Accounting for Success

by
Jordon N. Rosen, CPA, AEP
Belfint Lyons & Shuman, P.A.

"How does a DAF work and why is it a good idea?"

Bunching Charitable Contributions Using a Donor Advised Fund

In the aftermath of the Tax Cuts and Jobs Act (TCJA), many taxpayers who used to be able to itemize deductions prior to 2018, now find themselves not being able to itemize and claiming the standard deduction. For 2019, the standard deduction is $24,400 for a married couple and $12,200 for a single filer. This simply means that if the total of your allowable itemized deductions is less than these amounts, the government will give you the higher standard deduction on your tax return and you don't have to save all of those receipts or fill out Schedule A as part of your tax return.

Example: In 2019 a married couple has a total of $23,000 of deductions, comprised of $8,000 mortgage interest, $10,000 state and local taxes, and $5,000 charitable contributions. For 2019, they will claim the higher $24,400 standard deduction. Assuming the same numbers for 2020 and 2021, the total standard deduction over the 3-year period will be $73,000 (not accounting for indexing in 2020 and 2021).

If instead, the couple set up a donor advised fund (DAF) and contributed 3 years' worth of contributions in 2019 (total of $15,000), they would have a total of $33,000 of deductions in 2019 ($8,000 + $10,000 + $15,000) and would be able to itemize the deduction for the year. They would make few, if any, additional contributions in 2020 and 2021 and would claim the $24,400 standard deduction in those years; for a total of $81,800 over the 3-year period. This is an added $8,800 of deductions over the 3-year period, which could translate into significant federal and state tax savings.

So how does a DAF work and why is it a good idea? First, a DAF is a tax exempt 501(c)(3) entity sponsored by either a community foundation or a charity, therefore your upfront contribution to the fund is fully tax deductible (subject to annual limits based on adjusted gross income, with a 5-year carryover provision for excess deductions). Setting up the fund is relatively easy as the sponsoring organization will generally provide the paperwork. In addition, there are no IRS applications, annual tax filings, or required distribution rules as would be the case if you instead created an endowment.

Second, to fund your DAF, you can contribute either cash or appreciated securities (which will avoid being subject to the capital gains tax). Like any other charitable contribution, once made, you no longer have use of the funds.

Third, assuming you fund the DAF in 2019, you don't have to immediately decide where the funds should be directed. Each year, until the funds are exhausted, you can advise the sponsoring organization (thus the term "donor advised" fund) how much of the earnings and principal you want to send to one or more charitable organizations, although you don't get a second charitable deduction when the funds are disbursed. In short, a DAF allows you to get an upfront deduction and decide later where you want to contribute the funds.

Some families set up donor advised funds with significant amounts to benefit a particular cause or field of interest, while some use it to fund various religious, educational and civic organizations. Since the fund is perpetual, many families use it as a way to involve children and grandchildren in philanthropic decision making, thus creating a family legacy.

For further information on this or other tax or charitable planning ideas, please contact Jordon Rosen at jrosen@belfint.com or at www.belfint.com.