Working With Donor-Advised Funds: The Basics

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A donor-advised fund is a little like a personal charitable savings account. A donor creates an account and makes a contribution of cash, stock, or other assets like real estate or artwork and can take an immediate tax deduction for the gift.

The accounts are controlled by a nonprofit, called a sponsoring organization, that invests the assets and manages the donor's account. Community foundations often serve as sponsoring organizations and so do nonprofit arms of financial-services firms, such as Vanguard Charitable and Schwab Charitable. Once a fund is established, donors tell the sponsoring organization which nonprofits they'd like to donate to from their accounts.

The use of donor-advised funds remains a relatively small part of philanthropy. But their popularity has mushroomed in recent years, catapulting Fidelity Charitable to the top of the Philanthropy 400, the *Chronicle*'s annual ranking of charities that receive the most in private dollars.

Because DAFs hold billions of dollars, and their growth shows no sign of waning, we consulted experts to get answers to some of the most common questions people have about these funds.

Are all donor-advised funds alike?

Absolutely not. Every sponsoring organization has its own rules and procedures that affect the funds someone opens. Generally funds fall into three categories: commercial, community-foundation, and single-issue funds.

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Commercial funds, such as Fidelity Charitable, Goldman Sachs Charitable Gift Fund, Schwab Charitable, and Vanguard Charitable, were started by national financial-services firms. Although they are separate nonprofit organizations, the assets in the funds are often managed by the related investment company. These funds are responsible for much of the explosion in donor-advised funds over the past few years. Their main selling points include low investment fees relative to other fund sponsors, and ease of use for donors.

Donor-advised funds may seem like new arrivals on the scene, but they were conceived by community foundations decades ago and remain a key donation vehicle for most regional grant makers. Many donors open accounts at community foundations because the grant makers have a good understanding of the area's nonprofits and offer services such as family philanthropic consulting, says Christy Eckoff, director of gift planning at the Community Foundation for Greater Atlanta. These donors tend to be engaged in their giving and are looking for help to develop a plan.

"They want someone to hold their hand," she says.

Sponsoring organizations that focus on a single issue encourage giving to a particular cause or organization. They include schools and faith-based organizations, such as Cornell University and the Jewish Federation of Cleveland. Sometimes sponsors of these funds stipulate that donors must steer a certain percentage of their gifts to an institution, like a university.

Who controls the money in a donor-advised fund?

The sponsoring organization. A donor who makes a contribution to an account cedes control of the asset. "It's irrevocable," says Ken Nopar, senior philanthropic adviser at American Endowment Foundation, a donor-advised-fund sponsor. "They can't get it back." After the contribution is made, the donor can advise the sponsor when and where to make gifts, but the sponsor isn't legally obliged to follow that advice.

In reality, though, the organization almost always abides by the donor's wishes, as long as the intended recipient is a qualifying tax-exempt organization.

Can donor-advised-fund accounts be handed down to heirs?

It depends on the sponsors, Eckoff says. Some don't allow it, but others are fine with unlimited succession, meaning donors can pass accounts down through generations. Often a primary adviser is named as an heir, with a contingent adviser serving as backup in case the primary adviser is unable to serve.

Some sponsors allow accounts to be broken up into smaller funds, each with designated heirs serving as advisers. And some allow a single fund to be handed down to several heirs. In these cases, Nopar says, the advisory role can be held by one person or a team. Advisory teams generally have one spokesperson who makes grant preferences known to the sponsor and committee members who can weigh in.

If an account is not passed to a successor, what happens to the money?

When donors set up accounts, sponsors recommend that they either name successors or select charities to receive the remainder of their funds upon their death. Each fund sponsor has its own rules. However, when funds remain inactive after a designated number of years, money in the accounts usually is placed in a general fund that goes to charities picked by an advisory panel convened by the sponsoring organization.

Can assets in an account be used to fulfill a pledge?

Yes. But be careful because this is a gray area, Eckoff said. Many have interpreted IRS rules as putting the nix on such gifts. That's because fulfilling a pledge could be interpreted as providing a more-than-incidental benefit to the original donor. Remember, technically the donor is only an adviser; the assets in a donor-advised fund are legally controlled by the sponsoring organization.

Because fulfilling a pledge can be viewed as a benefit — getting the donor off the hook for a pledge — the IRS could subject that gift to a tax.

But in December 2017, the agency issued a notice that clarifies the issue. Making good on a pledge is fine, the agency said, as long as the donor doesn't attempt to take an additional tax deduction. And nonprofits be warned: Don't ask the sponsor whether the gift fulfills a pledge. To comply with the IRS guidance, the sponsoring organization may not mention the pledge when making the gift distribution.

Whether a pledge has been properly fulfilled is a matter of contract law, which varies among the states. Because of differences in the law and the b unique facts of every case, the IRS removed from sponsoring organizations the burden of deciding what does and does not fulfill a pledge. That's a matter, the guidance suggests, for the donor and the grantee. As a result of the guidance, Eckoff predicted, more pledges will be fulfilled using the accounts.

What about buying a table at a gala? Is that okay?

The IRS has given rules on galas and other events another look, too. Because donors receive something of benefit from a gala (food and entertainment), paying through a donor-advised fund presents challenges.

All of the money in a donor-advised fund has already been subject to a tax deduction, so a gift from an account can't cover personal benefits. Some sponsors will bifurcate payments, which means donors can pay for tickets to an event through their funds but cover the cost of dinner or other benefits out-of-pocket. And sometimes a donor will pay for a table at a gala but not attend. This is fine, as long as the guests at the table are not associated with the donor because hosting one's friends could be a benefit even if you are not there.

Nopar urges caution about accepting DAF money for events until the IRS comes out with a final rule.

"We're looking to the IRS to tell us once and for all," he said.

Can a private foundation give to a donor-advised fund?

Certainly. Foundations open donor-advised funds for a variety of reasons, Eckoff says. Sometimes a grant maker will start a fund to meet the federally mandated 5 percent payout, a minimum required annual donation to charity.

Some make grants to the funds because they are addressing a new issue but don't want to publicize it. And sometimes foundations set up funds so family members can conduct their own philanthropy without getting board approval for specific grants.

Aren't gifts from donor-advised funds anonymous?

Not usually. While it is true that some people choose donor-advised funds to cloak their identities, anonymous gifts are relatively rare. According to Fidelity Charitable, only 3 percent of their donors request anonymity.

And remember: Even if the contribution is anonymous, you can still thank the donor. Many sponsors, large or small, would relay thank-you notes to anonymous donors, Nopar said, so it’s worth asking.

It’s especially worth the effort with community foundations, said Eckoff. Regional grant makers keep track of donors’ interests. If you keep a line of communication open with the community foundation, even if the gifts you get through its DAFs are anonymous, there’s a better chance its donors will respond to urgent needs or become repeat donors.

How can we glean the identity of the actual donor of the gift when we receive a check from an account?

Some grants from donor-advised funds don’t include the full name and address of the donor. But that doesn’t necessarily mean the donor’s identity is a mystery. If that information isn’t made clear on the gift letter, simply check the name of the fund. Often the gifts are from something like the "Jane Doe Fund at Schwab Charitable" or the "John Smith Memorial Fund." Use those clues to try to get more information about the donor.

Upon receiving a contribution, Eckoff says, some nonprofit gift-processing staff separate the check from the attached letter before sending the check to a gift officer. Instead, keep all of the documentation together.

Unlike a personal check that has crucial identifying information, sometimes a check from a donor-advised fund doesn’t yield much. But the attached page might have all the information you need.

Should gifts from donor-advised funds be acknowledged differently than other gifts?

Do not thank donors for their "tax-deductible gift" made through a DAF. Remember, donors who use their accounts most likely already took a tax deduction when they made the original contribution to the fund. Thank them for the gift, but leave the IRS out of it.

A good rule of thumb, Nopar says, is to explicitly state that the contribution came from a donor-advised fund. Often, he says, donors file away gift acknowledgments and hand over a stack of them to their accountants at the end of the year. By stating clearly that the gift came from a DAF, you’re letting the accountant know not to double-count it for the purpose of a tax deduction.

Rachel Earl, chief development officer at St. Labre Indian School suggests gift recipients go even further. When she follows up, she asks whether donors would like to make regular, or "sustaining," gifts or if they'd like to designate the school as the fund's beneficiary in the event of death. Since all of the money in a donor-advised fund is already earmarked for charity, this gives supporters other options for giving, she says.

How often do donor-advised-fund holders ask sponsoring organizations for advice on their philanthropy?

Among community foundations, fairly regularly, Eckoff says. More than one-third of account holders with the Greater Atlanta Community Foundation seek advice. "A lot of times, they'll see an article about something in the newspaper, and they'll ask if any local nonprofits are addressing the issue," she says. "Or they'll have a certain interest in a passion area, and they want to know who is doing good work."

How can a nonprofit attract gifts from donor-advised funds?

This is the crucial question. First of all, says Earl, you have to ask. Let donors know on your website and in all of your communications that you can handle gifts from DAFs, and consider placing a prompt on your website that allows donors to give to your nonprofit directly from their DAFs.

Often, Earl says, nonprofits can "reverse engineer" donor-advised-fund gifts by checking to see if incoming checks from sponsoring organizations include a donor-adviser's name and address. With that information, she says, start soliciting gifts from those donors a bit more aggressively. If they've made a contribution from an account, it's a good bet they have more charitable resources at their disposal.