

WHAT ELSE YOU SHOULD KNOW ABOUT DONOR ADVISED FUNDS AND THEIR ALTERNATIVES

or

Where Have All The Dollars Gone?



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Outline

- Donor Advised Fund Basics
- Other Public Charity Alternatives
- Handling DAF Grants and Administration
- DAFs As Part Of Estate Planning and/or Used With Other Giving Vehicles



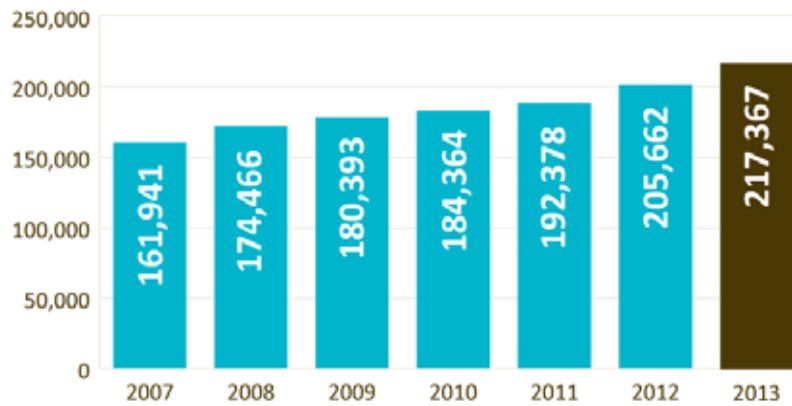
Donor Advised Funds Basics

Growth

- Gifts to DAFs were 5.2% of all gifts to charitable organizations or \$17.28 billion of the \$335.17 billion given to charities in 2013.
- Gifts to DAFs generally increased each year since 2007 (besides downturn in 2008/9)
 - 217,367 accounts
 - \$53.74 billion in assets
 - \$9.66 billion in grants



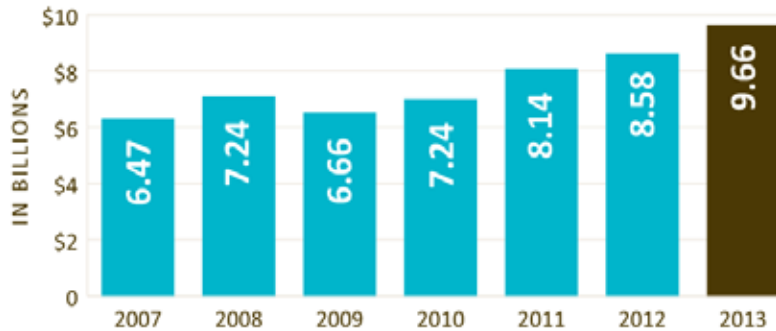
Total DAF Accounts



Aggregate Assets in DAFs



Grants from DAFs



Aggregate Contributions to DAFs



PROVIDERS

- Community Foundations
- Single-Issue Charities
- Commercial Entities



Why do People Like Donor Advised Funds?

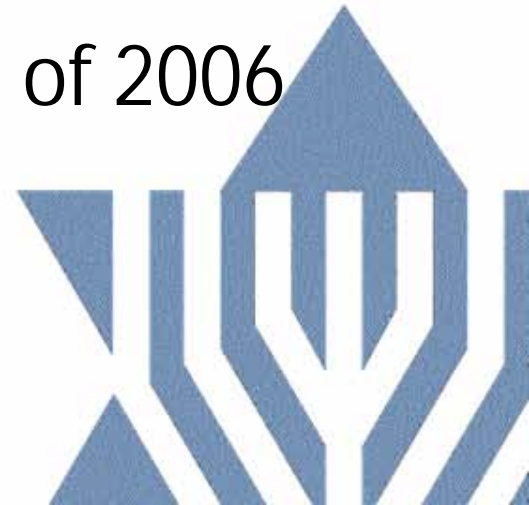
- Easy Set Up
- Tax Advantages
- Flexibility
- Fewer Rules
- No Administrative Burdens
- Anonymity




History

- A. First started in 1930's with community foundations, Jewish Federations; grew with Tax Acts of 1969 and 1986—and with entrance of commercial organizations (e.g. Fidelity) in 1990's.

- B. Codified by Pension Protection Act of 2006 (PPA).



History (cont'd)

- C. Donor advised fund now defined in Internal Revenue Code (IRC) Section 4966 as any fund or account:
1. Which is owned and controlled by a “sponsoring organization” ;
 2. Which is separately identified by reference to contributions of a donor or donors; and
 3. Which a donor or person appointed by the donor had advisory rights with respect to investments or distributions.
- 

Private Foundation vs. Public Charity


Private foundations and public charities are both included under Section 501(c)(3) of Internal Revenue Code.

- **Public charities** generally receive a greater portion of their financial support from the general public or governmental units, and have greater interaction with the public.
- **Private foundations** are typically controlled by members of a family or by a small group of individuals, and derive much of their support from a small number of sources and from investment income.

Private Foundation vs. Public Charity

Continued

A private foundation is a Section 501(c)(3) organization that does not qualify as a public charity under one of the following Sections:

- **509(a)(1)** – A church, school, hospital, medical research organization operated in conjunction with a hospital, a governmental unit, college or university endowment organization, public charity, or an organization that normally receives a substantial part of its support from a governmental unit or from the general public.
 - **509(a)(2)** – An organization that receives substantial support from grants, gifts, and contributions, and fees for services.
 - **509(a)(3)** – Supporting organizations.
 - **Section 509(a)(4)** – Public safety testing organizations.
- 

Private Foundation Rules & Regulations

- **Grantmaking:**
 - Must give out at least 5% of fair market value of the foundation's non-charitable assets in the previous year.
 - 30% tax on any undistributed income and additional 100% tax if foundation doesn't make up the deficient distribution within 90 days of receiving notification from the IRS.
 - Also, an excise tax of 1 to 2% on net investment depending on amount of grants.



Rules & Regulations

Continued

- **Self Dealing:** no sales, exchanges or leases of property, most loans, or the provision of goods, services or facilities between a disqualified person and a private foundation.
- **Excess Business Holdings:** private foundation and its disqualified persons together may own no more than 20 percent of the voting or ownership interest in a business enterprise.



Do Donor Advised Funds Give Out Enough Money?

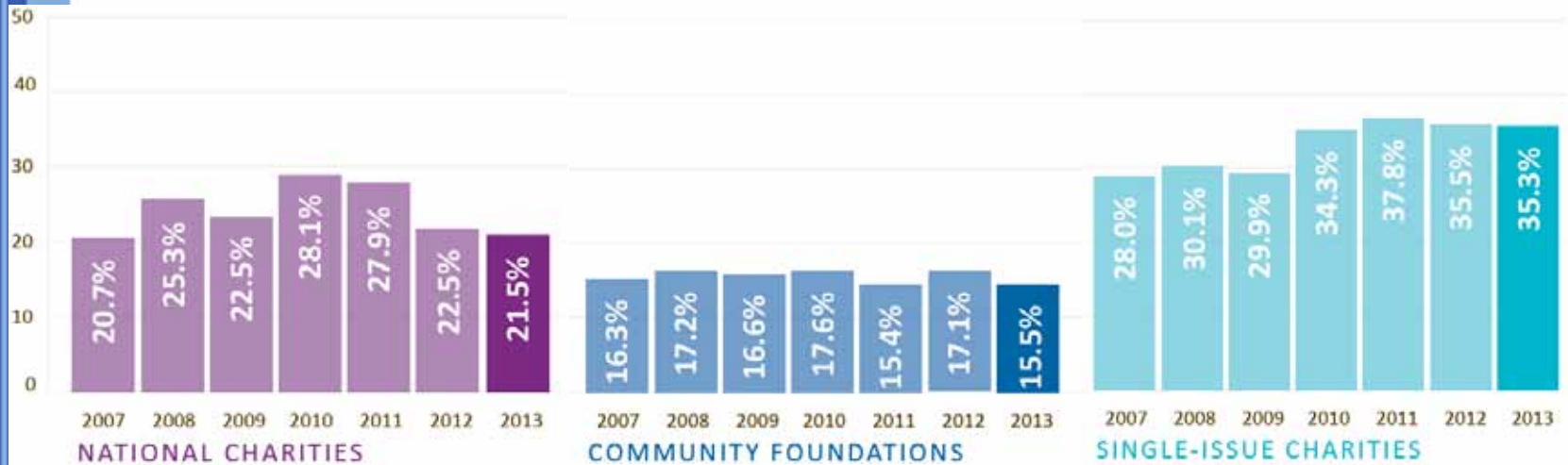
Arguments that they don't are:

- Commercial companies are just making money off DAFs by sitting on funds and charging fees.
- Donor gets a tax advantage for money that doesn't necessarily go to charities.

BUT...



DAFs Give Out A Lot



Other Public Charity Alternatives

- Field of Interest Funds
- Designated & Scholarship Funds
- Giving Circles
- Supporting Organizations



Field of Interest Funds

- Established for specific area of donor's interest:
 - Distributions can be set amount or as donor recommends
 - Can last in perpetuity/cy pres doctrine



Designated & Scholarship Funds

- These are types of Field of Interest Funds:
 - Designated funds support one or more specific charities
 - Scholarship fund: donor can sit on larger committee that chooses who gets the scholarship, but cannot control/direct who gets scholarship



Giving Circles

- Group of donors band together to contribute to a defined cause and work together to make grants to programs that address that cause.



Supporting Foundations

To be supporting organization, you must meet four tests

- Organizational Test
- Operational Test
- Relationship Test: One of the three defined relationships and each one is a “type supporting organization.”
 - Type I – “Operated, supervised or controlled by”, which means supported organization designates a majority of the board.
 - Type II – “Supervised or controlled in connection with” – same individual supervise both organizations.
 - Type III – “Operated in connection with”, which has its own complicated tests to meet, the first being a responsiveness test, the other and integral part test.
- Control Test



Benefits of a supporting organization

- Public charity status, bypassing a number of private foundation limitations
- Subtle bootstrapping of future descendants
- Forcing a clear direction of the grant-making by affiliating with donor's favorite charity to ensure that significant support continues to that charity and others closely related to its purposes
- Very flexible vehicle



Common uses of a supporting organization:

- As a fundraising arm of public charity
- As a family grant-making entity under the control and supervision of a like-minded public charity
- As an endowment or asset holding company
- As a scholarship fund
- Problematic holdings or operations with liability problems



DAF Grants & Administration

Or

My Life As a Paper Pusher



Some Rules for DAFs (like Private Foundations)

- No grants:
 - to individuals, private foundations, for expense reimbursement, non-charitable purpose, certain supporting organizations (all considered taxable distribution).
 - where the donor (or his/her family member) receives more than an incidental benefit: things like events, memberships, tuition, payment of a legally enforceable pledge.
- No excess benefit transaction:
 - automatic excess benefit for ANY grant, loan, compensation, or similar payment from a DAF to a disqualified person; also can be where value of the economic benefit provided by the charity to disqualified person exceeds the value of the consideration received for providing the benefit.

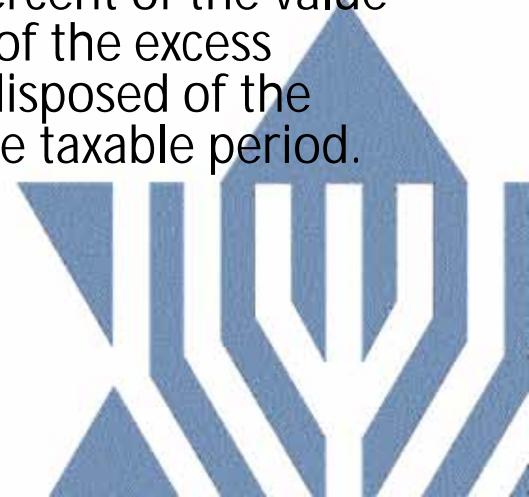
Some Rules for DAFs (continued)

- No Excess Business Holdings (same as private foundation):
 - DAF and its disqualified persons together may own no more than 20 percent of the voting or ownership interest in a business enterprise.



Some Rules for DAFS (Penalty Phase)

- Big Penalties for everyone:
 - For taxable distributions: 20% tax on sponsoring organization and 5% on fund manager
 - For grants where donor gets more than incidental benefit: a 125% on the donor or donor advisor and 10% excise tax on fund manager
 - For excess benefits: 25% of the excess portion on the person who received the benefit; if uncorrected, tax equal to 200% of the excess benefit on the disqualified person and 10% on fund manager; for automatic excess benefit cases, entire payment is considered excess benefit
 - For excess business holdings: An excise tax of ten percent of the value of the excess holdings an excise tax of 200 percent of the excess holdings is imposed on the foundation if it has not disposed of the remaining excess business holdings by the end of the taxable period.



So....

Some things, you just can't do, but:

- What if your donor has pledged a gift and wants to pay it from a DAF?
- What if your donor wants to come to your fundraising dinner and pay for it from a DAF?
- What if your donor wants to make a multi-year commitment and pay for it from a DAF?
- What about all those posters, mugs and keychains?



Best Defense Is A Good Offense

Know Your Donor And Work With Sponsoring Organization

- Find out how the donor wants to make payment when planning the gift to:
 - Avoid compliance problems before the gift
 - Learn useful information about the donor
 - Gain an opportunity for planning and stewardship
- Work with the sponsoring organization to:
 - Address questions in advance
 - Educate the donor



What do you do with this?



Jewish Federation of Metropolitan Chicago legacies & Endowments

Ben Gurlon Way • 30 South Wells Street • Chicago, Illinois 60606-5056 • (312) 357-4853 • Fax (312) 855-3284 • www.juf.org • E-mail: legacy@juf.org

May 15, 2015

The Jewish Federations of North America
25 Broadway
Ste. 1700
New York, NY 10004

Dear Friends:

The Jewish Federation of Metropolitan Chicago is pleased to present a grant to your organization from the fund listed below:

Fund Name:

Person(s) recommending this grant:

Amount: \$1,000.00

Purpose: General Operating Support- Keren Yaldenu Tikvatenu Centers

Your endorsement of this check is your affirmation that:

Your organization is tax exempt as described in Section 501(c) (3) of the Internal Revenue Code of 1986, as amended, is classified as a public charity under Section 509(a) (1) or (2) or is a qualifying governmental unit or a religious organization, and is not a Type III supporting foundation; and Neither the individual(s) recommending this grant, nor their family members nor any related parties, have received or will be entitled to any goods, personal benefits or services in consideration of this grant; and This grant is not in satisfaction of a pledge or other personal financial obligation of any individuals recommending this grant, their family members or any related parties.

You may choose to thank the donor(s), but please do not issue a tax receipt to the recommending donor(s) for this grant. The donor(s) received a tax receipt at the time they contributed to the Jewish Federation of Metropolitan Chicago. You can send your acknowledgement to the donor(s) at the address below.

We wish your organization continued success in its work.

Sincerely,

Eric Devir
Director, Donor Advised Programs
(312) 444-2083
EricDevir@juf.org

Cc:

FIDELITY Charitable™

Make more of a difference

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P.O. Box 770001
Cincinnati, OH 45277-0053

— MARY THOMAS
JEWISH FEDERATION OF METROPOLITAN CHICAGO 30 SOUTH WELLS STREET
SUITE 4057
CHICAGO, IL 60606

— May 1, 2015

Dear Colleague:

Enclosed is a check in the amount of \$2,000.00. This Fidelity Charitable grant is made possible through the generosity and recommendation of the Fund, a donor-advised fund.

Designation: Where it's needed most

Grant Terms: No goods, services or more than incidental benefits may be provided in exchange for this grant. This grant may not satisfy a legally enforceable obligation/pledge. This grant may only support purposes deemed by you to be 100% tax deductible.

You may choose to thank the donor, but please do not issue a tax receipt to either Fidelity Charitable or the recommending donor(s) for this grant. The donor received a tax receipt at the time they contributed to Fidelity Charitable. **You can send your acknowledgement to the recommending donor(s) named below.**

The Fund is a donor-advised fund at Fidelity Charitable, a public charity. Donors make irrevocable and tax-deductible contributions to Fidelity Charitable, which are owned and controlled by Fidelity Charitable in a segregated account known as a "donor-advised fund" Our donors exercise the privilege of, among other things, recommending grants to qualified public charities.

By cashing this check, you certify to Fidelity Charitable that (i) your organization is formed under the laws of the US and its territories and is a public charity described in Internal Revenue Code sec. 509(a)(1), (2) or (3), or a private operating foundation described in IRC sec. 4942(b)(3), and applicable regulations and IRS authority; (ii) this grant will be used exclusively for your organization's exempt purposes; (iii) neither the recommending donor nor other third party will receive goods, services or any impermissible benefits (e.g., tuition, memberships or dues with more than incidental benefits, admission to events or goods bought at auction) as a result of this grant; (iv) this grant does not satisfy any portion of a financial obligation (including an enforceable pledge) of any individual or entity; and (v) this grant will not be used for political contributions, political campaign activities, or excess lobbying expenditures as described in IRC sections 501(h) and 4911.

Please contact a Fidelity Charitable representative at 800-952-4438, Monday through Friday, between 8:30 a.m. and 8:00 p.m. Eastern time, with questions regarding this grant.

We wish you continued success in your charitable mission.

Sincerely,

Fidelity Charitable

What That Letter Means

- What Do You Do About The Letter?
 - Read it! Is there a pledge, incidental benefit?
 - Thank the donor
 - Acknowledge the donor
- Your Donor Is Thinking About Philanthropy
 - Why did he/she open the DAF?
 - What are the donor's intentions with it?



How Families Work Together (or not) with DAFs

- Children can be part of fund – either while parents are alive or after they're gone
- What happens when:
 - A couple gets divorced
 - Siblings stop talking to each other
 - Kids just don't think similarly about philanthropy



DAFs As Part Of Estate Planning and/or Used With Other Giving Vehicles



Key Times for Donors to Think about DAFs

- High Income Years
- Retirement Planning
- Capital Transaction



DAF as a Bequest Alternative

- Provides enhanced flexibility to make testamentary gifts.
- Super-charge a DAF.



Retirement Assets to a Donor Advised Fund

- Does not qualify for on again off again income tax exclusion.
- Can leave to DAF
 - Significant tax savings
 - Nice and tax efficient way to encourage descendants to be generous.



Donor Advised Fund Case Study

Maker and Lotta Bucks

Maker and Lotta Bucks married in college. Maker started a small candy company that grew to a name brand manufacturer. Lotta became a partner at an investment house. They had three children, Mega, Caring and Simple.

As the family grew, the Bucks fortune grew, especially with Lotta's financial acumen.

The Bucks wanted to give back and decided to create a giving vehicle. They give to 20 charities a year (\$1,000 each).

Assets:

Stock in Makers Candy

Lotta's Partnership in Investment Co.

2 Retirement IRA's – each with 1,000,000 in them

Stock portfolio 3,000,000

Explore the Bucks Family's Options



The Saga Continues...

The three sons marry and start their families:

- Mega marries Minnie, have 6 kids. Mega starts a hedge Fund in college and makes at least \$10 million a year.
- Caring marries Caren, have 2 kids, and both are city high school teachers.
- Simple who works at Maker's marries Simpler, an aspiring yoga instructor.

Maker and Lotta want to get the kids and grandkids involved in giving.



And The Saga Continues...

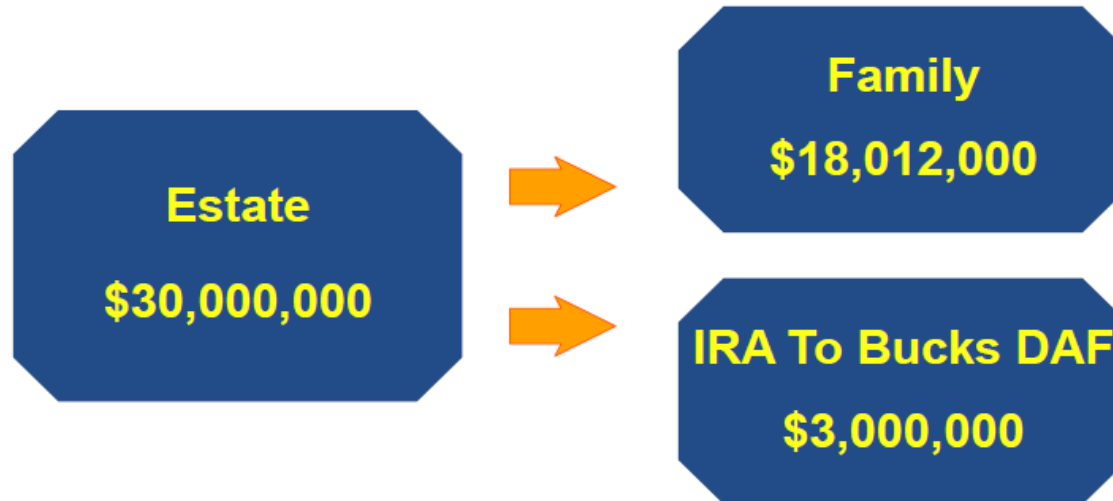
Maker and Lotta Bucks decide to revise their planning.

Lotta joins the Board of the local Art Museum, and she is immediately solicited to leave a major endowment .



BEQUEST OF IRA

Prepared For Maker & Lotta Bucks



1. Create by will a plan with bequest to charity. Maintain full control of property during life.

2. Bequest to charity enables a charitable estate tax deduction of \$3,000,000 and income/estate tax savings of \$2,102,880.

As the World Turns

- Siblings have disagreements and very different charitable interests.
- This is exacerbated by Simpler running off to the Himalayas with her meditation teacher.
- Mega wants to go his own way.



Annuity Lead Trust

Prepared for Mega Bucks

5.00% Lead Trust

Original Property

Value \$25,000,000

Cost \$5,000,000

Gain \$20,000,000



Trust Principal

\$25,000,000



Trust to Family

\$56,624,519

Term of 25 Years



1. Gift asset to lead trust, charitable gift tax deduction of \$24,987,125. Deduction reduces taxable gift from \$25,000,000 to \$12,875.

2. Income of 5.00% to charity for 25 years. No income tax. First year income \$1,250,000. Total charitable payments in 25 years \$31,250,000.

3. After term of years, trust distributed to family. Passing \$31,624,519 growth to family saves \$12,649,808 in gift or estate taxes.

Retain Asset vs. Lead Trust

Prepared for Mega Bucks

I. Retain Property During Life and Pay Estate Tax



II. Fund Lead Trust



Term of  25 Years

1. Gift asset to lead trust, charitable gift tax deduction of \$24,987,125. Deduction reduces taxable gift from \$25,000,000 to \$12,875.

2. Income 5.00% for 25 years; charity paid \$31,250,000. In hold asset illustration, property value grows until value is \$88,952,699.

3. After term, in Opt. I estate tax paid, leaving \$53,371,619 to family. In Opt. II no tax paid, leaving \$56,624,519 for the family.

CLT Issues

Lead interest to private foundations vs DAF organization:

If private foundation, there are control issues which could lead to an argument that this was not a completed gift if the settlor was on the board of the private foundation.

