Donor-Advised Funds Are Essential to Democratizing Philanthropy

Kathleen Enright

It's no secret that there has been a lot of spirited debate about the role of donor-advised funds lately, and it's easy to understand why — many people have limited interactions with DAFs so they remain a mystery. I came to the Council on Foundations with nearly two decades of experience working in philanthropy. However, I admit I had never focused on DAFs in a significant way before assuming my role as chief executive.

At the council, I work closely with people and organizations that donate to, manage, and benefit from DAFs — especially community foundation leaders and nonprofits. The positive impact of DAFs was especially evident during the pandemic, when DAFs at community foundations quickly granted billions of dollars to relief and recovery efforts.

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But I also had some of the same concerns as DAF critics. I wondered: Do DAFs ultimately expand the resources available for charitable causes, or do they primarily serve as an instrument to reduce taxes for the wealthy? I questioned whether DAFs were well suited to the pursuit of a more inclusive, equitable society for everyone. I read headlines, many of which are part of the debate about the Accelerating Charitable Efforts Act, a measure introduced in the Senate, that appeared to show DAFs being used inappropriately and felt chagrined.

Based on what I have learned during my time at the council, I am now convinced that — while there is certainly room for improvement, particularly as an instrument to advance a more equitable society — DAFs are an essential tool to democratize giving and enable donors of all financial means to expand their giving capacity and sophistication over time.

Recently, a series of reports about DAF giving in 2020 were released, and they showed the same thing — record-high DAF grant payouts, the highest DAF payout rate in a decade, and DAF grant making growing faster than contributions to DAFs. In short, every measurable metric for DAFs showed more resources reaching nonprofits.

A Growing Force for Democratizing Philanthropy

DAFs play a role in democratizing philanthropy by giving more people access to a vehicle to expand their giving.

Last year, my 84-year-old father opened his first DAF. Initially he donated an amount equivalent to three years of his normal contributions so that he could benefit from a charitable tax deduction he would otherwise not receive. DAFs are a terrific option for American taxpayers who, like my father, take the standard deduction and therefore don't regularly receive a tax deduction for their giving (except for the temporary $300 deduction for non-itemizers that expired at the end of 2021). The tornados that recently devastated the western part of my home commonwealth of Kentucky motivated many, including my dad, to accelerate giving out of their DAFs.

Critics say DAFs are a piggy bank for the wealthy and that the donor gets the tax benefits of donating but isn't required to move the money out. But most DAF donors are more like my father than the ultrawealthy. The truth is that many DAF sponsors have low or no minimums for establishing a DAF so individuals at many different income levels can use a DAF to plan their giving over time.

When money in a DAF sits idle, the DAF-sponsoring organization should certainly act. In fact, the majority of DAF sponsors have policies governing inactive funds, including all those certified by National Standards for US Community Foundations, an accreditation program for community foundations affiliated with the council. The council encourages DAF sponsors to make sure their fund-activity policies are transparent and include a mechanism to make sure DAF assets are going to charitable purposes on a regular interval.

Critics argue that instead of encouraging donors to give to nonprofits, DAFs actually divert money away from charities. This criticism misses the mark on the fundamental premise of DAFs — once donated, the money is under the control of the community foundation or other DAF sponsor and irrevocably committed to charitable purposes. Donors can't reclaim the money or recommend charitable gifts for personal benefit. In fact, DAFs safeguard against donors engaging in illegal or unethical actions to gain undue benefits from their charitable activities.

Additionally, the best available national data shows that funds move out of DAFs at a high rate. Recent reports from the Giving USA Foundation and National Philanthropic Trust indicate that the DAF payout rate has remained well above 5 percent — in some cases more than 20 percent — for every year on record.

Adding to this is emerging evidence that DAFs are an effective form of countercyclical giving.

When times are tough, it is harder to raise new funds from individual donors — but money in DAFs has already been committed and is therefore insulated from financial uncertainty and tighter personal budgets.

The Covid-19 crisis illustrates this point. In response to urgent needs arising during the pandemic, in 2020, DAF grants to nonprofits surpassed $30 billion for the first time and represented the highest payout in a decade, according to the newest report from the National Philanthropic Trust. Though both grew substantially, money moving out of DAFs grew 7 percent faster than contributions going to DAFs.

Patient Giving Can Multiply Impact

Even though the needs right now are visible and urgent, the truth is that communities need a healthy mix of funds to address current and future challenges.

As we have seen, some DAFs have high payout rates, which provide critical funds in times of unexpected need. But long-term challenges, like finding cures for diseases and creating accessible, affordable neighborhoods, require a committed and patient approach, which is why endowed DAFs constructed for a sustained level of long-term giving are also critical. These kinds of DAFs provide capital to address emerging community needs and multiply the volume and impact of the original donation. It is shortsighted to assume future generations of donors will be there to address long-term issues.

Take, for example, a DAF sponsored at a community foundation in upstate New York that started with an original principal of $100,000 in 1987. Over the last 34 years, this DAF has distributed grants of more than 200 percent of its principal. And because the original principal has grown, this DAF can keep growing its giving for the foreseeable future. There are many more cases like this across the nation, and these kinds of DAFs play an important role in the philanthropic ecosystem in ensuring and increasing giving for long-term challenges.

So What Comes Next?

Proponents of the ACE Act suggest this legislation will advance equitable outcomes and ensure more resources are flowing to the communities and nonprofits that have previously not received a fair share. And yet the forcing mechanisms in the ACE Act are unrelated to that objective. DAF sponsors and DAF holders can and do contribute to building a more inclusive, equitable society when they are clear about their values, including equity, and align their giving with those values.

With an ultimate goal of making it easier for more everyday donors, like my dad, to give larger amounts to charitable causes for the long term, DAFs are an important part of the solution.

Some concerns over DAFs are valid and warrant changes in practice and policy. These changes must be guided by organizations operating in real-world conditions and backed by credible national data. This is why the council continues to actively consult with members and a diverse range of other key players to arrive at policy recommendations that increase the size and impact of, as well as the trust in, philanthropy. This is also why the council:

- Supports a permanent charitable deduction that includes people who don’t itemize on their tax returns. If we want to see more giving to working charities and increased advocacy for — and resources reaching — those most burdened by systemic inequity, strengthening giving incentives for all taxpayers holds greater promise than the ACE Act.
- Believes we need holistic, national data on DAFs so that we are not debating policies of national significance based on anecdotes or studies focused on a single state. We encourage the U.S. Department of the Treasury to update data on DAFs and, where gaps exist, to seek data that better informs the nonprofit world and policy makers.
- Advocates that all DAF sponsors adopt an inactive-funds policy that establishes guidelines for what to do with a dormant DAF. The council also encourages organizations that already have one in place to strengthen their policy and demonstrate their commitment to good practice by becoming accredited through National Standards for U.S. Community Foundations.

Last year the Council on Foundations convened a group of community foundation leaders to develop recommendations to address some of the concerns about DAFs. We will share these recommendations in the coming weeks, and we remain committed to finding ways to enhance public trust in philanthropy. One way to do that is to ensure the nation continues and expands incentives so that everyone will get involved in giving that strengthens our multicultural, pluralistic society for generations to come.

https://www.philanthropy.com/article/donor-advised-funds-are-essential-to-democratizing-philanthropy