The Power of Charitable Planning

Helping Your Clients Manage Good Deeds Through Better Giving

AMERICAN ENDOWMENT FOUNDATION
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Introduction

The number of donor-advised fund (DAF) accounts has continued to rapidly increase to over 450,000 nationally. Many individuals and families open accounts as more of their financial advisors, accountants, and attorneys recommend DAFs than they did ten or even just five years ago. Some donors open DAFs by initially contributing cash or publicly-traded stock, while others donate privately-held stock, limited partnership interests, real estate, or other complex assets.

Advisors have seen how receptive different types of clients are to the charitable conversation and to the idea of opening and using DAFs. Many advisors and their clients quickly understand how these funds are beneficial to them as well as the charities they support.

This Ebook is designed to help advisors better understand which clients may be an ideal fit to open a DAF, how to engage the clients in the charitable discussion, how the discussion is helpful to both the advisors and their clients, and how a charitable vehicle may be helpful or appropriate for the clients.

Types of Clients Who Are Opening Donor-Advised Funds

While ten years ago, most donors who created accounts were retired, the average age has been trending lower and a majority of new donors are under 65. Some advisors are still under the impression that primarily older clients would be interested, but the types of clients who have established DAFs in recent years include:

1. Clients who are approaching retirement since it is advantageous for them to make large donations while they are working and earning a large income. They also desire to do this so they can subsequently continue to make grants from their DAF account in retirement when their income is less.

2. Clients who have a pending liquidity event (i.e. sale of business/real estate/other asset or will inherit wealth).

3. Clients who have already retired or sold a business and now has the time, assets, and interest to get involved with charitable giving.

4. Clients who want to donate highly appreciated securities or assets with an unknown basis. Often advisors utilize these to create or fund DAFs when onboarding new clients or when looking to rebalance investments.

5. Due to 2017 tax law changes, many clients now bunch their donations in one year and make grants from their DAF over time.
6. Women, who are generally more charitably inclined and generous, now are earning more, living longer than men, and are controlling more money, especially after being widowed or divorced.

7. Couples or individuals without children who must decide what to do with their wealth in their remaining years or after death.

8. Clients who want to involve heirs in charitable planning, instill charitable values in them, or create a charitable legacy.

9. Clients with financially independent children, or who do not want to leave them too much.

10. Clients who have been impacted by an emotional trigger (illness, natural or manmade disaster, visit to impoverished area, etc.).

11. Younger clients who want to establish a baseline for giving that will grow over time, or who wish to involve their young children.

12. Clients who seek a simple, efficient, tech-savvy way to make charitable donations.

13. Millennials or entrepreneurs who want to give back and who will continue to earn a high income.

14. Clients who have been frustrated with cumbersome and costly foundations and seek simpler and less costly alternatives.

15. Clients who seek privacy and may wish to donate anonymously.

16. Clients who are disorganized with their giving, or who frequently ask their advisor to donate stock to many different charities.

Nearly all clients contribute to charities each year. Some should donate directly to charities and do not need a DAF or other charitable vehicle, while others would benefit significantly from creating a donor-advised fund. The rest of this Ebook will help advisors better understand how to have the conversation with clients as well as when a DAF may be most appropriate.
More than ever before, advisors and their clients have been talking about charitable planning. Recent tax law changes, the concept of bunching donations, the popularity of DAFs, the generosity of clients, the continued needs of nonprofit organizations, and the understanding that advisors can help clients have more of an impact are just some of the reasons why these conversations are increasingly taking place.

Advisors realize that these discussions are good for them, their clients, and the charities they support. Some of the reasons why so many advisors now understand that the conversation is beneficial to them and their practices include:

1. It enhances and deepens their relationships with clients.
2. It demonstrates to clients that their advisors are interested in them and not just in managing their assets.
3. It increases exposure to their clients’ spouse and children who will be more likely to remain as clients after the death of the wealth creator.
4. It differentiates them from other advisors and can be the difference-maker when a prospect is deciding between firms.
5. It helps bring in additional referrals from existing philanthropic clients.
6. It enables advisors to encourage donations of outside assets not under the firm’s control or of illiquid assets to the DAF, resulting in more assets that they can manage.
7. It allows for ongoing conversations about a positive and important topic to clients rather than market volatility and uncertainty, death, and taxes.
8. It reduces year-end stress upon advisors and associates by encouraging clients to make donations throughout the year rather than just in December.
9. It reduces the work of the advisors’ staff by recommending that clients donate stock to one donor-advised fund sponsor rather than to many charities, or by donating assets with difficult to ascertain cost basis which can take much time.
10. It helps to develop relationships with clients’ accountants and attorneys, and increases the likelihood that the financial advisors will be included in any discussion about charitable planning or in selecting a DAF sponsor where the advisors can manage the charitable assets.
11. It eliminates the likelihood that clients will set up a DAF account or other charitable vehicle on their own, or make charitable decisions that will prevent advisors from managing significant assets.

12. It creates the opportunity to help clients achieve an impact greater than they could have done on their own or in consultation with non-experts.

Advisors increasingly realize that nearly all of their HNW clients are already donating to charity, and that if they do not discuss charitable planning with clients, another advisor will. These deeper conversations help many advisors retain clients even when investment returns are subpar. And finally, understanding clients’ charitable plans and how these fit into their overall goals will enable advisors to provide clients with the most appropriate financial plan.

What Your Clients Need to Know from You About Better Giving

Most advisors today understand how the charitable conversation deepens client relationships and is an important topic to be discussed. As a result of the increasing number of these discussions, more clients are now more effectively and efficiently supporting their favorite charities.

Some advisors, however, have not yet engaged their clients in these conversations, possibly because their clients have not asked for help or they fear that their clients may not be receptive to the discussion. Since nearly all HNW clients give to charity, they would appreciate any input since this would help them give with greater impact.

Some of the benefits that clients would receive from the conversation include:

1. They may not realize that other assets besides checks or cash can and often should be the source for their charitable donations.

2. They may be missing significant tax benefits through annual and estate giving.

3. They can give even more to charity, give more to their family, or keep more themselves.

4. They can learn how to maintain their current level of annual giving to their favorite charities when their income varies from year to year, or the value of their investments drops in a particular year.
5. They can contribute to a DAF now and fund their future giving as they approach retirement, since they want to continue to support charities during retirement but fear their income and tax benefits will be less.

6. They may be receiving poor advice from friends, family, nonprofit staff, or other advisors and may set up an inappropriate charitable vehicle or a DAF that is very restrictive or does not allow their advisor to manage the assets.

7. They can make wise lifetime and legacy charitable decisions now since they are advancing in age and may be unable to make prudent decisions in the future.

8. They can discuss philanthropy with their children, include them in decisions and pass down their charitable values, and put together a plan to use charitable giving as a means to keep their family united after their deaths.

9. They can make changes to avoid being frustrated by having to keep track of numerous tax receipt letters from charities, receiving many solicitations from nonprofits, or deciding how, when, how much, and which assets to donate.

10. They can learn that they can go to giving portal at AEF and quickly make all of their grants to their favorite charities online and check their previous grants.

11. They may be overwhelmed or burdened by the responsibility of running their own private foundation, unhappy about the cost, and may be looking for a simpler or less expensive alternative.

12. They will be able to be proactive and plan their yearly giving in advance rather than procrastinate and make hasty decisions at the end of the year.

Some clients are not aware that they can turn to their advisors for help with many of these matters and feel they should just try to figure out the best charitable path themselves. As a result of these conversations, clients will feel a greater sense of confidence, satisfaction, and pride with their giving.
Increasingly, advisors have been talking about charitable planning with clients. Past US Trust studies indicated that clients felt that advisors did not bring up the subject frequently and that the conversation tended to revolve around the tax benefits of giving. Clients, on the other hand, felt that their interest and connection to various causes and charities were the primary reasons behind their philanthropy and that the tax benefits were far down the list.

More advisors have in recent years realized the benefits of having the charitable conversation with clients and are proactively engaging in this discussion. Additionally, the 2017 Tax Cuts and Jobs Act passed, and more clients have turned towards their advisors since they realized that there may be a better and more tax-efficient way to donate than in the past.

Though each situation may be different, some of the questions that advisors can ask current clients or prospects include:

1. “Are you involved with any charities now as a board member, donor, or volunteer?”
2. “Do you feel that you will become more or less involved or change the amount that you will donate to charities?”
3. “Did the 2017 Tax Cuts and Jobs Act change the way or how much you give?”
4. “Do you prefer to give during your lifetime, at death, or for many years after death? If after death, who will make the decisions?”
5. “Do you anticipate leaving any bequests to charities or to a charitable vehicle? Are you planning on making donations from your retirement accounts during your lifetime or upon death?”
6. “Who is involved in making the charitable giving decisions? Have you included your children or others, or do you plan on doing so?”
7. “Is a charitable legacy important to you?”
8. “How do you feel after making donations? Do you always feel satisfied and pleased or are there any frustrations with the giving process?”
9. “How do you decide how much to give each year?”
10. “How do you decide which charities to support?”
11. “Do you donate throughout the year or is there a rush to give at the end of the year?”

12. “Which types of assets do you typically donate each year?”

13. “Have you established any charitable vehicles such as a private foundation or donor-advised fund (DAF)? Did you set these up recently? Are these working well for you or do you have any concerns with them? How are these assets invested?”

14. “Do you prefer to give publicly or anonymously? To big organizations or small? To many charities or just a few?”

15. “Do you feel confident that your donations are having an impact?”

Because nearly all high net worth clients are active donors and are often passionate about their giving, the conversation is very natural as the clients understand that it will enable them to have a greater impact on the causes and charities that are of most importance to them. Though the tax benefits are not the reason they give, they want to learn how they can donate most efficiently. Since clients’ interests and plans change over time, this discussion should take place on a regular basis.

Many more DAFs than private foundations have been opened in the past decade. In 2010, there were approximately 75,000 foundations and 150,000 donor-advised fund accounts, but currently the foundation numbers have increased only to 82,000 while there are now over 450,000 DAFs. While foundations are still appropriate for certain clients, most advisors today indicate that a client should not begin to contemplate a foundation unless they would fund it with at least $10, $20, or $50 million, and even then, a donor-advised fund may be more appropriate.

Establishing either a DAF or foundation enables donors to make a large donation and receive the tax benefit at the time, and then make grants in subsequent years. This is especially helpful since many donors do not want to give too much to a charity at one time, and it allows them to provide consistent levels of funding over time since both their income and market performance may fluctuate annually. These vehicles can be used to help teach philanthropy and pass on family values to heirs.
DAFs have become far more popular than foundations for the following reasons:

1. There is no cost to open DAF and annual fees are minimal, while foundations are expensive to create and maintain.

2. Donor-advised funds can be opened within days while foundations can take months.

3. Clients can receive significantly higher tax deduction for donating certain assets to a DAF (i.e. Cash donation deductible up to 60% of AGI for DAFs vs. 30% for foundation, and other assets deductible up to 30% of AGI for DAFs vs. 20% for foundation).

4. Donors are generally entitled to a tax deduction of the full fair market value of a donation to a DAF for many complex assets, instead of the original cost basis that would be applicable to a private foundation.

5. No required annual tax filings for DAF accounts while foundations must file annual complicated 990PF and state filings.

6. No excise tax on investment income in DAFs, while foundations are subject to tax of 1.39%.

7. DAF donors’ anonymity is assured if desired, while all foundation grants can be viewed by the public and other charities.

8. DAF sponsors handle all grant administration, while foundations must be responsible for their own.

9. Donors want the simplicity that DAF sponsors provide as they are easy and efficient to use.

10. Many DAFs offer online granting and viewing of past grants and donations, while many foundations do not or must pay for this option.

11. DAF sponsors are responsible for complying with the laws, thus relieving donors of this burden. Foundations must keep official meeting notes, provide compensation benchmarking backup to IRS to justify salaries paid to family members, carry various types of insurance for board members, ask trustees to sign conflict-of-interest statements, etc.

12. No minimum annual distributions for DAFs, compared to 5% minimum for foundations.
Some donors are more comfortable in opening foundations for some of these reasons:

1. Grants are assured, not recommended, though most DAF sponsors approve nearly all grants.

2. They are not concerned about costs, complexity, or IRS oversight, or may desire the perceived greater status of having a foundation.

3. They can pay for expenses and hire and pay for staff including relatives, though IRS can review.

4. Foundations can grant to individuals in case of hardship if IRS criteria is met.

5. Can allow for more control over investment options, though AEF allows donors’ financial advisors to manage assets.

Clients are best served when their advisors discuss their charitable goals. They can help determine their clients’ desire for simplicity or tolerance of complexity, the timeframe for giving, who will be involved, how much clients want to invest in a structure for their giving, and why they want or need a charitable vehicle.

Advisors should determine whether clients need absolute control and don’t mind all of the regulations, requirements, responsibilities, and costs of a foundation, or whether a DAF can accomplish all of their goals. The best solution for some clients is to have both a foundation and a complementary DAF, and in recent years, many clients have closed their foundation and opened up a donor advised fund instead.

**Conclusion**

Discussing charitable planning with clients has become more prevalent both during good economic times when clients feel that they have more they can give, but also during downturns when clients still want to provide support to the charities they feel strongly about. Clients and their families, their advisors, and their favorite charities all benefit when the conversation takes place.