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“Generous Tax Tricks”

Donor-advised funds trump creating private foundation

Ashlea Ebeling | December 16, 2013 issue of Forbes Magazine

When Brooklyn couple Norm and Elaine Brodsky wanted to help their favorite charities, they used to write personal checks. As those checks carried more zeroes, however, their UBS AG financial advisor suggested they set up a formal structure and giving plan.

The Brodskys on the roof of Brooklyn's League Education & Treatment Center

So in 2008 Norm, now 70, and Elaine, now 65, created the “Brodsky Foundation” – which isn’t (despite its name) a private foundation but a donor-advised fund. Like a private foundation, a DAF functions as a conduit. You make your contribution and claim your tax deduction now, then dribble money out to specific operating charities over years or decades while your charitable dollars are invested and growing tax free or nearly tax free (with a private foundation, there’s a small investment tax).

The DAF is like a subaccount at a public charity. You have less control than you do with a private foundation and a lot less hassle. “Some of our friends had gone through the expense and torture of setting up private foundations with the stringent rules and reporting requirements,” explains Norm. ***“We felt we’d be best served by going with a donor-advised fund. We wouldn’t have to have accountants and lawyers at every step, and it gave us a lot of flexibility.”*** Then, this past fall, the Brodskys tapped into two other advantages of DAFs that explain why some very rich people who in years past would have set up private foundations are now using DAFs or “supporting organizations” instead. They donated $2.5 million worth of shares of CitiStorage, a private-document-archive business Norm founded.

Here’s the first tax advantage: If you give private stock to a foundation you can deduct only what it cost you (your basis), whereas if you give it to a DAF, a supporting org or any public charity like the United Way, you can claim the full market value as a charitable deduction–without ever paying taxes on the appreciation.

Here’s the second tax goody, which matters to generous givers such as the Brodskys. If you donate publicly traded appreciated stock to a private foundation, you can claim a deduction for its full market value, offsetting a maximum of only 20% of your adjusted gross income each year. But if you donate appreciated property (including private stock and real estate) to public charities, DAFs or a supporting org, it can offset 30% of your AGI. Similarly, if you give cash to a private foundation it can offset only

30% of your income, compared with 50% for cash contributions to a public charity, DAF or supporting org. (In all cases any deduction you can't use in the year of the gift can be carried forward for up to five additional years.)

Norm says the couple has a "pretty good" carry forward. So far they've used their swollen DAF kitty to direct $250,000 to the League Education & Treatment Center in Brooklyn, which helps autistic kids; a seven-figure amount for a new synagogue planned by the BACH Jewish Center in Long Beach, N.Y.; and $100,000 to the Telluride Foundation in the Colorado ski town where they have a second home.

Serial entrepreneur Norm (he writes a startup column for Inc.) says he is so pleased with the way the CitiStorage donation worked out that he might eventually donate interests from his latest ventures – a chain of Japanese fast-food restaurants, Kobeyaki, and the Black Gold Suites hotels in North Dakota oil country.

"Contributing closely held stock is definitely an underused giving strategy; with all the hoopla publicly traded stock gets, private stock is the redheaded stepchild," says Bryan Clontz, president of Charitable Solutions in Jacksonville, Fla., who helped with the logistics of the Brodskys' CitiStorage donation.

To be sure, a lot of rich folks still crave the bragging rights that come with a private foundation. But assets in donor-advised funds hit $45 billion in 2012, as yearly contributions rose to $13.7 billion–equal to 45% of the amount contributed to private foundations that year, up from 36% in 2007, the National Philanthropic Trust calculates. ***"People once thought it was the lesser choice of a foundation, but now DAFs are the fastest-growing charitable vehicle out there,"*** NPT Vice President Andrew Hastings says. ***This year's jump in the top federal tax rate, as well as the run-up in the stock market and in pre-IPO values, are magnifying the tax advantages of using DAFs***, points out Claudia Sangster, director of philanthropy services at Harris myCFO.

Intrigued? Investors who want to be free to give to any cause can open a DAF at a charity affiliated with Vanguard, Fidelity or Schwab, or at the "private label" DAFs the National Philanthropic Trust offers through UBS, J. P. Morgan and other financial service providers.

If you want a good chunk of your money to help local charities, consider a community foundation – more than 600 of them nationwide offer DAFs, with a minimum contribution of $5,000, and some also offer supporting orgs, usually with a minimum contribution of $2 million. (Supporting orgs give the donor more control. Facebook founder Mark Zuckerberg has used one to donate $550 million worth of stock.)

Clontz points out that ***if your primary concern is to get the most tax and charitable bang for the buck, giving appreciated public stock is the way to go.*** Private stock donations require a qualified appraisal, which runs $5,000 and up.

Glen Tullman, managing partner of 7wire Ventures, a VC firm, opened a donor-advised fund at Fidelity Charitable in 2009 with stock in Allscripts Healthcare Solutions, which he took public in 1999 and where he served as CEO through 2012. He's used the account to funnel nearly $5 million to the IDRF (previously the Juvenile Diabetes Research Foundation) and additional amounts to other public charities, and he replenishes it as needed with Allscripts shares.

While he doesn't rule out giving private stock from the ventures he backs, Tullman likes the ease of donating Allscripts shares. "One account allows us to do all of our giving and make decisions that are the right decisions at the right time and not be driven by any particular calendar date or tax event," he says.