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## TAXES

# Donor-Advised Funds Offer a Charitable Way to Harvest a Tax Break

The number of DAFs has nearly tripled to 1.3 million since Congress approved the Tax Cuts and Jobs Act in 2017.

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*By Andrew Maykuth, The Philadelphia Inquirer (TNS)*

After charities experienced a gangbuster year in 2021 with record donations, philanthropic experts say that charitable giving is likely to plateau or decline this

year after the stock market's prolonged downturn.

Even though the generosity of Americans may be diminished somewhat by the market's misfortunes this year, an increasingly popular tool for maximizing the tax benefits from charitable deductions is still attracting interest.

The number of donor-advised funds (DAFs), the charitable vehicles sometimes referred to as a "poor man's foundation," has nearly tripled to 1.3 million since Congress approved the Tax Cuts and Jobs Act in 2017, which dramatically reduced the need for many taxpayers to itemize their annual returns.

Americans contributed \$72.7 billion to DAFs in 2021, up 47% from the previous year, according to the National Philanthropic Trust (NPT), a Jenkintown, PA charity that sponsors the accounts and also tracks the national DAF sector.

DAFs contained \$234.1 billion in assets at the end of 2021 and made \$45.7 billion in grants to individual charities last year, said Eileen R. Heisman, president of the trust, which analyzes the public tax filings of about 1,000 fund sponsors in its annual DAF Report.

"These were the most dramatic increases we've had in years," said Heisman, who said her initial reaction to the tally was disbelief until the researchers assured her the figures had been double-checked.

Heisman said many donors were induced to donate more of their wealth in 2021 after the prolonged bull market had increased their exposure to capital gains taxes

Is a DAF right for your charitable giving? Here's what you need to know about the funds.

## **What are donor-advised funds (DAFs)?**

DAFs are a way for taxpayers of any means to group charitable contributions into a single year to reap tax benefits, and then to distribute the funds to their favorite charities over time.

## **What are the benefits of creating a DAF?**

DAFs are a convenient method for philanthropists to donate appreciated stock shares, or other assets. The donor receives a tax deduction for the full value of the asset while avoiding capital gains tax on the increase in the assets' value.

“People were sitting on highly appreciated assets, and a lot of advisers are telling them [a DAF] is a really easy tool, you can make the gifts relatively easily,” Heisman said. “You can have years of grant-making out of a single gift in one year where you’ve had an abundance of capital gain.”

DAFs became more attractive after the new federal tax law went into effect, dramatically increasing the standard deduction for most taxpayers and putting limits on some itemized deductions, such as state and local taxes and mortgage interest. Charitable contributions are still deductible, and the new tax law created an incentive for taxpayers to consider batching or “bundling” deductible expenses in a single year, so those count toward reducing your taxes.

For some donors who have DAFs, the tax benefits of the funds are of secondary importance. A DAF offers a convenient and easy way to manage a family’s philanthropy, said Janet Wischnia, an owner and managing partner at Thomaston Mills, a family-owned Wyncote firm that manufactures bedding and linens.

Wischnia is no newcomer to DAFs. Her father, Jerome Zaslowsky, set up a fund at National Philanthropic Trust more than 20 years ago to pay for scholarships in Philadelphia for young entrepreneurs, which she now manages. With NPT’s assistance, the fund now operates mostly on autopilot.

“The people at NPT are really nice and helpful,” said Wischnia, who founded an online bedding line in 2019 called American Blossom Linens. “To do it on your own would be a lot harder. They really supported us.”

## **What can I donate?**

Most DAFs will let you donate cash as well as stock. Some may also accept other types of assets, such as real estate, private equity, insurance, retirement fund disbursements, or even art and cryptocurrencies such as bitcoin.

## **To whom can I make a grant?**

You can make grants to charitable organizations that are tax-exempt under Internal Revenue Code. DAFs cannot make grants to private nonoperating foundations, individuals, political candidates or political parties. Grants cannot be used for any personal benefit, such as tuition, dues, membership fees or any goods purchased at a charitable auction. Grants are not allowed for table sponsorship or tickets at charity

events. The DAF sponsor will examine and approve any grants before releasing the funds.

## How much do I need to start a donor-advised fund?

Josh Birkholtz, chairman of Giving USA, a Chicago organization that analyzes philanthropic trends for nonprofit clients, chuckles at the “poor man’s foundation” characterization, since DAFs still appeal largely to middle- and upper-income individuals. Indeed, the average DAF last year contained \$183,000 in assets, according to the National Philanthropic Trust.

The amount you can invest varies, depending upon the sponsor. Some DAF sponsors have no minimums. National Philanthropic Trust has a \$10,000 minimum. Vanguard requires a \$25,000 initial investment, and \$5,000 minimum on subsequent investments. The Community Foundation of New Jersey requires a \$25,000 initial investment, but no minimum on subsequent investments. There are hundreds of DAF sponsors, so examine their terms closely.

For taxpayers who itemize, there are limits to the amounts they can deduct each year for gifts to public charities, including donor-advised funds, according to Schwab Charitable. A taxpayer can claim 30% of adjusted gross income (AGI) for contributions of non-cash assets held more than one year and 60% of adjusted gross income for cash contributions. Contributions in excess of these deduction limits may be carried over up to five subsequent tax years.

## How much will a DAF cost me?

Most DAFs charge annual fees based on the value of the fund—Vanguard’s fee is 0.6%, or \$300 for a fund containing \$50,000. The percentage fees go down for accounts with larger balances. The sponsors also assess fees on the investments, which vary depending upon the complexity of the investment. The fees on money market funds are minuscule, and the fees on index funds are less than those on actively managed funds. Most national DAF sponsors clearly spell out their fee schedules on their websites.

DAF sponsors also set minimums for investments and for grants. Vanguard requires an initial investment of \$25,000 and allows charitable donations of no less than \$500. T. Rowe Price has a minimum investment of \$5,000 and a minimum disbursement of \$100. Fidelity and Charles Schwab have no minimum investment and allow donors to make grants of as little as \$50.

“Some donor-advised fund organizations have really focused on democratizing it,” said Giving USA’s Birkholtz. “I believe Fidelity was the first to drop the minimums.”

## Is it complicated?

DAFs can be as simple or as complex as the donor chooses. Many large national investment management firms—Vanguard, Fidelity, and Schwab—have established 501(c)(3) charities to sponsor DAFs and provide a wide range of investment funds where donors can put the assets to work until they make grants. The growth of online banking has also contributed to the growth of DAFs, allowing donors to conveniently create a fund online and transfer assets into it with a few keystrokes, said Heisman.

Sixty large national DAFs, including the National Philanthropic Trust, accounted for 70% of the \$45.7 billion in grants that all DAFs made to individual charities last year. About 600 community foundations, such as the Philadelphia Foundation and the Foundation for Delaware County, also sponsor DAFs and made \$9.6 billion in grants. Another 300 single-issue charities, which support specific religious faiths or institutions, also sponsor DAFs that made \$4 billion in grants last year.

## Why not set up a private foundation for charitable giving?

DAFs still offer many advantages over setting up a private foundation, which requires legal paperwork, and a staff to make grants and to prepare annual tax returns to verify that 5% of the assets are disbursed each year.

DAFs don’t require a minimum payout each year, a sore point for some critics who say the accounts are warehouses for capital. But the National Philanthropic Trust says that donor-advised funds on average disburse far more than 5% of their assets each year. Last year DAFs payed out 27% of their assets in grants, according to the trust.

“If I were a billionaire, I would still choose a DAF over a foundation,” said Birkholtz. “Although Elon Musk didn’t disclose this, he probably did \$5 billion-plus in donations last year, and we assume he dropped that in some sort of a donor-advised fund.”

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