Advantages of a Donor-Advised Fund as the Charitable Component of your Financial Strategy

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For those who want to give back, one of the first decisions that must be made is to determine what philanthropic tools are best suited for one's individual charitable goals and financial circumstances. One philanthropic vehicle that has skyrocketed in popularity over the past decade, is the donor-advised fund, or DAF. For nearly a century, DAFs have been offered by local community foundations. More recently, DAFs have become available through the charitable extension of wealth management organizations such as Peak Trust Company's Donor-Advised Fund (PTDAF).

What is a DAF?

A DAF is an account within a charitable organization. To create a DAF, a donor contributes personal assets to the account, where the contribution can be invested and grow tax-free until a grant is made to a qualified charity. Once contributions are made into the DAF, they become assets of the DAF and no longer belong to the donor. As a result, all contributions qualify for tax deduction in the year contributed. DAFs allow individuals to establish a fund and advise how and when the charitable organization managing the DAF should distribute grants from that fund.

A DAF can be thought of as a marriage between a private foundation and a mutual fund. Where a DAF differs from a private foundation is in its financial and administrative efficiency for the donor. When a private foundation is created, a new entity is formed, requiring extensive legal guidance to ensure compliance with the stringent IRS rules. With a DAF, the individual setting up the DAF is simply opening a fund with an already-established entity (i.e., a managing charitable organization).

The advantages that DAFs offer over private foundations have contributed to their growing appeal over the last few years. Due to their low set-up and ongoing maintenance costs compared to establishing and running a private foundation, DAFs have become increasingly accessible to a larger donor base. Additionally, most DAFs can receive a broad range of asset types, including cash, publicly-traded securities, real estate, as well as other financial and physical assets. Any asset accepted by the managing charitable organization may be contributed to the DAF, which can help donors leverage the best income tax deduction opportunities.

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Efficiency and Privacy

DAFs provide professional management and philanthropic distribution for significantly less than the cost of establishing and managing a private foundation. A DAF can be quickly established at a managing charitable organization by completing an application and making an initial contribution. By comparison, private foundations can take months to establish and require significant time and financial investment, largely due to legal fees.

Once established, the managing charitable organization handles all administrative work, including investment management, recordkeeping, tax receipting, and grant administration. This allows the donor to focus on their charitable goals rather than the operational components. A private foundation, by contrast, must hire staff, contract advisors to manage administration and tax matters, or be managed solely by its trustees or board. They must also form a board, hold board meetings and record minutes, file state and federal tax returns, and perform other governance duties, generally at a significant expense.

A DAF is a great option for those who desire to make anonymous charitable donations. DAF grants are made in the name of the managing charitable organization or the individual fund name, which can protect the identities and personal information of the underlying donors. On the other hand, private foundations are required to maintain an annual publicly-available filing (form 990-F) that discloses board members, grant recipients, and other information. This is not the case for DAFs, which are the only charitable giving vehicle that allow donors to make grants 100% anonymously.

Tax Advantages

Contributions to a DAF are tax deductible and offer the maximum benefits allowed by the Internal Revenue Code. Since a DAF is considered a public charity, a taxpayer can deduct a donation of up to 60% of adjusted gross income (AGI). For individual contributions to a private foundation, the tax deduction limit is only 30% of AGI. This creates a meaningful planning opportunity in years where a taxpayer has a windfall and experiences a significant increase in taxable income. Contributing to a DAF can help mitigate the tax burden of that one-time event.

With the recently increased deduction of $12,000 for individuals or $24,000 for a married couple, DAFs are a leverageable giving vehicle. It may be advantageous to bunch deductions in only certain years to allow the taxpayer to

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obtain the maximum deduction during those targeted years, where exceeding the standard deduction is desired. This would also cover any planned giving need for other years in which the taxpayer plans to take the standardized deduction. Having already taken advantage of the full deduction of contributions to the DAF, taxpayers can then request that grants be made to the charities of their choice, regardless of whether they plan to itemize deductions later.

The tax deductibility of certain contributions made to a DAF can also be leveraged. This is achieved by contributing highly-appreciated assets. The deduction on low cost-basis property contributed to a DAF is determined by its current value, not its cost. Because of this, when giving a highly-appreciated asset, the donor receives a double benefit: a larger deduction and no capital gain on the property's appreciation.

For example, if a donor has 100 shares of low-cost but highly-appreciated stock and decides to donate this asset to a local soup kitchen, then the donor must sell the stock, pay capital gains tax on the sale, and donate the remainder. While the donor still receives a deduction for this contribution, they could have instead used a DAF to take an immediate deduction for the full market value of the stock at the time of donation. In this scenario, the donor would contribute the stock directly to the DAF and request that a grant be made to the soup kitchen in the amount of the value of the donated stock. The managing organization would sell the stock—exempt from tax—and make the grant to the soup kitchen from the DAF. The donor would receive a deduction for the full market value of the asset and not pay any tax on the appreciation in the asset's value.

Estate and Legacy Planning

DAFs can provide useful estate-planning opportunities. When assets are contributed to a DAF, they permanently leave one's estate, making those assets no longer subject to estate taxes. With the lifetime exclusion currently at more than $11 million, this offers individuals the flexibility to use a DAF in their planning. Donors can use their annual gift tax exclusion to make contributions to their fund. This means that a married couple can each contribute a combined total of $30,000 every year. Since assets in a DAF are allowed to grow tax-free indefinitely, this can create a philanthropic legacy that will last well beyond the donor's generation.

The donor's heirs will be equipped to direct gifts throughout their lifetimes as well

For families with charitable intent and a desire to pass that value on to future generations, a DAF provides the opportunity for both donors and their descendants to be involved in the decision-making process of grantmaking. As its name implies, a donor-advised fund gives the donor the ability to advise the managing charitable organization on how to gift the money in the fund. Because a well-funded DAF will often outlive its benefactor, involving younger generations in the process can create a legacy of continued philanthropy through apprenticeship. As a result, the donor's heirs will be equipped to direct gifts throughout their lifetimes as well. While contributions made to a DAF provide an immediate benefit in the form of a current year tax deduction, they can also provide long-term gifting opportunities.

Considering the Options

There are many options for continuous philanthropic planning to suit individual needs and maximize impact. When determining the right structure for a donor's philanthropic priorities, assessing the purpose, operating costs, and tax considerations, will help guide donors in the right direction. In terms of comprehensive financial planning, there are few strategies that provide the same benefits with tax deductions, donation types, or charity selections. Including a DAF can be an excellent way for a donor carry out their philanthropic intent as a component of their unique financial planning objectives.

	Donor-Advised Funds	Private Foundations
Start-Up Time	Immediate	May vary from several weeks to several months
Start-Up Costs	None	Legal fees and other start up costs are tipically substantial
Ongoing Administrative and Management Fees	Peak Trust DAF fees begin at 70 basis points (0.70%), or less depending on the fund size. Most funds do not exceed 85 basis points (0.85%).	Can be in the range of 250-400 basis points (2.5% - 4% pear year)
Tax deduction limits for gifts of cash	60% of adjusted gross income	30% of adjusted gross income
Tax deduction limits for gifts of stock or real property	30% of adjusted gross income	20% of adjusted gross income
Valuation of gifts	Fair market value	Fair market value for publicly-traded stock, cost basis for all other gifts, including gifts of closely-held stock or real property
Required Grant Distribution	None	Must expend 5% of net asset value annually, regardless of how much the assets earn
Excise Taxes	None	1% to 2% of net investment income annually
Privacy	Names of individual donors can be kept confidential if desired, and grants can be made anonymously.	Must file detailed and public tax returns on grants, investment fees, trustee or director names, staff salaries, etc.
Administrative Responsibilities	Recommend grants to favorite charitable causes	Manage assets, keep records, select charities, administer grants, file state and federal tax returns, maintain board minutes, etc.
Control of Assets	When a gift is made to a DAF it is irrevocable and under the ultimate control of the DAF's managing organization. The donor serves in an advisory capacity in determining which charities the DAF will support.	When a foundation is established, the founder(s) may appoint a board of directors or trustees which may include the founder(s) and other family members. If the board chooses, legal and financial control of the foundation and its assets can remain with the family in perpetuity.

For more information please visit the Peak Trust Company website at www.peaktrust.com or contact one of our knowledgeable team members at (844) 391-2789.

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