Benefits of a Donor Advised Fund

Wealth Management Blog

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Each year around the end of March, I spend at least half a day tracking down my charitable contribution receipts in the hope of increasing my tax refund with a charitable deduction. There are plenty of tools to help me keep track of the donations, but inevitably I find myself hunting through stacks of paper and a year of emails for records of the donations I gave to charities. If you experience similar frustration at tax time you may want to use a donor advised fund for charitable giving instead of making individual gifts. Donor advised funds can make keeping track of gifts much easier and provide financial benefits.

Donor advised funds are charitable giving vehicles that have been growing in popularity in recent years. They can be a cost and time-efficient way to give to 501(c)(3) public charities, often a goal of many Americans for tax-savings and philanthropic reasons. According to the National Philanthropic Trust's 2016 Donor-Advised Report,[1] total assets in donor advised funds passed $78 billion at the end of 2015. Additionally, over $14 billion was given to charities from donor-advised funds in 2015.

A. How does it work?

Donor-advised funds are 501(c)(3) public charities themselves. An individual sets up an account with a provider, like Fidelity Charitable, American Endowment Foundation, or the local Community Foundation of Greater Birmingham. The individual contributes cash, appreciated securities, and less frequently, more complex assets such as real estate or business interests. The donor benefits from a tax deduction in the year the gift was made.

After funding the account, the individual is able to recommend grants to public charities, making gifts as usual. The individual keeps up only with the donation receipts to the donor advised fund and has the flexibility to make charitable grants at the time and in the amount desired. Gifts can also be made anonymously or by identifying the original donor directing the gift.

It is important to remember that the gift to the donor advised fund is irrevocable.

B. What are the benefits?

- Tax Savings. The structure of a donor advised fund generally makes it very easy to donate appreciated securities. Consider a person who bought and held 100 shares of Apple, Inc. stock for the last ten years.[2] The ~650% gain would be taxed as a long term capital gain if sold. Table 1 below shows how donating the appreciated stock saves an investor in the highest marginal tax and capital gains rates (including the Medicare surcharge) ~$4,200 in taxes and results in an additional ~$3,000 being available to give to the charity.

Table 1: Charitable Gift Comparison

	Donate Securities	Sell Securities, Donate Cash	*Difference*
Purchase Price	2,000	2,000	
Fair Market Value at Sale	15,000	15,000	
Long Term Capital Gains Tax Paid (23.5%)	-	3,055	
Charitable Contribution / Deduction	15,000	11,945	
Net Tax Savings (39.6%)	5,940	1,675	*4,265*
Total to Charity	15,000	11,945	*3,055*

- Tax Planning. Having a separate vehicle for charitable donations allows for efficient tax planning. For example, in years of higher income, one could make a larger contribution to the fund to offset income and can spread eventual grants to specific charities over multiple years. Furthermore, some providers can accept complex assets like private equity, private company stock, or oil & gas royalty interests, which can offer additional financial planning options.

- Cost Efficiency. Donor advised funds can be used in place of setting up a private foundation meant for leaving a longer term charitable legacy. While there are benefits to both structures, a donor advised fund is typically easier and cheaper to administer. Funds can be set up with multiple and successor account holders, which accomplishes legacy giving goals. A donor advised fund cannot make a transfer to a private foundation, although it can receive gifts from private foundations.

- Investment of Funds. Gifts to a donor advised fund can also be invested for long-term growth and grow tax-free, which also enhances the ability to leave a charitable legacy. There is no requirement to distribute minimum percentages of the fund in any year.

- Foster a Family Culture of Giving. Setting up a family fund can be an easy way to foster discussions with children of all ages and to involve them in decision making. Extended families can also come together to make charitable grants.

Depending on your or your family's tax planning or charitable goals, a donor advised fund can be a helpful tool to maximize your financial assets and accomplish more complicated planning goals while easing administrative burdens.

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Important Note: This document is intended to raise issues for consideration by friends and clients. Assumptions are made based on current tax code which may change. Consequently, readers are encouraged to seek competent tax counsel and not rely solely on any of the statements made herein.

Any advice concerning U.S. federal tax issues contained in this communication is not intended or written to be used for the purpose of (1) avoiding penalties under the Internal Revenue Code or (2) promoting, marketing or recommending to another party any transaction or tax-related matter addressed herein.

[1] https://www.nptrust.org/daf-report/index.html
[2] Assumed purchase price on 7/30/2007 of $20 and sale price of $150 on 7/27/2017.