involving the DAF: grants, loans, instances of compensation, or other similar payments. It can be imposed not only on the donor or other disqualified person (in which case the rate can be as low as 25 percent of the excess or as high as 200 percent), but also, with some exceptions, on any of various individuals involved in operating the sponsoring organization.

4. Miscellaneous Issues

Taxes can also apply in connection with distributions from a DAF to certain supporting organizations, but such scenarios are relatively uncommon and therefore will not be addressed in this paper. Finally, pursuant to IRC 508(c), a sponsoring charity must notify the IRS that it sponsors one or more DAFs and provide information about how it will operate any DAF it sponsors. Such operational considerations include some of those covered in the following discussion.

B. What's Optional

A sponsoring charity has quite a bit of discretion in the requirements it establishes for DAFs. These matters of policy include:

- The types of assets that may be contributed for a DAF
- The minimum amount needed to establish a DAF
- The minimum amount of any subsequent contribution for a DAF
- The minimum amount, if any, that must remain in the DAF at any given time to keep the DAF from being terminated
- Fees and how they will be charged to the DAF
- The minimum amount of a distribution
- Requirements, if any, the recipient of a distribution must meet in addition to being a public charity
- When and how recommendations regarding distributions (or investments, if applicable) are to be made, along with how recommendations will be handled once received
- The circumstances under which a DAF will be terminated, as well as how whatever may remain in the DAF upon termination will be used
- Documentation regarding any of the matters listed above

Two additional matters merit a bit of discussion. One is how much of the DAF the sponsor will make available for distribution at any point during the DAF's existence. Most DAFs are established with the advisors having the ability to recommend at any time that the entire value of the DAF be distributed to one or more public charities (recognizing, as noted in the fourth bullet point above, that this may cause the DAF to terminate). That being said, some sponsors will allow – or even require – a DAF to be endowed, meaning that the advisors may make recommendations only as to whatever portion of the DAF the sponsor designates as being available for distribution each year.

The other matter is the extent to which, if at all, advisors other than the donor will be permitted. Some sponsors will permit additional or successor advisors only if such persons have a certain relationship to the donor. Examples would include no one beyond the donor's children (if any) or grandchildren (if any). Also, as noted earlier, if the sponsor allows more than one person at a time to be an advisor, it may require that the advisors as a group designate a spokesperson. Interestingly, some sponsors permit what are essentially self-perpetuating advisory rights, meaning that whoever holds those rights at a given time can designate a successor to those rights, although perhaps potential successors must meet certain requirements established by the sponsor.

IV. The Intersection of DAFs with Planned Giving

A. A DAF Is Not a Type of Planned Gift

A DAF is, in a sense, a charitable giving vehicle or tool, but it is not a gift structure in the way that planned giving arrangements such as bequests, charitable gift annuities, and charitable remainder trusts are. Furthermore, while most gifts to DAFs are structured as outright transfers of assets (some of which, such as real estate, are transferred only after significant planning with regard to the gift has occurred), every other type of planned giving structure can be used to establish or augment a DAF.

Once again, technically every gift should be made *to* the sponsoring charity *for* the DAF, as the DAF itself is merely a component of the sponsoring charity. This has implications for how the charitable beneficiary of a planned gift is identified, whether in connection with a bequest, a non-probate asset beneficiary designation, or a charitable trust. Sometimes it will be advisable for the direction that a planned gift be used to fund a DAF to be included not in the gift instrument itself, but in a separate document that references the gift arrangement. For example, a donor's will might provide simply for a bequest to the sponsoring charity, with the donor and the sponsoring charity executing a separate agreement indicating that the sponsor will add the bequest to the DAF.

Of course, in connection with any deferred gift used to establish a DAF, the donor and the charity will need to ensure that by the time the gift matures, it will remain an appropriate way to establish the DAF. Likewise, if by the time the gift matures the donor is no longer living, the sponsor will obviously need to permit persons other than the donor to be advisors.

One gift structure in particular, the charitable gift annuity, deserves a bit of special attention. This structure will not be an option unless the sponsoring charity issues gift annuities. Even if the charity does issue them, it may not permit them to be used to establish or augment a DAF. Finally, assets in a DAF cannot be used to establish a gift annuity with the sponsor or with any other charity.

B. The Role of the Institutional Gift Planners

A gift planner who works for a charity that offers DAFs mostly just needs to make sure donors know about this option as they do their charitable planning. Likewise, he or she should be familiar with all of the organization's policies regarding DAFs, as well as the rationales for those policies. If a donor complains that the charity's minimum gift amount is too high, its fees too high, or its options for naming successor advisors too strict, being conversant on these and related issues will enable the gift planner to provide the donor with an explanation and perhaps nurture a conversation that will eventually lead the donor to change his or her thinking. Moreover, the gift planner should make sure he or she has good working relationships with everyone at the charity who has anything to do with administering DAFs so that they can be brought into conversations with donors as necessary and so that if the gift planner has any concerns about how the DAF program is being operated, he or she can speak with the appropriate person.

If a gift planner's charity does not offer DAFs, he or she will still need to be sure that those in the organization who acknowledge gifts understand that DAF distributions come from the sponsoring charity, not from the donor or some other advisor. This does not preclude the gift planner's charity from according such individuals "soft credit" for distributions received from DAFs and recognizing such persons accordingly. Nevertheless, care must be taken in expressing appreciation. For example, reference should be made to the "distribution you recommended," rather than to the "gift you made." Similarly, to the extent relevant colleagues of the gift planner understand potential situations in which the charity might inadvertently provide a DAF donor, advisor, etc., with a prohibited benefit, he or she can help ensure that the charity will be vigilant in preventing such benefits from being provided.

Ideally, a charity that does not offer DAFs will at least be proactive in learning which supporters have DAFs (and with which sponsoring charities) and then work with those donors to be sure they consider the charity when recommending distributions and – perhaps more importantly – when designating which charities will receive any assets remaining in their DAFs when those DAFs terminate. The identities of such donors may not be easy to learn, but if a charity can at least position itself as “DAF-friendly,” it will be more likely to gather useful information.

Despite the fact that not all charities should offer DAFs and very few actually do offer them, a gift planner with a charity that does not offer them might want to initiate a discussion of whether doing so would be feasible and beneficial. Again, if the charity has consciously (as well as conscientiously) confronted the question, a gift planner will be better able to respond to a donor who inquires as to why the charity does not offer DAFs.

V. The Future of DAFs

Likely because DAFs are so popular (which, in a very real way, is the same as saying “because so much money is involved”), they are the subject of scrutiny and criticism both within the federal government and among charities, donors, and those who analyze and opine on the social and fiscal health of our country. The primary concern is the “give now, grant later” aspect of DAFs cited earlier in this paper as one of the characteristics that appeals to donors. Indeed, sponsoring charities often tout this feature when encouraging donors to consider establishing DAFs.

The critics claim that because the tax deduction associated with a gift for a DAF is received by the donor as soon as the gift is made, allowing the charitable impact of the gift to be delayed indefinitely (with fees charged against the DAF all the while) undermines the tax policy of encouraging philanthropy by making it, in effect, less expensive. They are especially concerned that private foundations sometimes satisfy their five-percent distribution requirement by having those distributions be made to DAFs, with foundation board members thereafter being free to recommend DAF distributions at their leisure.

Of course, the delay between a donor’s receipt of an income tax charitable deduction and the charitable impact of the gift is not limited to DAFs and is nothing new. This is what happens in the case of a charitable remainder trust. It is also what happens when a donor makes a current gift to a charity to establish an endowment, although usually no later than a year or two after the gift is made, the endowment begins making distributions, albeit distributions of only a fraction of the amount contributed. Combining a charitable remainder trust with an endowment funded with what remains in the trust upon termination is a further application of the same principle.

While egregious abuses of the give now, grant later phenomenon can be cited, for the most part DAF money is flowing out to other charities in the form of distributions at what some consider to be an acceptable rate. Fidelity Charitable reports that less than one percent of its DAFs have made no distribution for seven years or more. Moreover, even private foundations often distribute more than five percent of their assets, as shown in statistics gathered by Foundation Source, a company that provides administrative services for private foundations.

In short, some see a problem and others don’t. Nevertheless, one should not underestimate the ability of Congress, even the largely dysfunctional one currently in session, to take sudden farreaching, long-lasting action. This is essentially what occurred with passage of the Pension Protection Act of 2006. Many observers were aware that the IRS and key members of Congress were troubled by the fact that DAFs were essentially unregulated, but the legislation actually enacted took many by surprise.

The DAF provisions added to the IRC in 2006 could be regarded as simply a first round of regulatory action. Next might well come time limits for distributions attributable to gifts added to a DAF in prior years: for example, all of a particular gift must be distributed within X years. The record keeping associated with meeting such a requirement could be onerous, and, as noted above, the requirement could have little effect on what actually happens, if it can be shown that substantially all gift amounts are already being distributed within X years anyway. Another, more extreme approach would be to require all DAFs (query: even those established as endowments?) to terminate within Y years, thereupon distributing any remaining assets to one or more public charities.

VI. Concluding Thoughts

Understanding DAFs and the role they play in the interactions between donors and charities (and the IRS) is helpful to gift planners, although not because such an understanding gives them another arrow for their quivers. Rather, it encourages them to think about how one or more existing arrows might be sharpened and then aimed more truly. For example, a gift planner could do something as simple as include in marketing materials dealing with beneficiary designations a bit of information prompting donors with DAFs to think about the possibility of arranging for distributions from their DAFs to the charity, whether upon death or – even better – during life. In addition, as a gift planner works with donors, he or she should make it a point to learn which of them have DAFs, what they think of their DAFs, what they think of the sponsoring charities, and how they might make use of their DAFs going forward. In summary, a basic command of DAFs will help gift planners meet donors where they are and then go from there.

Appendix

Successor Election page from DAF Donor Application

5. Successor Election

For more details, refer to the Program Circular, available online at FidelityCharitable.org.

Account Holders can name individuals (Individual Account Holders) to succeed them on the Giving Account and/or may recommend IRS-qualified public charities (Charitable Organizations) to receive part or all of the balance and/or may recommend the Endowed Giving Program. If no successor is elected upon notification of the death of the last remaining Account Holder, the Trustees will redeem the remaining units in the Giving Account and distribute the proceeds to the Trustees' Philanthropy Fund. You may specify more than one successor for each option (attach additional sheets), and **you may choose any combination of the two successor options. (Total successor allocation among the two options must total 100%.)**

A. Individual Account Holder *Attach additional sheets if more than one*

% of Giving Account: %

First Name	M.I.	Last Name	Social Security or Taxpayer ID Number

Date of Birth MM DD YYYY	Email	Relationship to Account Holder

Legal/Residential Address

Provide the address used for tax reporting. Cannot be a P.O. Box, mail drop, or c/o.

Address			
City	State/Province	ZIP/Postal Code	Country

Citizenship

Check one. ☐ U.S. citizen ☐ U.S. resident alien

B. Charitable Organization *Attach additional sheets if more than one*

% of Giving Account: %

Organization Name	Federal Taxpayer ID Number *if known*

Phone

Mailing Address

Address			
City	State/Province	ZIP/Postal Code	Country

COMBINED TOTAL OF SECTIONS A AND B MUST EQUAL Total 1 0 0 %

Successor Charitable Organizations are reviewed (1) at initial recommendation, (2) upon the death of the last remaining Account Holder, and (3) before every recommended or scheduled grant distribution.

Endowed Giving Program *$100,000 minimum*

Account Holders who wish to support charitable organizations beyond their lifetime by providing ongoing grants to up to six (6) charitable beneficiaries may enroll in the Endowed Giving Program. A $100,000 minimum Giving Account balance is required at activation, which occurs at the death of the last remaining Account Holder. Please refer to the Program Circular and the Endowed Giving Program Enrollment Form found online at **FidelityCharitable.org** for eligibility and further details.

DAF Grant Recommendation Form (page 1)

FIDELITY Charitable® Make more of a difference

Questions? Go to FidelityCharitable.org or call 1-800-952-4438.

Grant Recommendation Form

If you prefer to complete your grant recommendation online, visit **FidelityCharitable.org**.

For grant recommendation guidelines, refer to the *Fidelity Charitable® Policy Guidelines: Program Circular*. Fidelity Charitable® will not forward any enclosures with grants.

Please type or print clearly in CAPITAL letters and black ink. If you need more room for information or signatures, make a copy of the relevant page.

1. Giving Account® Name and Number

Giving Account® Name	Giving Account Number

2. Recommended Recipient Charity

Before making your recommendation, please review the certifications in Section 7.

Have you previously recommended a grant to this organization from Fidelity Charitable?

Check one. ☐ Yes ☐ No

If you are unsure of the organization's official name and/or mailing address, visit FidelityCharitable.org/guidestar.

Fidelity Charitable may contact the recipient charity.

Organization's Official Name			Federal Tax ID Number
Contact Name			Phone
Address			
City	State/Province	ZIP/Postal Code	Country

Recommended Purpose

Is there a recommended purpose for this gift? If yes, describe (e.g., annual fund, in memory of, to honor, etc.). If the purpose of your grant is to honor a loved one and you wish to notify the family of the honoree, include the name and address of the person to be notified.

Details

3. Grant Amount *Minimum of $50*

Grant Amount	Please also write out the amount of the grant.
$.	

4. Indicate Where the Grant Should Come From

Check one box only from Investment Pool Balances or Advisor Managed Charitable Balance.

Investment Pool Balances

Recommend the pool(s) from which this grant should be drawn (in whole dollars). If you do not recommend a pool(s), Fidelity Charitable will disburse funds proportionately from all pools with balances.

☐ Disburse funds proportionately based on current allocation.

☐ Disburse funds evenly among current allocation (example: 33%, 33%, 34%).

☐ Other

Write in request

Advisor Managed Charitable Balance

If you are participating in the Charitable Investment Advisor Program, you may select to have this grant drawn from the advisor managed charitable balance within your Giving Account.

☐ Allocate funds from advisor managed charitable balance.

Form continues on next page. ▶▶

DAF Grant Recommendation Form (page 2)

5. Acknowledgement

Grants to charities are accompanied by a letter that includes the name(s) of the individual(s) recommending the grant so the charity may thank them. Please check only ONE box to indicate who should be acknowledged for the grant.

Check one. ☐ The individual(s) named on the Giving Account ☐ The name of the Giving Account only ☐ Anonymous

☐ The following individual(s) in lieu of those named on the Giving Account:

Name(s)			
Address			
City	State/Province	ZIP/Postal Code	Country

6. Timing of Grant

Check one. ☐ As soon as possible ☐ Issue this grant on a specific date Date *MM DD YYYY*

☐ Issue this grant on a scheduled/recurring basis. *The grant amount in Section 3 will be sent for each scheduled occurrence.*

Frequency: Monthly, Quarterly, Semiannually, or Annually.

Frequency	Start Date *MM DD YYYY*	End Date *MM DD YYYY*
☐ M ☐ Q ☐ S ☐ A		

Your grant recommendation is nonbinding and is subject to review and approval by Fidelity Charitable. If approved, the grant will generally be made within 10 business days; however, this process may take longer. Confirmation that the grant was approved and sent will be mailed or emailed to the Primary Account Holder once the grant has been issued.

7. Signature

By signing below, you:

- Certify that neither you nor anyone else will receive any impermissible benefit (e.g., tuition, membership fees with more than incidental benefits, dues, admission to charitable or other event, goods bought at auction, etc.) from the recommended charitable organization from this grant, if distributed. Examples of permissible benefits include benefits that are not more than incidental, such as free or discounted admission, free or discounted parking, token logo-bearing key chains, caps, T-shirts, and calendars.
- Certify that this grant will not fulfill all or a portion of a pledge to the charitable organization.
- Acknowledge that this grant does not entitle you or any other person to an income tax charitable deduction, because the donor was eligible to take a deduction at the time of the contribution(s) to Fidelity Charitable. Any tax receipt that may be received from the recommended charity will be disregarded.
- Certify that if the grant you are recommending is for a supporting organization, neither you nor any other Account Holders on the Giving Account, nor any parties related to you or to any other Account Holders on the Giving Account, directly or indirectly control any supported organization of the recommended grant recipient. Supporting organizations are 501(c)(3) public charities that typically carry out one or more functions of their supported public charity (for example, an alumni association that fundraises for a university, or a parent-teacher association that performs certain functions at a school).
- Acknowledge that you have read the Grant Recommendation Guidelines in the current *Fidelity Charitable® Policy Guidelines: Program Circular.*

Account Holder Name	Phone Number
Account Holder Signature	Date *MM DD YYYY*
SIGN	

Sign the form and send or fax to Fidelity Charitable.
Questions? Go to FidelityCharitable.org or call 1-800-952-4438.
Fax the form to: 1-877-665-4274

Regular mail
Fidelity Charitable
P.O. Box 770001
Cincinnati, OH 45277-0053

Overnight mail
Fidelity Charitable
100 Crosby Parkway
Mail zone KC1D-FCS
Covington, KY 41015-9325

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