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Donor Advised Funds' Key Advantages at Risk

Hopefully, you've had a chance to review our recent article titled 'Billions in Charitable Tax Deductions, But Where is the Money?'. The article focuses on some key features of Donor Advised Funds (DAFs) that are advantageous to many who are charitably inclined and why the vehicle may be more attractive than a private foundation.

Firstly, like most donations, the donor receives an immediate tax deduction in the year the DAF is funded. An important feature of the DAF is that there is no requirement to distribute to charity in any specified time frame. This feature is especially useful if a taxpayer needs to offset a large amount of income in a single year and would like time to consider which charities receive donations. This 'take, wait, and give' feature is advantageous when compared to a private foundation, where 5% of the assets must be distributed each year. Donations from DAFs to charities are anonymous compared to a private foundation, where it's required to keep detailed records of where the funds are distributed.

Interestingly, Private Foundations are allowed to contribute to DAFs and have found a loophole around the annual distribution and transparency requirements. Sometimes a private foundation uses a DAF to give funds indirectly to an important cause while avoiding straying from the organization's stated mission, such was the case during the COVID pandemic.

Two legislative and administrative changes are underway that target the typical user of the DAF and Private Foundations. The Accelerating Charitable Efforts (ACE) act sets forth two new rules**:** **1)** A deduction is not allowed for contributions of property until the sponsoring organization sells the property for cash. **2)** A deduction is disallowed for any year until the sponsoring organization makes an actual distribution of donated cash to charity. If both rules are met, the deductions available each year are limited to the amount distributed from the organization to the charity. These rules negate the unique features of the DAF, which is to take a full deduction at the time of contribution and the ability to wait indefinitely before selecting a recipient charity.
The ACE act proposes two scenarios where a donor can take the deduction immediately. The qualifying criteria are complex and include constraints such as the fund terminating after 15 years, minimum distributions of 5% over 15 years, limitations on the types of donations, minimum fund size, and proximity of charities that receive the distribution.

Biden's proposal within the 2023 budget is more aggressive than the ACE and targets Private Foundations.
The two major provisions require that the funds contributed to a DAF be distributed to a charity by the end of the next taxable year. The foundation must also provide detailed records of the funds contributed to the DAF and which charities received the donations.

In summary, these changes, if passed, will limit the advantages the DAF offers consistent support, intentional philanthropists, and Private foundations. We will keep you up to date on any changes in the legislative and administrative proposals.