DONOR - ADVISED FUNDS:

SIMPLE, FLEXIBLE, & TAX-EFFICIENT

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EXECUTIVE SUMMARY

What is a Donor Advised Fund (DAF)?

A Donor Advised Fund (DAF) is a "private fund administered by a third party and created to manage charitable donations on behalf of an organization, family, or individual."[1] It allows a person to contribute assets to an account today, receive an immediate tax deduction, and "grant" funds to the charity of choice at their leisure or some point in the future.

Why Use a Donor Advised Fund (DAF)?

Flexibility, Simplicity and Tax Efficiency

Tax Benefits Donor Advised Funds Can Provide:

- Income Tax
- Capital Gain
- Estate Tax
- Tax-Free Growth
- Alternative Minimum Tax (AMT)

Six Steps to Open a Donor Advised Fund?

A donor makes an IRS-eligible irrevocable contribution to a sponsoring organization's DAF and receives an immediate tax deduction against taxable income. The assets held in the DAF grow tax-free. The donor makes "grants" to their desired charity at a convenient time in the future.

Five Most Effective Strategies to Utilize a Donor Advised Fund:

1. One-Time Taxable Event: Spike in Taxable Income
    a. For Example, sale of a business, deferred compensation distribution, exercise of stock options, etc.
2. Help Specified Service Trade or Businesses (SSTBs) Qualify for the Qualified Business Income (QBI) 199A Deduction
3. Overcome the Standard Deduction
4. Lower Taxes in Retirement
5. IRA Roth Conversion: Moving Qualified Funds to Non-Qualified Funds

WHAT IS A DONOR-ADVISED FUND?

A Donor-Advised Fund (or "DAF" for short) is "a separately identified fund or account that is maintained and operated by a section 501(c)(3) organization, which is called a sponsoring organization. The sponsoring organization obtains legal control over the account. However, the donor retains advisory privileges with respect to the distribution of funds and investments of the assets in the account."[2] It allows for a donor to contribute securities or other assets to the account, receive an immediate tax deduction, and then disburse the funds, known as "grants," to their favorite IRS-qualified public charities at their convenience. Furthermore, while waiting to be granted and from the DAF, these funds can be invested for tax-free growth, potentially making an even bigger impact on the charities who receive the grants.

Donor-Advised Funds were first recognized in the Tax Reform Act of 1969 and, given the recent 2017 tax law, are now one of the fastest-growing charitable giving vehicles in the United States. They are a simple, low cost, flexible and tax-efficient tool when giving to charities. They are also highly effective and in the right situations can be used to maximize the tax benefits when a person is charitably inclined.

WHY USE A DONOR-ADVISED FUND?

1. **Flexibility**

- DAF holders will receive an immediate tax benefit for their contribution in the year of contribution, and DAFs are not required to make distributions, unlike private foundations that must adhere to the IRS annual legal payout requirements. DAFs can make grants at a time that best suits the donor, either now or at a date in the future. This flexibility allows the donors to develop a giving strategy over a longer time frame and at the discretion of the donor of the DAF.
- Donors can choose **Full or Partial Recognition** for their grants, or they can choose **FULL ANONYMITY** when giving grants to their charities, unlike a private foundation which all information is publicly available via IRS Form 990-PF.

2. **Simplicity**

- A DAF can be set up in as little as one day, unlike a private foundation, which typically is time-consuming and requires IRS approval.
- A DAF can have little to no setup costs with low administration fees.
- The Donor has **NO FILING and ADMINISTRATION requirements.** The sponsoring organization that holds the funds for the DAF has the responsibility for the preparation of tax returns, IRS compliance, accounting, grants management, fiduciary oversight and legal and audit for the funds.

3. Tax Efficiency: Primary Benefits to Donor

- **Income Tax:**
- The Donor receives an immediate full market value income tax deduction in the year of contribution. The IRS mandates certain limitations, depending on the donor's adjusted gross income (AGI):
- Deduction for cash – up to 60% of AGI
- Deduction for securities and other appreciated assets – up to 30% of AGI
- Five-year carry forward for any unused deductions

- **Capital Gains Tax:**
- Appreciated assets contributed to the DAF are **NOT** subject to Capital Gains Tax.
- Appreciated assets could include both public traded securities and closely held stock (C-Corp & S-Corp), real estate, or other illiquid assets.

- **Alternative Minimum Tax (AMT):**
- Since the Donor receives an immediate income tax deduction in the year of contribution, this deduction can also help minimize or eliminate the impact of the Alternative Minimum Tax for those that are subject to it.

- **Tax-Free Growth:**
- Investments in the DAF appreciate tax-free.

- **Estate Tax:**
- The DAF is **NOT** subject to Estate Taxes.

SIX STEPS TO OPEN A DONOR-ADVISED FUND

Donor-Advised Funds allow you to easily manage your charitable gifting strategies while providing the funding needs to organizations you choose to support at a time of your leisure. There are typically six steps when opening and operating a DAF:

First: Determine your Sponsoring Organization and open a Donor-Advised Fund at your desired Sponsoring Organization.

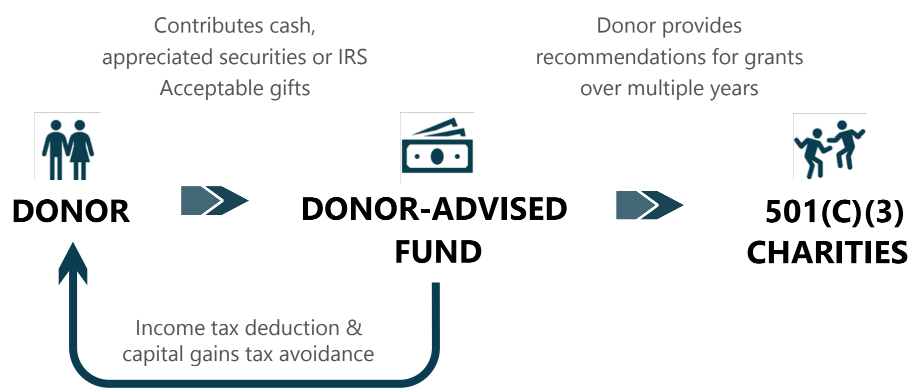
Second: You can name your donor-advised account (e.g., The Smith Family Fund), the financial advisors you wish to help manage the investments inside the DAF, and any successors or charitable beneficiaries.

Third: Make an **irrevocable** contribution of cash, stock, real estate, or eligible IRS contributions to fund the account.

Fourth: You will immediately receive a tax deduction up to the IRS limits, consult with your tax preparer for further details.

Fifth: All contributions into the DAF account can be invested and continue to grow tax-free

Sixth: When convenient, the Donor makes recommendations to the Sponsoring Organization for grants from their account to qualified 501(c)(3) organizations and charities of your choosing.



TOP FIVE EFFECTIVE STRATEGIES TO USE A DONOR-ADVISED FUND?

A DAF can be an extremely effective tool to lower taxable income, provide huge tax savings, and provide flexibility on the timing of the grants to the desired charities. It is important to note that when contributing to a DAF, a person should be charitably inclined or intend to give in the future. The Top Five strategizes for utilizing a Donor-Advised Fund are listed below, however, consult with your tax preparer for details on how each potential strategy would impact your tax situation:

1. **One-Time Taxable Event**
   a. Major liquidity events that result in a huge income spike including the sale of a business, winning the lottery, the sale of rental property, payment of deferred compensation or the execution of stock options, etc.
      i. In a year where a spike in income occurs, utilizing a DAF can help minimize the tax impact for that year while creating a charitable legacy for years to come.
      ii. In the event of the sale of a business, the business owner can set up a DAF and super fund "or frontload" the account with proceeds from the sale. The contribution to the DAF will lower his taxable income in the year of the sale and thus lower his tax liability from the proceeds of the sale of the business.
   b. Inheritances are NOT eligible since they are not taxable events for the recipient, however could be used in following years.

2. **Help SSTBs Qualify for Qualified Business Income (QBI) 199A Deduction:**
    a. Utilizing a DAF could help a business owner who is identified by the IRS as a Specified Service Trade or Businesses (SSTBs)[3] to qualify for the Qualified Business Income deduction, resulting in substantial tax savings.
        i. A DAF can then be used to help qualify an SSTB for a partial or full QBI deduction. "In 2019, the start of the phaseout range for a married couple filing a joint tax return is when their taxable income before the QBI deduction exceeds $321,400. This deduction is completely phased out when the taxable income reaches $421,400."[4]
        ii. To fully understand and utilize this strategy, please consult with your tax preparer for details on your situation.

3. **Overcome the Standard Deduction:**
    a. This strategy is useful when itemizing is no longer feasible due to the higher standard deduction in the Tax Cuts and Jobs Act of 2017.
        i. Contributing to a DAF allows you to execute a strategy called "bunching," "grouping," or "lumping" in the years the contributions are made to the DAF.
        ii. For Example: In 2019, if you are married and receive the Standard Deduction of $24,400 and typically give annually over $6,000 to charitable organizations, you could make five years worth of charitable contributions to a DAF, take the full $30,000 deduction in year one and then itemize your deductions in that year. You would skip the standard deduction that year. Subsequently, you would then give the charity its normal $6,000 in years one through five.
            1. If you typically give $10,000 annually and use the same strategy as above over a five-year time frame, you would itemize in year one and then again in year six. Your DAF would receive a $50,000 contribution, and you would receive a $50,000 tax deduction in year one. For the next four years, you would take the standard deduction while providing the charity with your annual $10,000 grant.

4. **Lower Taxes in Retirement:**
    a. While the current regulations do not allow you to directly make IRA Required Minimum Distributions (RMD) into a Donor Advised Fund, you can make contributions of non-qualified assets into the DAF to offset the increase in taxable income from the RMD.
    b. This strategy is useful if you have appreciated stocks, for example, and would like to offset your RMD income and potentially reduce taxes.[5]
    c. In this situation, you would make stock contributions to your DAF from your non-qualified accounts and receive a tax deduction. Essentially, the contribution to your DAF offsets the income from your RMD.
        i. This strategy allows you to donate to your charity immediately, or later over time.

5. **Execute a Roth IRA Conversion Without Paying Taxes:**
    a. Financial advisors and tax preparers often use a Roth IRA Conversion in combination with a DAF. You do a Roth IRA Conversion and offset the increase in taxable income with a contribution to the DAF for the exact amount of the Roth IRA Conversion. Qualified funds move over to a Non-Qualified bucket without creating a spike in income due to the contribution to the DAF Fund. Why would you do this?
        i. It allows for qualified funds to move into a Roth IRA to grow tax-free and can also have positive estate planning implications from a legacy standpoint. Additionally, in lowering the balance of the qualified account, we've essentially lowered the required minimum distribution the IRS will require in years to come.
        ii. This can be a fantastic planning tool before RMDs begin and provides tax flexibility in later retirement years to help qualify for certain federal benefits.

SUMMARY

The ease, flexibility, and tax efficiency of Donor Advised Funds have contributed to the rapid growth they have experienced over the last couple of years. With careful strategic planning and guidance from your financial advisor and tax preparer, Donor Advised Funds can now be an invaluable tool and resource in your overall financial plan.

Your charitable giving strategy doesn't have to wait for the future. It can start today!!

If you have any questions or would like help opening a Donor-Advised Fund, please feel free to reach out to us.

REFERENCES

[1] *https://www.investopedia.com/terms/d/donoradvisedfund.asp*

[2] *https://www.irs.gov/charities-non-profits/charitable-organizations/donor-advised-funds*

[3] The IRS states "a SSTB is a trade or business involving the performance of services in the fields of health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, investing and investment management, trading, dealing in certain assets or any trade or business where the principal asset is the reputation or skill of one or more of its employees or owners." It is important to note the IRS does not classify the following as SSTBs: Engineering, Architects, Insurance and Real Estate Brokers/Agents.- *https://www.irs.gov/newsroom/taxcuts-and-jobs-act-provision-11011-section-199a-qualified-business-income-deduction-faqs*

[4] *https://www.onefpa.org/journal/Pages/JUN19-Tax-Planning-for-thePhase-Out-of-the-QBI-Deduction-for-Professional-Service-Businesses.aspx*

[5] This strategy works if you want to control the timing on when the charity receives the donation. If timing is not a concern then it is typically more advantageous to directly donate the RMD to the charity as a Qualified Chartiable Deduction. Please consult your tax preparer to identify best strategy to utilize.

DISCLOSURES

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