THE COMPLEMENTARY ROLES OF COMMUNITY FOUNDATIONS AND NATIONAL DONOR-ADVISED FUNDS[1]

HOWARD HUSOCK*

EXECUTIVE SUMMARY

At 2.2 percent of GDP in 2006, the most recent comparable year, U.S. charitable giving is approximately twice as high as that of the U.K. and roughly fourfold that of Ireland, the next most charitable E.U. country. (At the individual level, France and Germany barely give at all.)[2] Yet even as overall wealth has continued to increase in the U.S. (notably, among higher-income households, which are disproportionately likely to make significant charitable donations), overall philanthropic giving has, over the past generation, remained roughly constant as a percentage of economic activity.[3]

Giving has remained flat even as a variety of rationales have emerged for the need for more such giving: declining discretionary government spending because of increased fixed costs; concern, in some quarters, over the efficacy of publicly funded social programs; and new social needs in the wake of stagnant wage growth and decreased workforce participation. At the same time, a new generation of not-for-profits, led by young social entrepreneurs, is injecting both greater dynamism and stiffer competition for funds into the charity marketplace.

Given such conditions, the question of whether total U.S. philanthropic giving remains flat, or increases, becomes increasingly pertinent. One specific, tax-advantaged vehicle for charitable giving, Donor-Advised Funds (DAFs, see box, page 2), shows signs—thanks to a 2006 clarification of the federal tax law governing them, as well as their increased marketing by major national financial-services firms (MNFSFs)—of becoming a means through which net U.S. charitable giving, along with the funds supporting it, might significantly increase.

---

[1] The original title of this paper is "Growing Giving: American Philanthropy and the Potential of Donor-Advised Funds". It has been modified for this conference.

* Manhattan Institute. Thanks to the Manhattan Institute's Alex Armlovich for his research assistance.

[2] Charities Aid Foundation: International Comparisons of Charitable Giving in 2006, https://www.cafonline.org/PDF/International%20Comparisons%20of%20Charitable%20Giving.pdf.

[3] Statistics from *Giving USA: The Annual Report on Philanthropy, 2012 Edition*, http://philanthropy.com/article/The-Stubborn-2-Giving-Rate/139811.

This paper examines the potential for further growth in donor-advised funds: recent DAF growth (especially in funds established and marketed by National DAF Sponsoring Organizations, or National DAF Sponsoring Organizations, some of which are MNFSFs) could signal the start of a surge in the volume of total charitable giving, or merely its redirection through a new, more convenient vehicle (rather than, say, cumbersome individual check-writing). This paper concludes that, on balance, DAFs of all kinds—particularly, though not exclusively, accounts held with National DAFs—provide the preconditions for significant growth in overall U.S. charitable giving. If realized, such growth would likely be driven by:

1. *Increased giving from increased DAF participation, driven by MNFSFs*. Since 2007, the year after federal tax law significantly clarified the legal status and reporting requirements of DAFs, the number of such individual accounts held by National DAF Sponsoring Organizations—including MNFSFs like Fidelity Charitable, Vanguard Charitable, and Schwab Charitable—increased from 72,590 to 112,170, with the value of assets in such accounts growing from $11.11 billion to $24.82 billion.[4] Growth factors facilitated by National DAF Sponsoring Organizations include ease of donation (especially for donations of appreciated assets, such as equities) and control over the timing of donations.

2. *Nonredundant charitable giving*. National DAF-giving likely complements community foundation–based DAF-giving. DAF account holders in community foundations (which, prior to the growth of National DAF Sponsoring Organizations, had been the most important umbrella organizations for DAF accounts) typically support different charitable causes from those that DAF-account holders in National DAF Sponsoring Organizations do.

3. *Increased charitable capital*. Such an increase would result from tax-free appreciation of DAF assets (a consequence of the fact that the full amount of funds deposited in DAFs are not typically distributed in the same year that they are donated). Such funds, when held in National DAF Sponsoring Organizations, grow through investment in a mix of mutual funds chosen by their boards. Since 2009, undisbursed funds held in National DAF Sponsoring Organizations have appreciated by $6.56 billion.[5] In contrast to private foundations, which must make annual grants equivalent to 5 percent of assets, there is no legal DAF payout requirement—suggesting

---

[4] National Philanthropic Trust, "Total Value of Charitable Assets in Donor-Advised Funds by Charitable Sponsor Type," 2014 DAF Report, Figure 7, http://www.nptrust.org/daf-report/sponsor-type-comparison.html.

[5] Calculations, 2009–12: cumulative contributions = $39.72 billion; cumulative grants = $30.22 billion; difference (contributions – grants) = $9.50 billion; change in assets = $16.06 billion; implied appreciation = +$6.56 billion.

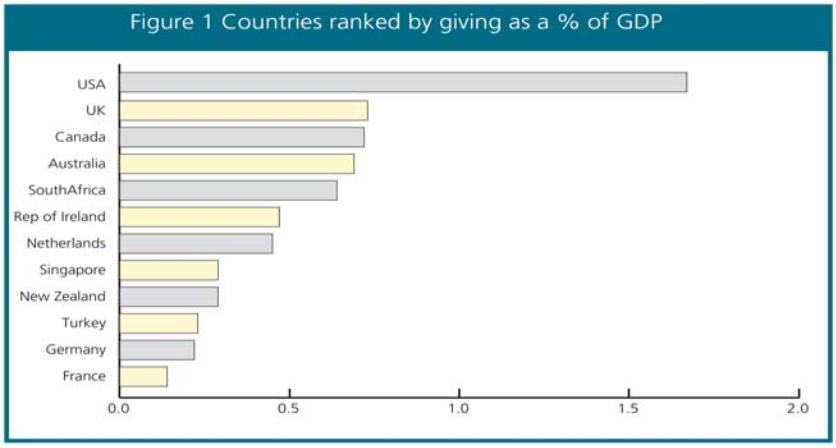
that such accounts will evolve into thousands of small, individually controlled charitable endowments. Typically, however, National DAF Sponsoring Organizations commit to a 5 percent minimum institution-wide payout requirement that would eventually become binding if institution-wide assets fail to pay out in a timely fashion.

Still, DAF growth is not inevitable. Changes in tax law, such as that proposed in the Tax Reform Act of 2014, could discourage the deposit of funds and assets into National DAF Sponsoring Organization-based and community foundation–based DAF accounts, curtailing overall U.S. charitable giving in the process.

Introduction

Private charitable giving is widely considered to be one of the distinguishing features of American society. The country's $325 billion in annual charitable giving—by individual households, private foundations, and corporations to not-for-profit organizations serving public needs—constitutes a significantly higher portion of the U.S. economy than in any other advanced economy (Figure 1).

Figure 1. Charitable Giving as Percentage of GDP, Select Countries, 2005



Sources: World Bank WDI 2005: for details of country surveys see Appendix B

During 2007–13, overall DAF assets increased from $31.97 billion to $53.74 billion, with total charitable gifts from such accounts rising from $6.47 billion to $9.66 billion. Over the same period, the number of DAF

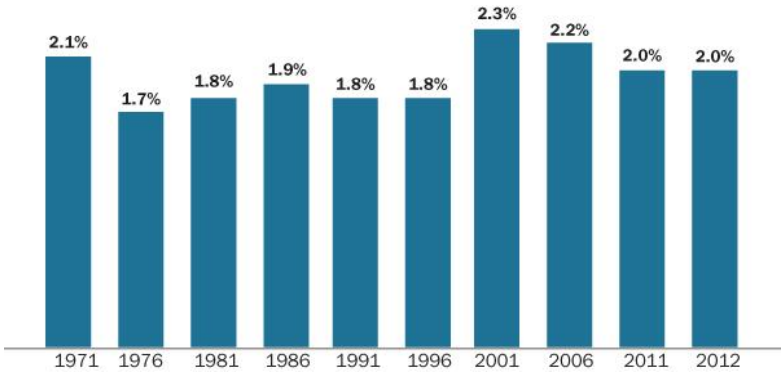
accounts grew from 160,941 to 217,367.[6] As a consequence, charitable giving of funds disbursed from such accounts has risen disproportionately, as a share of total giving.

WHAT ARE DONOR-ADVISED FUNDS?

DAFs are individual charitable-giving accounts housed within "sponsoring organizations"—notably, National DAF Sponsoring Organizations (which include MNFSFs), community foundations, and single-issue charities. DAFs allow donors to deposit cash and other assets and avail themselves of a federal tax deduction, for the same tax year, for the full value of their donation. With the exception of overhead—around 1 percent annually[7] for MNFSF-based DAFs—donations, once deposited, may be used only for charitable purposes. Account holders can then, at their discretion, recommend grants from such funds over the remainder of their lifetimes: hence the name "donor-advised." DAFs can be inherited, too.

It is not an exaggeration to say that if DAF donations had not continued at pre–financial crisis levels in 2008, overall U.S. charitable giving would have declined during the height of the Great Recession. It is also quite plausible that if growth in DAF giving continues to increase at current rates—and other charitable giving from individuals, foundations, and corporations remains flat—overall U.S. charitable giving, as a percentage of the economy, may break through its current, roughly 2 percent of GDP, ceiling (Figure 2). If such a development materialized, more funds would be available to charities of all kinds, making the U.S. even more of a nation in which private charity forms a significant element of the social compact.

Figure 2. U.S. Charitable Giving as Percentage of GDP, 1971–2012[8]



[6] National Philanthropic Trust, 2014 DAF Report, http://www.nptrust.org/daf-report/sponsor-type-comparison.html.

[7] Inclusive of administrative fees and the low- to medium-cost investment options.

[8] Source: Giving USA, http://philanthropy.com/article/The-Stubborn-2-Giving-Rate/139811

I. Donor-Advised Funds: A Brief History

DAFs are not a new phenomenon in the United States. In 1931, the New York Community Trust established the nation's first DAF account within its tax-exempt charitable umbrella.[9] The account exists to this day and, like other community-foundation funds that have proliferated across the country, provides both a legal home and advice to donors whose funds are housed within it.

At present in the U.S., there are more than 750 community foundations, which typically combine fund disbursements from a central pool directed by staff members, with disbursements from individual DAFs (often directed with advice from foundation staff). The focus of such giving has traditionally been local and regional. In this way, community foundations and the DAFs they house are classified by the IRS as sponsoring organizations: tax-exempt not-for-profits that disburse financial support to other tax-exempt not-for-profits that, in turn, provide specific types of services.

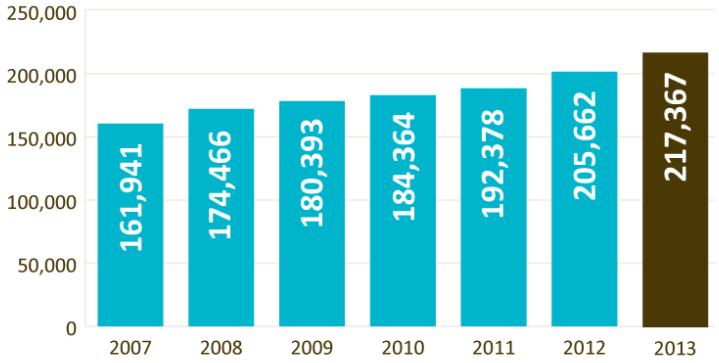
Religiously oriented organizations—such as the Jewish Federations of North America (which have individual chapters analogous to community foundations) and various Catholic charities—have historically played important supporting-organization roles. In later years, community-foundation DAF accounts were augmented by nationally oriented specialty organizations. For example, Virginia-based Donors Trust provides an umbrella home for donors generally classified as politically conservative, who entrust their charitable giving to staff knowledgeable about organizations with missions consonant with donors' views. The San Francisco–based Tides Foundation is viewed as the latter's counterpart on the political left.

In 2006, specific mention of DAFs, along with their codification in tax law, was included in the Pension Protection Act (a piece of legislation not generally focused on charitable giving).[10] In previous years, legal uncertainty had limited DAF growth; but from 2007 to 2013—the first year of high-quality data for DAF sponsoring organizations reporting via Form 990—the number of DAF accounts grew by 34 percent (see Figure 3).

---

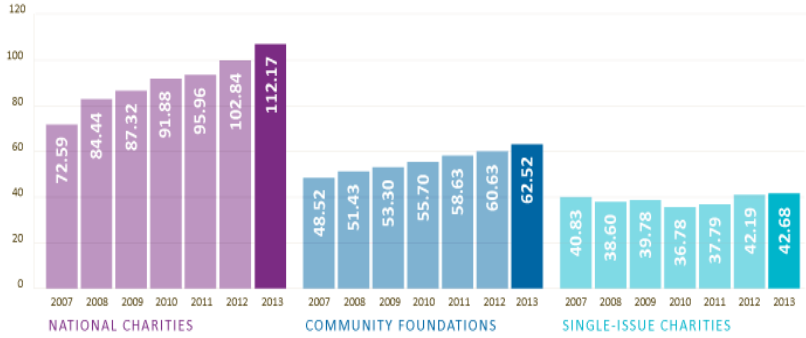
[9] See http://www.nycommunitytrust.org/AboutTheTrust/Overview/tabid/496/Default.aspx.
[10] See http://www.gpo.gov/fdsys/pkg/PLAW-109publ280/pdf/PLAW-109publ280.pdf.

Figure 3. Number of DAF Accounts, 2007–13[11]



Before 2006, some of the largest U.S. financial-services and wealth-management firms established separate, independent public charities to administer DAFs. Fidelity Charitable (founded by Fidelity Investments), Vanguard Charitable (Vanguard), and Schwab Charitable (Charles Schwab), among others surveyed by the National Philanthropic Trust (NPT), have since begun marketing the idea of individual charitable accounts to the extensive customer bases at their founding companies—to considerable success (Figure 4). The remainder of this paper largely focuses on the explosive recent growth of America's DAF industry.

Figure 4. Number of Accounts by DAF Sponsoring Organization, 2007–13[12] (NPT-surveyed DAF sponsoring organizations)



[11] Source: NPT 2014 DAF Report, http://www.nptrust.org/daf-report/sponsor-type-comparison.html

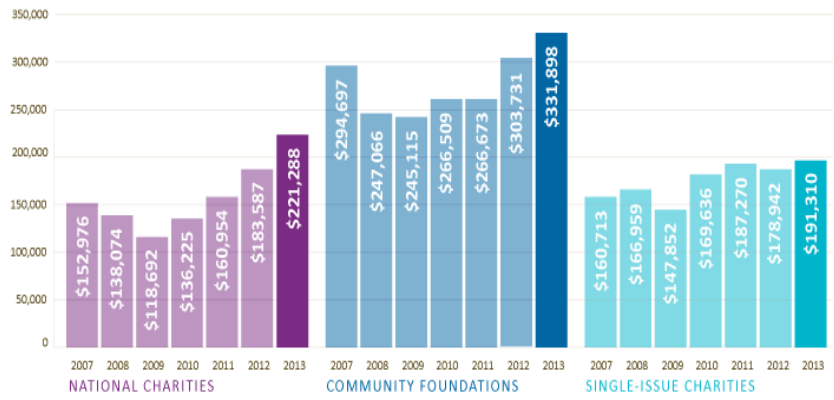
[12] Source: NPT 2014 DAF Report, http://www.nptrust.org/daf-report/sponsor-type-comparison.html

II. Characteristics of Donor-Advised Funds

Historically, DAFs have differed in notable ways from private foundations, with such differences encouraging the recent surge in new DAFs. New DAF accounts enjoy, for instance, existing organizational infrastructure rather than being required to establish a new management structure, with attendant costs (as with freestanding private foundations). Private foundations are subject to regulations (originally enacted in 1969) requiring minimum annual disbursements equal to 5 percent of assets; DAFs, in contrast, are legal public charities and are therefore not subject to a minimum, nor are they subject to the 1 percent excise tax on asset appreciation that private foundations must pay.[13] They do voluntarily implement sponsoring organization-wide payout minimums of 5 percent of assets, and they require account advisors to recommend grants at least once every several years.

Relatively low minimum-account-opening requirements at MNFSFs make DAFs comparatively more attractive to smaller donors. So, too, do minimal administrative costs and start-up deposits. At the three largest MNFSFs—Fidelity Charitable, Vanguard Charitable, and Schwab Charitable—minimum balances range from $5,000 to $25,000, while administrative expenses (excluding investment fees) start at 0.6 percent of assets per year, declining as account balances grow beyond $500,000.[14] Thanks to such advantages, small and medium donors constitute the norm (Figure 5).

Figure 5. Average Account Value by Sponsoring Organization, 2007–13[15]



[13] See http://www.nptrust.org/donor-advised-funds/daf-vs-foundation. Institutional voluntary payout minimums are de facto enforced by the watchful eyes of the IRS and the threat of corrective legislation, should payouts falter.

[14] See https://www.vanguardcharitable.org/individuals/fees_and_expenses.

[15] Source: NPT 2014 DAF Report, http://www.nptrust.org/daf-report/sponsor-type-comparison.html

The advent of MNFSF-based DAFs makes it possible for the former to market the idea of charitable accounts as complements to other personal accounts, such as those for investment or retirement. MNFSFs enable account holders to swiftly transfer assets held in other personal accounts to charitable accounts held at any National DAF Sponsoring Organization. Fidelity, in particular, offers an appreciated securities tool to help "identify potential long-term appreciated securities in your Fidelity brokerage account that you might consider contributing to charity."[16] Though it can be used to identify appreciated assets that may easily be given to any public charity, the tool nonetheless provides a convenient opportunity to open a Fidelity Giving Account.

Stock held in brokerage accounts can be transferred directly to DAFs without first being sold. The increased value of such shares—which would be taxed as a capital gain if the appreciation were realized as a private gain—is not taxed. Indeed, the value of long-term appreciated assets of all kinds—artwork, for instance—can be assigned to DAF accounts without being taxed.[17] Crucially, the full appreciated value of assets can qualify for the charitable tax deduction from the amount of income subject to federal income tax (provided such a deduction does not exceed 50 percent of gross income). In addition, assets that an individual realizes from major liquidation events (such as the sale of a privately held business) can be directly transferred to DAFs without facing capital-gains taxes, subject to limits on the amount of deductible income in a single year.[18]

MNFSFs are particularly well prepared to harvest such capital gains for the charitable purposes of DAFs. MNFSFs have the capacity to assess such donations as appreciated art and rapidly credit DAFs with accurate values. Vanguard largely relies on a third party for working with these assets; Fidelity offers significant internal expertise. Individual private charities, in contrast, may have to seek specialized legal help in the (relatively rare) event that they receive such gifts. Stated differently, MNFSFs have the capacity to facilitate charitable giving—giving that might not otherwise occur.

Additionally, assets held in DAF accounts that have not been distributed continue to appreciate, on average, over long periods. Assets in NPT-surveyed National DAF Sponsoring Organizations—including Vanguard, Fidelity, and Schwab—grew from $11.1 billion in 2006 to $24.82 billion in

---

[16] See https://www.fidelity.com/charitable-giving/overview.

[17] See http://www.fidelitycharitable.org/giving-strategies/tax-estate-planning/donate-non-publicly-traded-assets.shtml.

[18] See http://www.fidelitycharitable.org/docs/Using-Private-Foundations-and-Donor-Advised-Funds.pdf.

2013.[19] From inception in 1991 through 2013, Fidelity Charitable's investments alone have made an additional $2 billion available for grant-making.[20]

The advent of the DAF industry can thus be said to set the stage for the growth of financial assets that may be put only to charitable purposes (and receive an immediate, one-year tax break for that reason) but that can be disbursed at the recommendation of the donor or his heirs. This can be an attractive feature for individuals nearing retirement who may wish to avail themselves of DAF tax advantages—while they themselves are still subject to high marginal tax rates—thereby reserving funds for charitable purposes, to be pondered over the course of their retirement.

Critics of DAFs, such as Professor Ray Madoff of Boston College Law School, worry that donations would be so slow as to deprive charitable organizations of needed funds: "I and many other critics of the laws governing the funds are concerned that donors and the people who manage their money have been the primary recipients of benefits from the growth of donor-advised funds, while charities and the people they serve are being starved of resources. Donors get an immediate up-front tax benefit—money that drains the federal treasury of much-needed revenue for government services—but face no obligations to ensure that the money makes its way out to charities in a timely manner. Under the law, these funds can be kept in place in perpetuity."[21]

Madoff argues that the growth of inheritable funds with "merely" voluntary payout requirements risks tying up large pools of capital long after the deaths of the actual donors—echoing a concern historically consonant with the political Right over private foundations that stray from original "donor intent." Such criticism is generally credited with having prompted the February 2014 House Ways and Means Committee proposal that would have required funds placed in DAF accounts to be distributed within five years, or be subject to a 20 percent excise tax. Section VI discusses the implications of this proposal.

III. Fee Structure

All MNFSF-based DAF providers—Fidelity, Vanguard, and Schwab—charge administration and investment fees. All require a minimum starting account balance: $5,000 (Fidelity and Schwab) and $25,000 (Vanguard). For the average account, administrative fees for MNFSFs are ap-

[19] See http://www.nptrust.org/daf-report/sponsor-type-comparison.html#national-charities.

[20] See http://www.fidelitycharitable.org/about-us/history.shtml.

[21] Ray Madoff, "5 Myths About Payout Rules," *Chronicle of Philanthropy*, January 13, 2014, http://philanthropy.com/article/5-Myths-About-Payout-Rules-for/143919.

proximately 0.6 percent of assets; as balances rise, MNFSFs reduce charges (0.6 percent on the first $500,000; 0.4 percent on the next $500,000; and so on). Such fees, they assert, with some justification, are imposed to cover costs, not reap profits.

Vanguard, for example, realized less than $5 million in total fees for Vanguard Charitable in fiscal year 2014—a trivial sum when compared with overall revenues for an organization managing roughly $3 trillion.[22] Fidelity, which offers 15 mutual funds for those with accounts in Fidelity Charitable, sets fees (by independent boards of those respective funds) ranging from 0.07 to 1.17 percent. Fidelity Charitable's assets, meanwhile, constitute less than 1 percent of Fidelity's nearly $2 trillion in assets under management.[23]

The MNFSFs note that if individual donors were to establish their own foundations to house, invest, and disburse funds, then expenses—and thus the extent of funds diverted from charitable purposes—would inevitably be higher. Office and staff costs might well be incurred. Asset-management fees would certainly be incurred, just as they are when funds are managed by single-issue charities, community foundations, or MNFSFs.

Were, on the other hand, all DAFs donated immediately and entirely to charitable organizations, fewer administrative costs might plausibly be incurred. Such a scenario would also, of course, be entirely hypothetical: nonprofits themselves must manage the funds that they receive and pay others to do so, after all. Indeed, nonprofits must pay processing fees when receiving donations via credit card–based transactions. Moreover, in many situations (donations, say, of appreciated assets, such as stocks, art, and antiques), individual nonprofits often lack staff capacity for their conversion into the liquid assets required to cover expenses. In contrast, administrative fees at Fidelity cover the relevant legal costs of effectuating most such transactions.[24] Other MNFSF-sponsored DAFs are similar.

Another option for medium and large donors considering DAFs is the formation of a non-operating private foundation, where typical administrative expenses are 6.4 percent of grants[25] (versus, say, under 4.5 percent of

---

[22] See http://www.wsj.com/articles/how-vanguard-hit-3-trillion-1412539983.

[23] See https://www.fidelity.com/about-fidelity/fidelity-by-numbers/corporate-statistics.

[24] See http://www.fidelitycharitable.org/docs/Donating-Non-Publicly-Traded-Assets.pdf: "Fidelity Charitable does not charge a direct fee for helping its donors contribute complex assets (only unrelated business income tax, if applicable, actual carrying and maintenance costs, and certain tax preparation consultancy costs are taken from the proceeds of the sale of the contributed asset)."

[25] Foundation Center, "Benchmarking Foundation Administrative Expenses: Update on How Operating Characteristics Affect Spending," 2012, http://foundationcenter.org/gainknowledge/research/pdf/expenses2012.pdf.

grants for Vanguard).[26] Further, it is extremely unlikely that an active portfolio manager hired by a private foundation could match the investment expense ratio of even the most expensive Vanguard fund (a mere 0.17 percent of assets) offered by Vanguard Charitable. Median investment expenses at private family foundations equal approximately 0.7 percent of assets, according to the Foundation Center.[27] In other words, Vanguard's investment expenses are *threefold* lower than those of the median private family foundation. Moreover, for small donors with $250,000 or less to give, starting a foundation is not an option. Even for those with $5–$10 million to give, the start-up costs of a private foundation can be daunting.

It may be true that the advent of MNFSF-sponsored DAFs enables their parent sponsors to continue to earn the same investment fees from DAF donors that would have been lost, had the funds been donated to a private family foundation or other similar recipient. But these investment fees are lower, and the charitable tax benefits higher, than those available from nonoperating private foundations.

Ultimately, the debate over DAFs is one not about fees that may flow to private financial firms but about whether the U.S. wants to encourage growth in charitable giving as a portion of the economy. DAF account balances can be used, after all, for one thing and one thing only: charitable giving. Opposition to DAF giving is therefore not a defense of charity against large financial firms but simply an expression of impatience: better, the argument goes, to give smaller amounts immediately than larger amounts in the future.

IV. DAF Giving Patterns

As mentioned, debate over the merits of DAFs implicitly involves answering the question of whether it is worth forgoing tax revenue to encourage charitable giving—even if it means allowing charitable funds to be disbursed more slowly than might otherwise be the case (while gaining value in the interim). This is, fundamentally, a values question for the U.S. to consider, rooted in one's views on whether a larger charitable sector is desirable. For those (such as this writer) who hold the view that charitable giving

---

Foundation Center calculates administrative expenses as a percentage of grants, rather than a percentage of assets, and does not include investment expenses in the ratio.

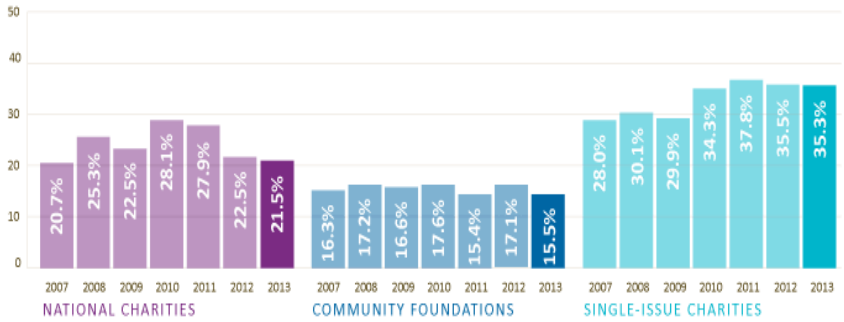
[26] Estimate based on FY2014 data from Vanguard Charitable. We estimated V.C. administrative expenses at 4.5 percent of FY2014 grants as the upper bound of V.C.'s expense ratio in this metric by assuming that all V.C. account holders' assets were in the most expensive administrative cost tier. This rate applies only to an account holder's first $500,000 in assets.

[27] Council on Foundations, "Governance & Administrative Expenses: Key Findings," p. 5, http://foundationcenter.org/gainknowledge/research/pdf/cof_manhighlights.pdf.

can support ideas and organizations for which government initiative cannot easily substitute, the answer is yes.

As a practical matter, concern to date about the pace of DAF distributions—itself a reflection of the assumption that rapid distributions are positive—does not appear warranted. The MNFSFs that are surveyed by NPT are reporting distributions equal to, on average, 21.5 percent annually, per account (Figure 6), far higher than the mere 5 percent distribution of asset value required of private foundations. The 21.5 percent average, true, masks wide variation. Some MNFSF-based DAF donors make no distributions in a given year; others distribute their entire funds. Such differences reflect varying circumstances, including the death of account holders and subsequent family reconsideration of recipient organizations. Notably, all National DAF Sponsoring Organizations have committed to an overall annual payout rate for DAF accounts, collectively, of no lower than 5 percent.

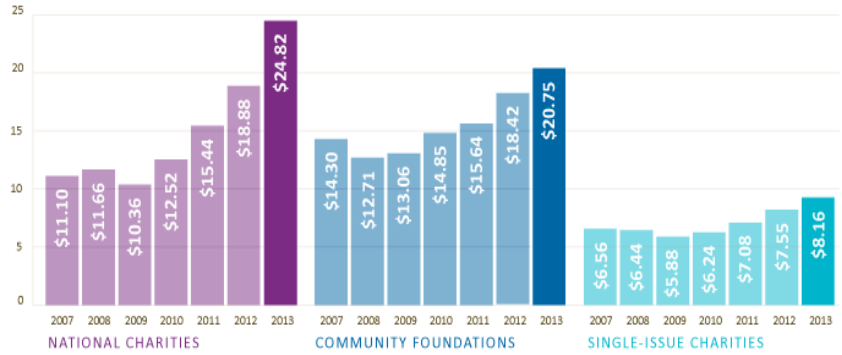
Figure 6. Distributions by Percentage of Sponsoring Organizations' Assets, 2007–13[28]



It is, however, certainly the case that all assets deposited in DAFs are *not* immediately distributed. Because they are invested with an eye toward increasing their value, such undistributed assets have appreciated (Figure 7) and will likely continue to do so.

[28] Source: NPT 2014 DAF Report, http://www.nptrust.org/daf-report/sponsor-type-comparison.html

Figure 7. Value of Undistributed Assets by Sponsoring Organization, 2007–13[29]



Still, it is virtually impossible to estimate the likely future rate of increase in the value of such undistributed assets. Doing so requires a great many assumptions, including the extent of undistributed assets; the growth in individual accounts; and the rate of investment return (itself linked to broader assumptions about the U.S. economy and interest rates). Nevertheless, the potential for DAF growth is significant.

If, for example, DAF account holdings earn 6 percent annually, if contributions continue to grow at the compound annual growth rate (CAGR) of 9.43 percent since 2007, and if the payout ratio holds at its average level since 2007 (i.e., about 22 percent of assets), then growth in appreciated assets—reserved exclusively for distribution to charitable organizations—could exceed $100 billion by 2020.

Yet rather than view this latter figure as capital denied to charity, it can instead be understood as a major philanthropic capital reserve fund that can be deployed, say, in the event of natural disasters or public health emergencies. And while the charitable affiliates of Fidelity, Vanguard, and Schwab do not, as a rule, provide guidance on organizations meriting support, they do offer useful links to those offering assistance in the aftermath of hurricanes and, more recently, in response to the West African Ebola virus outbreak.[30] In 2011, $15.5 million in relief efforts was donated, via these links, in the six months following Hurricane Sandy. Likewise, $5.9 million has been donated, to date, to organizations seeking to control the Ebola outbreak.[31]

---

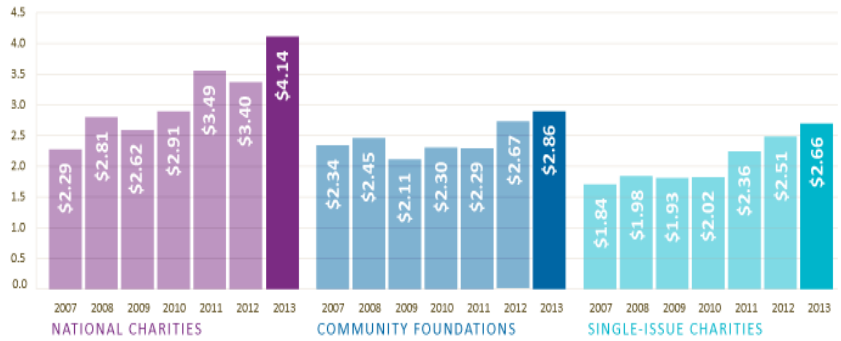
[29] Source: NPT 2014 DAF Report, http://www.nptrust.org/daf-report/sponsor-type-comparison.html

[30] E-mail correspondence with Fidelity Charitable management.

[31] Ibid.

In effect, growing MNFSF-based DAFs could become a major new source of philanthropic capital, controlled by relatively small savers but operating at a scale rivaling that of the largest private foundations, or even some government agencies (absent, of course, the central direction). Websites such as Charity Navigator—which rate U.S. charities on a range of criteria and facilitate direct donations from DAF accounts to cooperating charities—could magnify this phenomenon.[32] Because of their appreciated reserves, DAFs may respond countercyclically to economic downturns, too, providing a floor for overall charitable giving (Figure 8). In the wake of the 2008 economic crisis, this was largely the case: donations from accounts at two of the three MNFSFs increased even as overall U.S. charitable giving declined, from $311 billion in 2007 to $299.61 billion in 2008.[33]

Figure 8. DAF Distributions by Sponsoring Organization, 2007–13[34]



This potential for growth clearly applies to all DAFs, not merely to those based in MNFSFs. Thanks to hefty donations (such as $1.5 billion in gifts by Facebook's Mark Zuckerberg to the Silicon Valley Community Foundation),[35] some community foundations are also growing at a significant pace, such that they might be considered peers of MNFSF-based DAFs—in terms of assets, if not number of individual account holders (Figure 9).

---

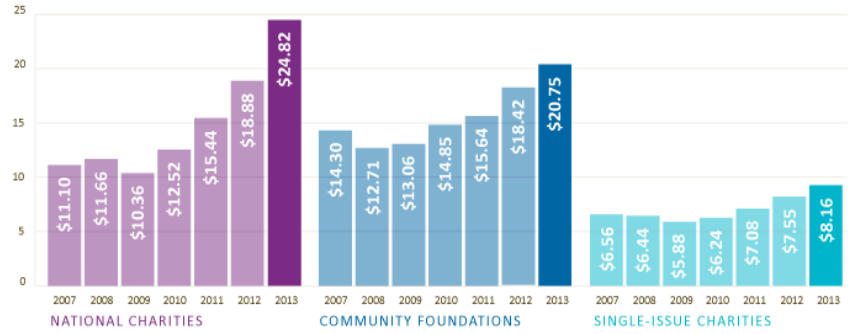
[32] Harnessing the growing popularity of DAFs to greatly simplify charitable giving, DAF Direct—the product of a joint initiative led by Fidelity Charitable—is the first web application enabling donors to initiate a grant from their DAF to a nonprofit, when on the latter's website.

[33] Giving USA 2011, "The Annual Report on Philanthropy for the Year 2010," pp. 290–91. Figures are in 2010 dollars.

[34] Source: NPT 2014 DAF Report, http://www.nptrust.org/daf-report/sponsor-type-comparison.html

[35] See http://www.telegraph.co.uk/technology/facebook/10528624/Mark-Zuckerberg-donates-1bn-to-charity.html.

Figure 9. Assets by Sponsoring Organization, 2007–13[36]



V. MNFSF-Based DAFs: Complements or Competition?

The fact that assets and distributions from MNFSF-based DAFs have increased significantly, while overall U.S. charitable giving has remained flat, raises an important question: Are the former merely a new vehicle for directing charitable giving to organizations that otherwise would have received funds?

It is a difficult question to answer, but it is possible to assess whether, in specific metropolitan areas, participants in MNFSF-based DAFs are supporting organizations that might not otherwise receive support. In other words, is the sizable marketing power of MNFSFs leading to the participation of donors who support different organizations from, say, those supported by a metropolitan area's community foundations? This paper uses data provided by Fidelity, Vanguard, and Schwab to compare giving patterns for donors in MNFSF-based DAFs with those of community foundations (including from the latter's general funds and DAF accounts).

Among Metropolitan Chicago's top 500 grant recipients by MNFSF-based DAFs and the Chicago Community Trust (CCT) foundation, 81 recipient organizations received contributions from both the former and the latter (Figure 10), with roughly 25 percent of grant dollars overlapping (Figure 11). (Figure 11 also reveals that of the roughly $31 million in giving overlap, the majority, $20.65 million, or 16 percent of total donations, came from the CCT.) Stated differently, 83 percent of the top 500 organizations supported by MNFSF-based DAFs were *not* supported by CCT (and vice versa). As such, both types of sponsoring organizations contribute significant diversity to charitable giving in Chicago—while indirectly supporting

[36] Source: NPT 2014 DAF Report, http://www.nptrust.org/daf-report/sponsor-type-comparison.html

the conclusion that MNFSF-based DAFs are expanding the reach of charitable giving nationwide.

Figure 10[37]

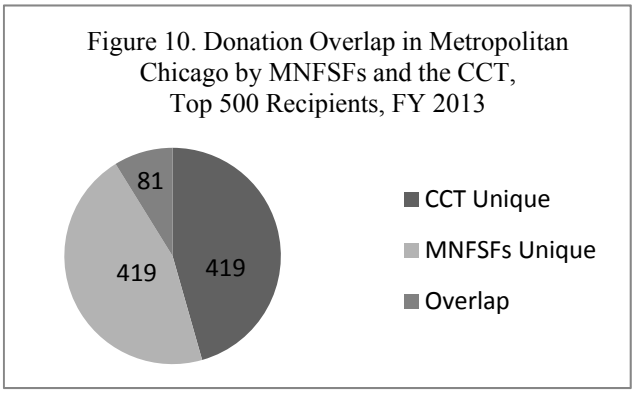
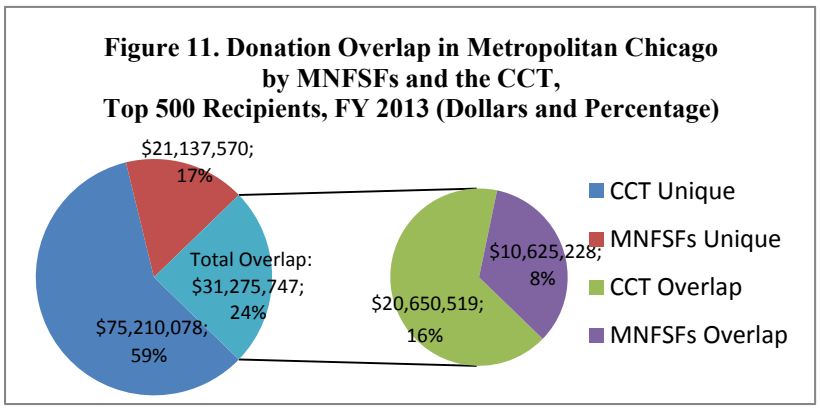


Figure 11[38]



In metropolitan Dallas, the author found similar results: 106 of each sponsoring organization type's top 500 recipients (Figure 12) received donations from MNFSFs and the Communities Foundation of Texas (CFT), with roughly 30 percent of total dollars overlapping (Figure 13).[39] In metro-

[37] Source: NPT 2014 DAF Report, http://www.nptrust.org/daf-report/sponsor-type-comparison.html

[38] Source: Fidelity Charitable, Schwab Charitable, and CCT

[39] We excluded a large one-off donation by a CFT DAF in 2013, to an organization that the MNFSFs had given several small overlapping donations. Had we not excluded this, the overlap would be 40 percent of the combined giving instead of 30 percent. Again, most of this overlapping donation came from the CFT side.

politan Denver, the author found a similar trend: 91 of the top 500 recipients (Figure 14) account for roughly 20 percent in donation overlap, by dollar value (Figure 15).

Figure 12[40]

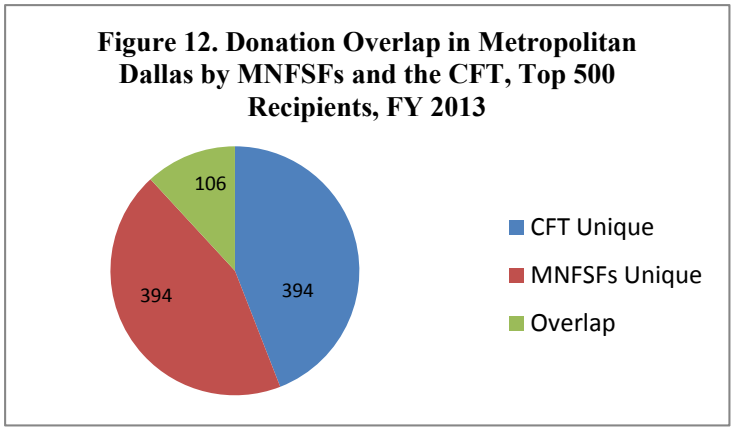
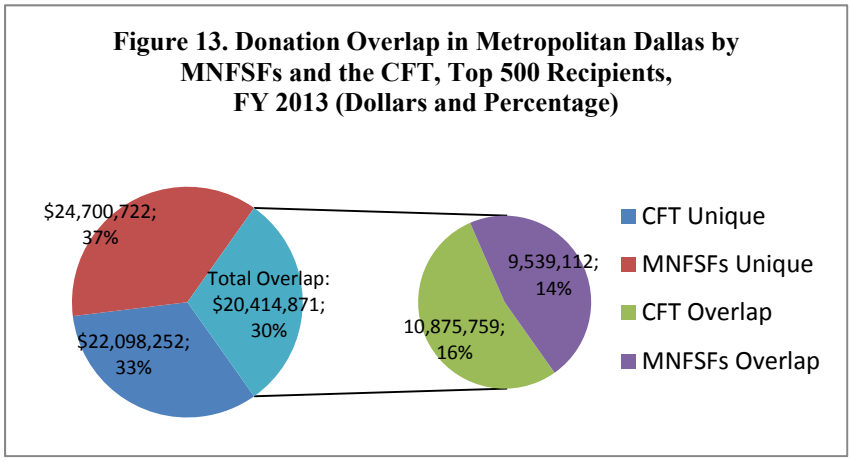


Figure 13[41]



[40] Source: Fidelity Charitable, Schwab Charitable, and CFT
[41] Source: Fidelity Charitable, Schwab Charitable, and CFT

Figure 14[42]

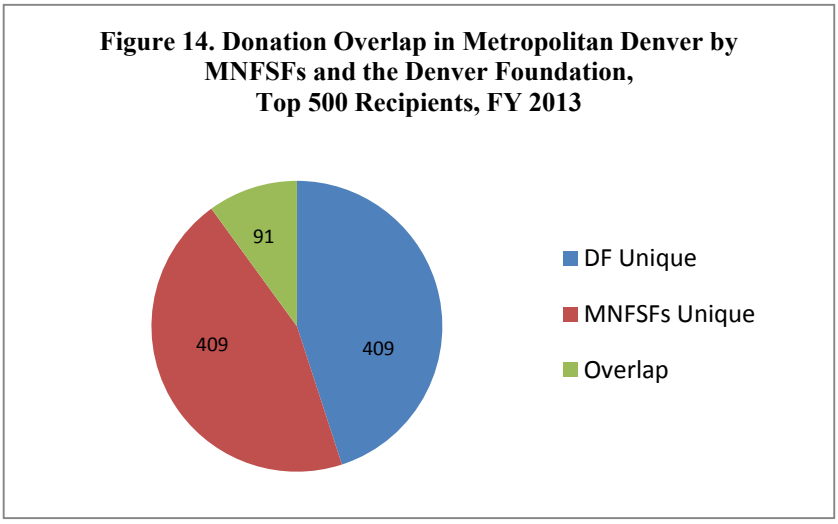
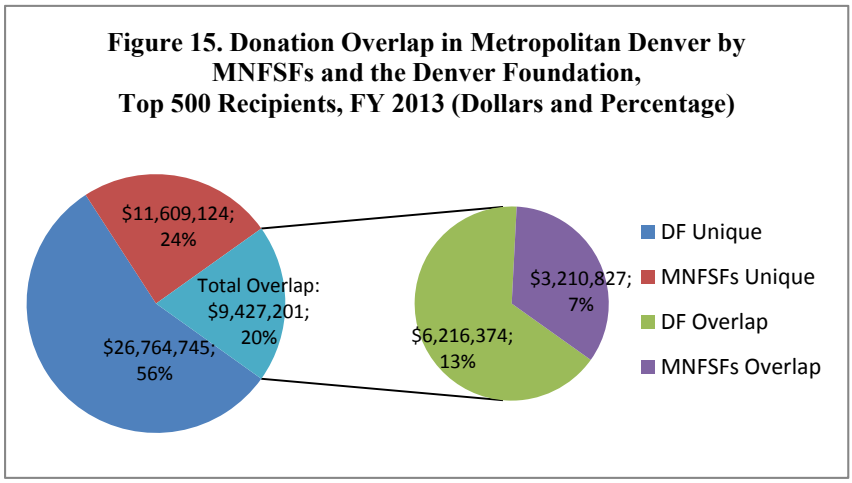


Figure 15[43]



VI. Implications of Proposed Regulatory Change

Arguably the most significant potential regulatory change affecting donor-advised funds is the February 2014 proposal by Rep. David Camp—which requires that funds placed in DAF accounts be distributed within five years, or face a 20 percent excise tax. The desire to ensure relatively rapid

[42] Source: Fidelity Charitable, Schwab Charitable, and DF
[43] Source: Fidelity Charitable, Schwab Charitable, and DF

disbursement of such funds is understandable, especially if one assumes that all such funds would otherwise have been disbursed in the same tax year for which their charitable deduction would be realized. There are, however, good reasons to believe that the five-year rule would significantly inhibit DAF growth.

Under the current rule, those on the cusp of retiring can avail themselves of a charitable tax deduction for funds set aside in a DAF and proceed to disburse such funds over the remainder of their lifetimes (almost as if they possessed their own family foundations but at far lower cost). This allows those planning retirement to reduce taxes during their earning years, in exchange for devoting a portion of their prospective estates to charitable giving. Donations made instead from retirement assets—or at a time when a retiree's earned income was lower—would result in a tax deduction of less value, thereby diminishing the incentive to set aside funds.

Likewise, the Camp requirement (that funds set aside be disbursed within five years) would diminish the capacity of DAF account holders to realize appreciation, which could, in turn, be devoted to favored charitable causes. It would also dramatically reduce account holders' flexibility to change charitable-giving priorities and magnitude, perhaps based on changes in family circumstances (e.g., a loved one who experiences a specific illness), evolving local or national needs, or the economic cycle. A rapid disbursement requirement would, moreover, disadvantage the many small, individual DAF donors over private foundations, which are only required to distribute 5 percent of overall assets annually.

In addition, the Camp requirement would impose considerable administrative obligations on sponsoring organizations. Sponsoring organizations would be called upon to track annual contributions to ensure that charitable donations of equal value were made within five years—at the same time additional funds were (potentially) being deposited and appreciation of deposited assets was occurring. Onerous verification procedures to ensure compliance would have to be established. Ultimately, rising administrative costs would reduce the amount of DAF balances available for charitable giving.

The time-sensitive distribution requirement embraced by Madoff and other DAF critics cannot obscure the fact that money that goes to donor-advised funds has been given irrevocably to charity. Therefore, it is difficult to understand why distribution within an arbitrary five-year period is preferable. At present, roughly 21 percent of National DAF Sponsoring Organi-

zations are distributed annually[44]—a trend that, if extrapolated, means that virtually all DAF deposits *are* disbursed, voluntarily, within five years.

CONCLUSION: CAN MNFSF-BASED DAFS BOOST OVERALL U.S. CHARITABLE GIVING?

As discussed, several factors will determine whether DAF growth leads to overall growth in U.S. charitable giving. Bullish forecasters should remain cautious: to date, DAF growth has coincided with a small decline in overall giving as a percentage of GDP.[45] The following observations nevertheless offer cause for optimism:

- Continued growth in appreciated DAF assets will lead to a significant pool of capital that, because gifts to DAF accounts are irrevocable, will be available exclusively for charitable giving. (Such appreciation could be limited if a more rapid payout rule is introduced.)
- Administrative efficiencies enjoyed by the large tax accounting teams and legal compliance departments at MNFSFs facilitate the giving of illiquid assets, thus reducing the effective cost of giving.
- Continued growth in the number of DAF account holders could precipitate increased charitable giving. (In surveys of account holders conducted by Fidelity Charitable, about two-thirds of respondents indicated that the use of a DAF account likely increases their charitable giving.)[46]
- The potential for growth in charitable accounts is significant: even now, only a small fraction of account holders at MNFSFs have DAF accounts.

The possibility that new DAF accounts will, over time, merely substitute for traditional check-writing to charities cannot be dismissed, but numerous factors—from convenience to asset appreciation—suggest that DAFs housed in MNFSFs and major community foundations could signal a new era in U.S. mass philanthropy (one rivaling, say, the Community Chest / United Way movement of the 1920s). The potential thus exists for a large group of relatively small donors to make a big positive difference in the magnitude of what is already the world's largest charitable giving sector.

---

[44] NPT 2014 DAF Report, "Total Payout Rate from Donor-Advised Funds by Charitable Sponsor Type," Figure 11, http://www.nptrust.org/daf-report/sponsor-type-comparison.html.

[45] See http://philanthropy.com/article/The-Stubborn-2-Giving-Rate/139811.

[46] See http://www.fidelitycharitable.org/docs/Giving-Report-2014.pdf.