ROBERTSON STEPHENS®

## August 21, 2023 – Wealth Planning Commentary

### Donor Advised Funds may be required to distribute funds

Donor-Advised Funds, otherwise known as DAFs, are accounts held at sponsoring organizations such as Fidelity or Schwab Charitable. Donors may donate assets to a DAF and distribute them to charities when desired. The donor may take a charitable deduction in the tax year that the donation is made. Taxes are not owed on realized gains and income inside the DAF. Donating highly appreciated securities to a DAF is a good strategy to receive a charitable income tax deduction and avoid paying capital gains tax. Assets may remain invested inside the DAF account and grow tax-free for as long as the donor wants or until they decide to distribute the funds to charity.

An individual DAF is not required to distribute to a charity in any tax year. However, the total pool of DAFs at a sponsoring organization (Fidelity or Schwab) is subject to a mandatory distribution of 5% of assets each year, the same as a private foundation. Each sponsoring organization chooses how to fulfill the distribution requirements and policies vary. An example is Fidelity Charitable, where individual DAFs must make a distribution once every two years. The distribution can be minute. If the DAF does not distribute once every two years, Fidelity will pay out 5% of the account to any charity that the DAF has donated to in the past. To emphasize this policy is specific to Fidelity Charitable. It's *not* a federal or state rule. Schwab Charitable, in contrast, does not currently force any distributions.

The DAF is a popular charitable vehicle for several reasons – their simplicity, minimal cost, privacy, and the ability to donate appreciated securities to charities that cannot accept them. DAFs appeal to all wealth levels, the mass affluent and the ultra-wealthy. Many wealthy donors see a DAF as an attractive alternative to a private foundation. Please see our article from last year on Mackenzie Scott (formally Bezos) for more details on how mega donors use DAFs. DAFs may be billions of dollars or a few hundred, Fidelity and Schwab do not require a minimum account balance. Additionally, DAFs may be treated as a family foundation and may be passed down to the next generation.

DAFs have come under fire in the past few years for 'hoarding' assets; those in the nonprofit world might argue that a DAF is supposed to be a conduit for a donation rather than a growth vehicle. Data from the National Philanthropic Trust shows that DAFs distribute at lower rates than private foundations. DAF donors can remain anonymous, and this has irked some who argue that they allow individuals to evade accountability.

Politicians have taken note, and some have advocated for new regulations. Last year we discussed two policies that may take away some advantages of the DAF. Biden's 2023 fiscal budget proposal aims to force all contributions to DAFs in a given year to be distributed by the end of the next taxable year. The second proposed regulation is the ACE Act. The ACE limits scenarios where a donor can take a charitable deduction immediately after contributing to a DAF. With Congress in gridlock, these proposed changes are unlikely to pass anytime soon, and the advantages of DAFs will likely remain intact for the foreseeable future.

Please reach out to your Wealth Manager with questions about Donor-Advised Funds.