

# MAKE THE MOST OF YOUR DONOR ADVISED FUND

## GUIDELINES, TIPS, DOS AND DON'TS

More and more individuals and families are using donor advised funds (DAFs) either as their primary charitable giving vehicle or as part of a more complex giving plan. To avoid common pitfalls and identify strategies for making the most of the giving vehicle, it is important to understand how DAFs work. Following are some important guidelines on what prospective donors and their advisors should do before establishing and funding an account.

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## DONOR ADVISED FUNDS OVERVIEW

### What is a DAF?

In essence, a donor advised fund is a charitable giving account, from which donors and a named advisor can recommend grants to charitable organizations. When opening and funding a DAF account, donors make an irrevocable gift to a public charity which is considered the “sponsoring charity” for the DAF account.

### Who advises a DAF?

One or more individuals can fund the account as donors. Donors may also choose advisors for the account, including themselves, who have the authority to recommend grants. In many programs, donors can also recommend successor advisors to take over the advisory role following the death of the original advisor(s).

### Who manages a DAF?

The sponsoring charity is the legal owner of the assets and is therefore responsible for the administrative duties associated with managing the DAF, such as vetting grantees and fulfilling regulatory filing requirements.

In practice, DAFs are owned and administered by a variety of organizations. For example, many financial services firms have established DAF programs for their clients. In some instances, these firms will establish their own public charity to act as the sponsoring charity for the program. In other instances, they will partner with an existing, independent public charity, such as a community foundation, to act as the sponsoring charity. Community foundations and single-issue charities, such as universities, colleges and hospitals, may also administer DAF programs.

*(Continued on next page.)*

**DONOR ADVISED FUNDS OVERVIEW** (continued)

**What are the tax implications?**

Donors may receive an income tax charitable deduction in the year that the DAF is funded, subject to certain Internal Revenue Service (IRS) limitations on donations to public charities.

**What are the distribution rules?**

Unlike private foundations, which are required to make annual minimum distributions based on the value of their investments, DAF accounts have no mandatory distribution requirements. Therefore, a donor may fund an account and then make grant recommendations at his or her own pace, without facing an annual distribution deadline. Keep in mind, however, that some DAFs have their own minimum distribution requirements.

**What should a donor know?**

Important questions to ask include:

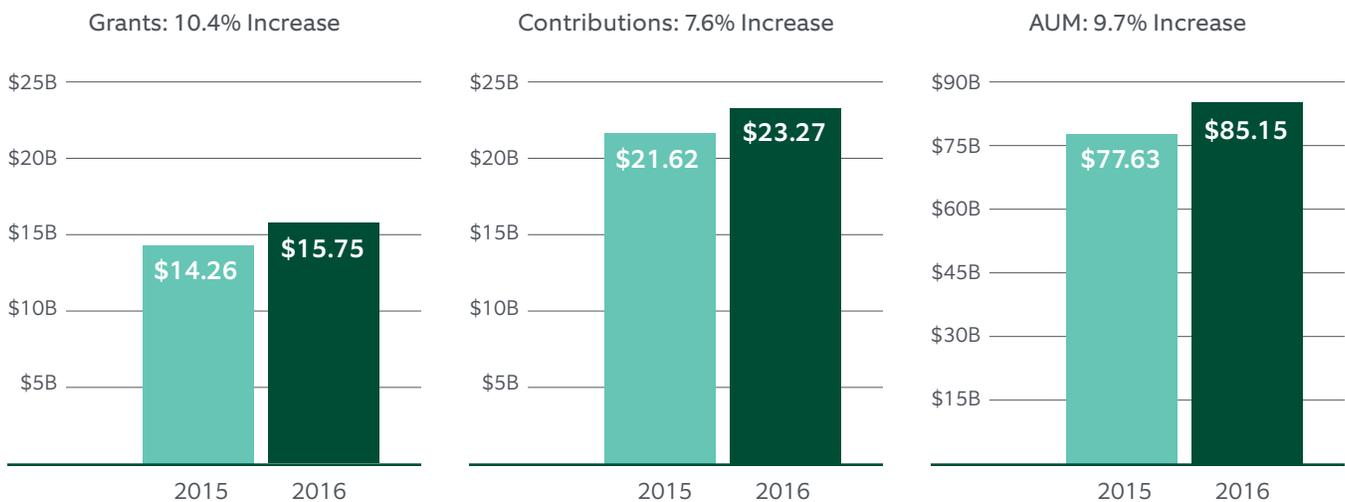
- What is the minimum contribution required to open a new account?
- What are the investment options? How often can an account's donor/advisor recommend investment changes?

- How frequently does the sponsoring charity process grant recommendations?
- Does the program allow multiple donors to recommend grants?
- Is there a minimum grant amount?
- Does the sponsoring charity have its own required distribution requirement?
- Will the account be charged a fee for each grant processed, or are all grants included in the program's administrative fee?
- Are grants to international charitable organizations allowed?
- What are the program's online capabilities (for example, can grants be recommended through an online portal)?
- How often does the program send account statements and in what format?
- Whom does a donor or advisor work with to resolve issues (an assigned relationship manager or a general help hotline)?
- How does the program handle successor donors if the primary donor is deceased or incapacitated?

## GROWTH OF DONOR ADVISED FUNDS

Donor advised funds have become the fastest-growing vehicle in philanthropy sustaining an annual growth rate of 6 percent or better for the past 6 years according to research obtained from the National Philanthropic Trust. Grants from donor-advised funds to qualified charities saw a 10.4% increase to \$15.75 billion compared to \$14.26 billion in 2015; contributions recorded an increase of 7.6% with \$23.27 billion versus \$21.62 billion; and the \$85.15 billion in charitable assets under management in all donor-advised funds represents an all-time high, and a 9.7% increase from 2015.

YEAR-OVER-YEAR GROWTH OF DONOR ADVISED FUNDS (\$ IN BILLIONS)



Sources: NPT Donor-Advised Fund Report for donor-advised funds; Giving USA 2017; Foundation Center for foundations, except where estimated by NPT as noted.

## CHECK THE FINE PRINT

While IRS rules governing donor advised funds are the same for all DAF programs, other details governing individual plans vary in important ways. Donors should ask for a program guide or a list of rules before opening and funding an account. For example, even though tax laws do not require DAF programs to distribute a specific amount each year, individual program sponsors may impose minimum distributions.

## REFRAIN FROM GRANT RECOMMENDATIONS WITH A TANGIBLE BENEFIT

Certain charitable giving vehicles have rules that prevent donors and their immediate family members (known as “disqualified persons”) from personally benefiting from their relationship to the charity. For example, tax laws prohibit the sale or lease of property between a private foundation and a disqualified person, even if the deal financially benefits the private foundation (for example, a below-market rate loan).

This is true for donor advised funds. The donor or advisor cannot receive thank you gifts or gala tickets as a result of their charitable donation. Donor advised funds are also prohibited from making what the tax laws deem are taxable expenditures — expenditures that do not fulfill a qualified charitable purpose or grants that materially benefit the fund’s donor or advisor.

Any violation of the following prohibited distributions may result in an excise tax of 20% to 125% to the fund:

- Ticket purchases to a fundraiser or other event
- Paying for a silent auction item purchased at a charity event
- Earmarks for salary or other benefits for a named grantee staff member
- Educational expense payments for a specific student
- Paying membership or giving society fees that have tangible benefits, such as free museum admission or tickets to a performance

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Certain grant types — some more obvious than others — are deemed personally beneficial to DAF donors and should be avoided.

## CASE STUDY: A NEW BOARD MEMBER’S DAF OPTIONS

Carmen is a long-standing volunteer with an organization that supports at-risk youth and is being courted to join the board of directors. She has been informed that every board member is expected to make an annual gift of \$25,000 as part of the board members’ service (often referred to as a “give or get”).

At a recent fundraiser for the charity, Carmen won a trip in a silent auction. Following the event, Carmen accepted the invitation to become a board member.

Carmen would like to use her DAF to pay for the trip and the \$25,000 “give or get.” What are her options?

- **Silent Auction:** Carmen may NOT use her DAF account to pay for the trip she purchased through the silent auction.
- **Give or get:** Carmen CAN use her DAF account to satisfy her “give or get.” There is also no conflict of interest if Carmen recommends a grant to an organization where she is a board member.

## **UNDERSTAND INVESTMENT OPTIONS**

Many DAF programs allow donors and their advisors to recommend investments, most often from a menu of pre-set investment pools. Often these pools are a mix of mutual funds, but some programs permit donors and advisors to recommend custom investments. In general, custom investment pools are assigned to a portfolio manager, require higher funding minimums and charge higher fees.

Regardless of whether the investment solution is custom or a pre-set mix of mutual funds, it is important to remember the DAF sponsoring charity has the ultimate legal authority and responsibility to select appropriate investments. Before funding a DAF account, the donor should understand the specific details of the investment offerings, such as the ability to customize investments, the associated costs and how frequently he or she can recommend changes.

## **CONSIDER MULTIPLE GIVING VEHICLES**

Often, donors have a list of charitable goals they hope to achieve. These goals may be focused on a philanthropic mission or vision, an estate planning objective or both. When determining what kind of charitable giving vehicle is best for a particular donor's priorities, conversations might naturally tend to focus on vehicle comparisons. However, instead of discussing "either/or," donors and their professional advisors should consider multiple giving vehicles.

Suppose a business owner sells her business and wants to use some of the sale proceeds to fund a charitable giving vehicle. Her goals include:

- Obtaining an income tax deduction to offset the sale income
- Establishing a permanent giving vehicle that makes grants exclusively to arts organizations in her home state, even after her death
- Making anonymous gifts to her children's schools

For this donor, a single giving vehicle may not be the best option: A donor advised fund may be an effective way to achieve the first and third goals, while a private foundation may satisfy the first two. With multiple giving vehicles, she could:

- Use the private foundation for the majority of grants made during her life and then direct the private foundation's assets to her favorite arts organization upon her death.
- Establish a DAF for making anonymous gifts to her children's schools that she could easily fully distribute and terminate once their education is finished. Using a DAF shields her from schools' fundraising lists.

## COMMUNICATE WHAT HAPPENS AFTER YOU'RE GONE

Before opening and funding a DAF account, potential donors need to consider what they want to happen after their death and whether the sponsoring charity's rules can accommodate those goals. Some important considerations include:

- **Successor advisors.** DAF programs have various rules regarding the right to name "successor advisors" to the fund after the death of the original donor advisor(s). For donors who want a DAF lasting multiple generations, it is important to understand the rules that govern successor advisors before opening and funding an account.
- **Charitable beneficiaries.** A donor advisor may not want successor DAF advisors to make recommendations from the account after the donor dies. In that case, what happens if there is a balance left in the account? Some sponsoring charities allow donor advisors to name one or more charities to receive the assets following the death of the account's last donor advisor. Other sponsoring charities — community foundations in particular — require some or all of the account's balance to revert to the sponsoring charity's endowment or general operating fund.

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Talking about death and post-death planning is not something most of us like to do. However, for philanthropists with charitable giving vehicles, post-death planning is often a crucial part of fulfilling their goals.

## CASE STUDY: WHAT ARE DAF OPTIONS FOR SUPPORTING MULTIPLE ORGANIZATIONS?

Marcus is a corporate executive for a large, multinational insurance company. In addition to his busy career, he serves on his college's board of trustees, plays a leadership role in his church and volunteers as a mentor with a youth development organization.

Marcus makes significant gifts to each of these organizations. He also makes several small charitable contributions each year to a variety of other organizations. In fact, in 2017, Marcus made contributions to 40 charities totaling more than \$50,000. Understandably, he struggles each year to keep track of his contribution receipts.

Marcus has also accumulated a significant number of unrestricted company stock awards. He has found it is difficult to contribute these shares directly, because his church and some smaller charitable organizations do not have brokerage accounts.

After voicing his frustration to his accountant, she recommends opening a donor advised fund as his primary charitable giving vehicle so he can:

- Make one charitable gift each year to the DAF and easily substantiate his income tax charitable deductions with just one receipt;
- Recommend grants out of his DAF account to the charitable organizations he currently supports, including his church and the organizations where he volunteers;
- Keep track of the organizations he supports through the DAF's online system and reporting features; and
- Contribute highly appreciated stock to the account which the sponsoring charity can sell to fund grants to smaller charities that don't have an efficient way to liquidate stock.

DAF DOS AND DON'TS		
<b>Investments</b>	<b>DO</b> check with sponsoring charity about available investment options.	<b>DON'T</b> expect complete control over investment options/solutions.
<b>Benefits</b>	<b>DO</b> make “bifurcated grants” from your personal assets.	<b>DON'T</b> use a DAF to purchase tickets to a gala, performance or fundraiser.
<b>Post-death planning</b>	<b>DO</b> check what your options are for naming post-death charitable beneficiaries.	<b>DON'T</b> assume all DAF programs allow the same flexibility after your death.
<b>Succession planning</b>	<b>DO</b> understand the multi-generation planning options permitted by your DAF.	<b>DON'T</b> list individuals as successor advisors without asking them if they are interested.
<b>Multiple giving vehicles</b>	<b>DO</b> consider how a DAF can be used in combination with other charitable vehicles.	<b>DON'T</b> assume all your philanthropy goals can be met by a single giving vehicle.

**SPEAK TO AN EXPERT**

Donor advised funds are growing more popular and for good reason. However, it is important to remember that each sponsoring charity has its own rules and policies. Prospective donors need to research options, read the fine print and ask lots of questions before choosing a program. And it is always a good idea to engage an advisor — such as a wealth planning or philanthropic advisor — to guide you through the process.

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