

FREQUENTLY ASKED QUESTIONS ABOUT DONOR ADVISED FUNDS

A Resource for Grantmakers, Donors and Advisors

Updated as of February 2023

This information is provided by Ask CMF, a technical assistance service of the Council of Michigan Foundations, for educational purposes only and does not constitute legal advice.

Grantmakers, donors and their advisors regularly reach out to CMF to learn more about donor advised funds (DAFs). While DAFs have been a philanthropic tool available to individuals, families and companies for decades, they have been increasingly popular over the last ten years. Between 2017 and 2021, contributions to DAFs grew from \$31.38 billion to \$72.67 billion, now comprising approximately 15.0% of all giving in the United States.¹

This resource is intended to explore frequently asked questions involving donor advised funds. Please note that DAFs are a continued topic of regulatory debate, and federal and/or state rules that affect the operation of DAFs are subject to change.

Due to CMF's work with community foundations in their capacity as sponsoring organizations that hold DAF accounts, this resource refers to "sponsoring organizations" based on community foundations serving as DAF sponsors. Donors and advisors working with other types of DAF sponsors should contact their account representative to understand their applicable policies and procedures.

Individuals and companies interested in establishing a DAF should contact sponsoring organizations directly to learn more about their unique DAF program. To find a community foundation in Michigan, visit [CMF's list of community foundation members](#) or contact CMF to learn about the community foundation serving your geographic region.

¹ National Philanthropy Trust, [2022 Donor-Advised Fund Report](#).

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TYPES OF DONOR ADVISED FUNDS

Donor Advised Fund (DAF): A DAF is housed at an external “sponsoring organization,” such as a community foundation. Individuals making gifts to DAFs can receive tax advantages for their gifts, similar to contributions to other public charities. Donors may use their DAF to make periodic distributions to qualified charitable organizations (typically 501(c)(3) organizations). All donations are legally subject to the approval of the sponsoring organization that holds the DAF. Most DAFs are held by a sponsoring organization on behalf of an individual, family, charity, other type of nonprofit or corporation.

Advantages: Relatively easy to establish within a sponsoring charitable organization, which also manages specific back office functions of grantmaking (i.e., processing grants, sending funds to grantees). Limited administration and no required tax returns. Community foundations and other sponsoring organizations offer community-based knowledge and grantmaking expertise to recommend new charitable organizations to DAF holders to meet their philanthropic goals. Potential alternative to private foundation.

Disadvantages: Donors have limited control to advise where these donations will be made, depending upon the rules of the sponsoring organization, many of which do not permit grants to non-charities or to charities that may be seen as “controversial.” Control is held by the sponsoring organization. Direct scholarship grants are only permitted if donor/advisor and related parties do not control the selection committee. Many sponsoring organizations limit donor influence to approximately two generations beyond establishment of fund (although that is not a legal requirement). Subject to many of the private foundation restrictions. (See [“What are the private foundation concepts that apply to DAFs?”](#))

Corporate Donor Advised Fund (DAF): A corporate DAF is housed at an external “sponsoring organization,” such as a community foundation. Similar to other types of DAFs, this fund receives periodic donations from the corporation (or other organization), which are then distributed on a regular basis. All donations are legally subject to the approval of the sponsoring organization that holds the DAF. A DAF may be the preferred giving vehicle rather than establishing a corporate foundation or giving program. For information on alternative forms of philanthropy available to individuals, families and corporate entities, see CMF’s resources [“Options for Your Financial Giving”](#) or [“Choosing a Corporate Philanthropy Approach.”](#)

Advantages: Relatively easy to establish within a sponsoring charitable organization, which also manages specific back office functions of grantmaking (i.e. processing grants, sending funds to grantees).

Disadvantages: Corporation has limited control to advise where these donations will be made (depending upon the rules of the sponsoring organization, many of which do not permit grants to non-charities or to charities that may be seen as “controversial”). Control is held by the sponsoring organization. Direct scholarship grants are only permitted via a sponsoring organization if donor/advisor and related parties are not in control of the selection committee. There are restrictions on the use of the fund’s name, requiring clarification that it is a fund at the sponsoring organization. Subject to many of the private foundation restrictions. (See [“What are the private foundation concepts that apply to DAFs?”](#))

A COMPARATIVE CHART OF DONOR ADVISED FUNDS

While many DAFs held by sponsoring organizations are derived from the donations of individuals and families, some accounts are created by corporate entities, such as local businesses or multi-state corporations. Other organizations that create a DAF – whether a 501(c)(3) or a non-501(c)(3) organization – would follow the “Corporate DAF” model. The rules for DAFs are generally the same across both categories. However, sponsoring organizations may establish and impose rules differently between individual/family DAF accounts and corporate DAF accounts.

	Individual/Family DAF	Corporate DAF
Legal Structure	The sponsoring organization has ultimate “discretion and control” of the funds once they are donated. Donors can advise regarding fund recipients but do not have legal control over them or ownership of them.	The sponsoring organization has ultimate “discretion and control” of the funds once they are donated by the corporation. Corporation can advise how the funds are distributed but does not have legal control over or ownership of them.
Lifespan	DAFs typically last for one to two generations beyond the original donor. After this point they are typically absorbed into the sponsoring organization’s general or category-based (field of interest) funds.	Due to the corporate entity serving as the original donor, a corporate DAF does not have a limited lifespan or “successive advisors.” Instead, the corporate entity and its executives serve as the ongoing representatives of the DAF.
Leadership	<p>A donor can serve as an advisor to the fund, with the ability to recommend grants from the DAF. Depending on the sponsoring organization’s existing policies, the advisor may also make recommendations regarding the general investing strategy for the fund.</p> <p>DAFs have specific rules that restrict any benefit to DAF holders, including the donors, their family members, advisors and other related entities.</p>	<p>The company or its representative can serve as an advisor to the fund, with the ability to recommend grants from the DAF. Depending on the sponsoring organization’s existing policies, the advisor may also make recommendations regarding the general investing strategy for the fund.</p> <p>DAFs have specific rules that restrict any benefit to DAF holders (including the corporation itself), corporate leadership, their family members, advisors and other related entities.</p> <p>In the case of a corporate merger, the DAF would remain with the newly-formed entity, but the advisor(s) is not implied in that transition and would need to be determined. For a sale or merger, the DAF’s advisor would need to</p>

		be negotiated between the two entities, similar to a corporate foundation.
Administrative Costs and Set-up	DAFs are relatively quick and easy to establish. The sponsoring organization will have an established process for creating a DAF, including set administrative fees (typically a percentage of the amount of the DAF). Process and criteria may vary by sponsoring organization.	The sponsoring organization will have an established process for creating a DAF, which is typically relatively quick and easy. The sponsoring organization will identify administrative fees (typically a percentage of the amount of the DAF). Process and criteria may vary by sponsoring organization.
Recommended Minimum Size	Sponsoring organizations set the minimum donation required to establish a donor advised fund. DAFs frequently require a minimum donation of \$5,000-\$10,000, although some sponsoring organizations may have a higher minimum.	Sponsoring organizations set the minimum donation required to establish a donor advised fund. DAFs frequently require a minimum donation of \$5,000-\$10,000, although some sponsoring organizations may have a higher minimum.
Funding	Donors can provide a contribution of funds or assets to the sponsoring organization at their convenience, at one time or periodically. Donors making gifts to the foundation have a tax deduction rate of 50% of adjusted gross income for gifts of cash and 30% for gifts of stock or property. ² These funds are then held in the DAF and can be distributed over time, in keeping with the rules set by the sponsoring organization, which may include a minimum payout. There is no universal legally mandated payout as with a private foundation.	The corporation can provide a contribution of funds or assets to the sponsoring organization at its convenience, at one time or periodically. (As the sponsoring organization is a public charity, the corporation can take a charitable deduction ³ ; greater deductions for some non-cash contributions versus private foundations.) These funds are then held in the DAF and can be distributed over time, in keeping with the rules set by the sponsoring organization, which may include a minimum payout. There is no universal legally mandated payout as with a private foundation.
Grantmaking	To Domestic Public Charities: Allowable. To Private Foundations: Allowable with expenditure responsibility and so long as there is no control by the donor, advisor or their family members, however this is considered generally inadvisable in the field. Many DAF sponsors refuse to make	To Domestic Public Charities: Allowable. To Private Foundations: Allowable with expenditure responsibility and so long as there is no control by donor, advisor or their family members. Considered generally inadvisable in the field. Many DAF sponsors refuse to make grants to private non-operating foundations.

² Deductibility rules and limits may vary based on special legislation. CMF recommends that donors or DAF holders consult with qualified legal or tax counsel to understand the current limits on charitable deductions.

³ Ibid.

	<p>grants to private non-operating foundations.</p> <p>To Foreign Charities: Allowable with expenditure responsibility or equivalency determination. Some DAF sponsors refuse to make international grants.</p> <p>To Individuals in Need: Not allowed to make contributions to individuals.</p>	<p>To Foreign Charities: Allowable with expenditure responsibility or equivalency determination. Some DAF sponsors refuse to make international grants.</p> <p>To Individuals in Need: Not allowed to make contributions to individuals.</p> <p>Employee Giving/Volunteering Programs: Generally, not involved with employee giving and volunteering programs, although special arrangements may be made if the sponsoring organization consents to do so. Additional fees may be involved.</p>
Lobbying	DAF holders may not earmark funds for lobbying, however they may support other advocacy activities and support charities that lobby.	DAF holders may not earmark funds for lobbying, however they may support other advocacy activities and support charities that lobby.
Scholarships and Grants to Individuals	Scholarships and grants to individuals are not allowable under the IRS regulations for DAFs, but would be permitted in another type of fund at a sponsoring organization (such as a community foundation) so long as exemptions to the DAF definition provided in Internal Revenue Code (IRC) 4966 are followed. (See “Can a DAF support scholarships?”)	Scholarships and grants to individuals are not allowable under the IRS regulations for DAFs, but would be permitted in another type of fund at a sponsoring organization (such as a community foundation) so long as exemptions to the DAF definition provided in Internal Revenue Code (IRC) 4966 are followed. (See “Can a DAF support scholarships?”)
Disaster Grantmaking and Community Relief Efforts	General rules for DAFs apply, including the ability to make grants in the case of federally qualified disasters. (See CMF’s “Frequently Asked Questions About Disasters” resource)	<p>General rules for DAFs apply, including the ability to make grants in the case of federally declared disasters. (See CMF’s “Frequently Asked Questions About Disasters” resource)</p> <p>For Corporate Employees: General rules for DAFs apply, however a federally-declared disaster allows for the one exception to employer-sponsored DAFs to support individuals, specifically employees and their families who are the victims of a qualified disaster. (See “Employee Assistance Programs” within CMF’s “Choosing a Corporate Approach” resource.)</p>

<p>Event Sponsorships</p>	<p>There is a strict prohibition on DAF grants providing any benefit back to the donor or any advisor (or their respective family members). The DAF sponsoring organization may prohibit payment of sponsorships where tickets are involved or may prohibit acceptance of tickets.</p>	<p>There is a strict prohibition on DAF grants providing any benefit back to the donor or any advisor (or their respective family members). The DAF sponsoring organization may prohibit payment of sponsorships where tickets are involved or may prohibit acceptance of tickets.</p> <p>While the DAF itself may carry the name of the company, the sponsoring organization likely has restrictions on the use of the fund’s name. Typically sponsoring organizations require that any time the corporation uses the DAF’s name it must clarify that it is as a fund at the sponsoring organization and not imply it is a stand-alone entity.</p>
<p>To Learn More</p>	<p>For more information, see CMF’s “Options for Your Financial Giving” resource.</p>	<p>For more information, see CMF’s “Choosing a Corporate Philanthropy Approach” resource.</p>

DONOR ADVISED FUNDS BASICS

What is and is not a donor advised fund (DAF)?

The concept of a Donor Advised Fund (frequently referred to as a “DAF”) is outlined in the Pension Protection Act of 2006 and the Internal Revenue Code (IRC) Section 4966. DAFs are accounts or funds with the following attributes:

1. Separately identified by reference to contributions made by a donor or donors.
2. Owned and controlled by a sponsoring organization, such as a community foundation or other public charity that holds DAFs.
3. The donor (or their designee) has, or reasonably expects to have, advisory privileges with respect to the distribution or investment of amounts held in such fund or account.

Both the Pension Protection Act of 2006 and IRC Sec. 4966 provide for a number of exceptions, which constitute accounts or funds held by sponsoring organizations that are not considered to be DAFs.

1. A fund that only makes grants to a single pre-identified organization or governmental unit.
2. A fund that meets all of the following criteria:
 - a. A person serves in an advisory capacity as part of a committee, where all of the committee members have been appointed by the sponsoring organization.
 - b. The donor, advisors appointed by the donor and related persons do not control (make up a majority of) the committee advising the fund.
 - c. The advisory committee uses a pre-established set of objective and nondiscriminatory criteria for its grantmaking decisions that have been pre-approved by the sponsoring organization’s board of directors.⁴

Based on definitions and distinctions established in the Pension Protection Act and IRC Sec. 4966, the following are examples of a DAF:

- A donor establishes a fund in memory or honor of his/her spouse at a local community foundation and maintains direct advisory privileges over grants made from the fund.
- A married couple establishes a fund at their local community foundation, where they make regular donations into the fund and recommend grants to a variety of charitable organizations out of the fund.
- A donor establishes a fund at a local community foundation and makes a significant initial donation, followed by a series of smaller donations in later years. Over a matter of decades, the donor, their lawyer and adult children recommend regular grants to charitable organizations out of the fund. After the original donor’s death, their children, grandchildren and additional appointed representatives continue to advise the foundation regarding grants generated from the fund.
- A donor makes a planned gift through their estate with the intent to establish a fund at a community foundation. The donor’s children, grandchildren and/or advisors are designated as

⁴ This criteria is consistent with the legal language used to describe scholarship funds. However, it also applies to most standard criteria for grantmaking to charitable organizations.

members of the advisory committee that makes annual grants out of the fund to benefit local charitable organizations.

- An organization (i.e., chamber of commerce, fraternal organization) establishes a fund at their local community foundation in its own name intended to benefit charitable organizations in the area. The organization establishes an advisory board made up of its members, board or other affiliated individuals.
- A corporation establishes a fund at a community foundation through periodic donations. The corporation establishes an advisory board of corporate leaders and employees to recommend grants benefitting charitable organizations in the community.

The following fund examples are **not** DAFs:

- A fund that receives contributions from a number of unrelated donors, the funds are not tracked by reference to a gift of any individual member of the group, and grant recommendations are a group decision (i.e., a fund created by a giving circle). Note that although memorial funds generally have several donors, if the fund is tracked by reference to the decedent and the decedent's family members will provide the advice, this should be treated as a DAF unless it falls under one of the DAF exceptions (i.e., scholarship fund or a fund designed for a single, charitable organization).
- A fund established at a community foundation that utilizes an advisory committee where the donor and related parties constitute less than a majority of the committee and all committee members are nominated by the sponsoring organization.
- A fund established at a community foundation designated by a donor to support a single charitable organization, such as a local historical society or regional humane society. (This is likely to be categorized as a designated fund.)
- A scholarship fund established by a donor at a community foundation, where an advisory committee is established by the community foundation and the donor (and related parties) constitute less than a majority of the committee members.
- A fund established by a donor at a community foundation where the advisory committee is made up of the donor and the majority of committee members meet expertise-based objective criteria related to the fund's purpose, even if these members are initially recommended by the donor. (The difference here is that the donor appoints the committee member *ex officio*, or by reason of their position (such as high school principal), as opposed to named individuals.)
- A fund established by a donor's planned or estate gift to create or support a fund at the community foundation, focused on a general field of interest (i.e., arts and cultural organizations, health, environmental concerns in the local area) and where the community foundation establishes an advisory committee (of internal and/or external members) to determine appropriate grants, following objective and non-discriminatory criteria for determining relevant grant recipients and projects.
- A fund established or supported in part by a corporation or organization at a local community foundation and where the corporate leaders and/or staff comprise less than a majority of the advisory board.

What is a sponsoring organization?

Donor advised funds function as “component funds” within a sponsoring organization and cannot function separately from the organization in which they are housed. Oftentimes, DAFs may be referred to as “accounts” within the sponsoring organization. The DAF sponsoring organization and its staff and/or board have ultimate jurisdiction (“discretion and control”) over the DAF account, while the donor and/or advisors can only recommend grants and sometimes choose an investment strategy for the account.⁵

Examples of sponsoring organizations include community foundations, religiously-affiliated DAF providers (i.e., Jewish Federation, Catholic Foundation) and national DAF providers, such as commercially-affiliated organizations associated with banks or other financial institutions or other nonprofit entities that serve a national market with DAF products.

A community foundation is a nonprofit grantmaking institution funded by a large group of donors to support their charitable interests within a geographic region. Michigan-based community foundations are established with the intent of serving the charitable needs of a specific geographic region, most commonly a county or multi-county area. They use an endowment (consistent with the accounting definition of the term) to ensure the presence of a permanent investment fund and the perpetual (“forever”) nature of the community foundation.

Donors can make gifts to community foundations similar to any other public charity, benefiting from the maximum charitable deduction available for gifts to most other public charities. Donors may also establish a donor advised fund at their local community foundation or choose to support other funds held by the foundation. For example, community foundations have organized funds designed to support fields of interest (i.e. arts, human services, etc.) and specific nonprofits within their designated geographic region, as well as hold scholarship funds intended to benefit broad categories of intended recipients.

Community foundations charge a relatively small administrative fee for establishing a fund, as the organizations’ staff handles back office and investment activities, allowing donors to focus on achieving their charitable goals. Those interested in creating a new donor advised fund or supporting an existing fund at a local community foundation should contact the organization directly for more information about giving opportunities and fund requirements. To find a community foundation in Michigan, visit [CMF’s list of community foundation members](#) or contact CMF to learn about the community foundation serving your geographic region.

What is a DAF advisor?

One of the three required attributes of a DAF listed in IRC Section 4966 is: “a donor (or any person appointed or designated by such donor) has, or reasonably expects to have, advisory privileges with respect to the distribution or investment of amounts held in such fund or account by reason of the

⁵ The option for donors to choose an investment strategy for their DAF is available at some but not all DAF sponsoring organizations and may be dependent on the relative size of the DAF account and/or sponsoring organization.

donor’s status as a donor.” As such, each DAF account has at least one “advisor” who recommends grants and/or investment strategy specific to the DAF. The initial advisor may be the original donor(s), family member(s), corporate representative or someone affiliated with the original institution that provides the funding into the DAF.

DAF advisors can only advise the sponsoring organization regarding their grants. The DAF sponsor’s staff and/or board can choose to carry out the advisors’ wishes or decline them, oftentimes on the basis of internal policies and external regulations.

As part of the DAF fund agreement, most DAF sponsoring organizations will require that the original donor choose a successor advisor, who is responsible for the DAF after their death. Most organizations will allow DAFs to continue for one or two generations beyond the original donor. Due to practical limitations and declining interest and involvement by donors’ representatives over time, the charitable sector has accepted the one or two generations limit as best practice. Additionally, the presence of “Inactive Fund Policies” (see [“What is an Inactive Funds Policy?”](#)) as a requirement of the National Standards for U.S. Community Foundations program has mandated that all DAF accounts actively grant funds out to charitable entities, ensuring the presence of a committed advisor or advisors associated with each DAF account.

In the case of a corporate DAF, the DAF continues to be advised by a representative of the company, even in the case of a change in the corporate ownership. DAFs held by a community foundation on behalf of another institution (i.e., 501(c)(6) or 501(c)(3) organization) should have designated representatives that make grantmaking decisions on behalf of the DAF account.

What is a fund agreement?

Fund agreements are the legal documents used by community foundations and other DAF sponsoring organizations that outline the agreement between the original donor and the DAF sponsor. The exact language of these agreements and their adherence to other relevant policies (i.e., those required by the National Standards for U.S. Community Foundations program) depend on the particular sponsoring organization.

Donors may have the ability to make decisions regarding the following elements of their DAF, depending on the options available at the DAF provider of their choice:

- **Endowed vs. Spendable (Non-Endowed):** Endowed DAFs are designed to continue in perpetuity, based on a required minimum size of account that is invested by the DAF provider. Spendable (non-endowed) DAF accounts can be spent down to a very small amount (oftentimes \$0) and replenished by the donor at any time. Some DAF providers offer endowed and/or spendable account options. These options may vary by region, provider, or size of the account. (See [“What is an endowed or spendable \(non-endowed\) DAF?”](#) for more information.)
- **Fund Advisors:** Those persons with an ability to provide advice as to grants from, or investment of, DAF assets. DAF advisors are appointed by the donor and often include the donor. Donors typically appoint their family members as advisors. Typically, sponsoring organizations permit only one or two successor advisors (including in those cases where generations of family

members are appointed as additional advisors), although this often does not apply to DAFs established by corporations. Additional advisors may be predesignated by the original donor.

- **Final Recipients:** In addition to the inactive funds policy, DAF sponsors should provide alternative options in the fund agreement for situations that may arise, i.e., if the sponsoring organization can no longer reach any of the advisors after a certain amount of time, if the DAF fund size reaches the minimum fund balance of the sponsoring organization (if it has one), or if the DAF donor no longer has the ability to appoint successor advisors pursuant to the sponsoring organization's rules. This could take the form of a field-of-interest fund held by a community foundation, a general/operating fund of the foundation, or a final grant to a designated charitable entity or entities.

Changes to a fund agreement can only be made with the permission of the original donor, with limited changes allowed by the DAF provider via variance power.⁶

Sample fund agreements for donor advised funds and other fund types are available to CMF members at: <https://www.michiganfoundations.org/resources/fund-agreements-sample-documents>

What happens to DAF funds after the last generation of advisors?

Depending on the fund agreement template language used by the community foundation, a DAF may be directed to a field of interest or designated (organization-specific) fund after the advisory period ends. The number of successor advisor appointments may vary significantly between community foundations. Donors and advisors should be aware of these limits in advance.

If a fund agreement does not outline the intended use of the DAF account's remaining assets (i.e., a specific fund), the community foundation can choose to absorb it into a general fund, award it to organizations that have received prior grants from the DAF or direct it to a field of interest fund or another means of aligning the final contributions within the scope of the donor/advisors' previous priorities. This may require the exercise of variance power. Community foundations should have a policy or procedure in place that outlines how these situations are handled, especially in the case that it is not otherwise included in the fund agreement.

How does a DAF function?

Donor advised funds are component funds that function within a DAF sponsoring organization, such as a community foundation. Once the original donor makes their donation and signs a fund agreement with the DAF provider, the DAF account follows the policies and procedures of the sponsoring organization.

- **Back Office Functions:** A sponsoring organization conducts the back-office functions for the funds held within the organization, including accounting, grant application management, grantmaking, reporting and investing of the assets. The sponsoring organization also ensures that the fund follows state and federal regulation. The costs of these activities are covered by a

⁶ For more information, see CMF's "Frequently Asked Questions About Fund Agreements," <https://www.michiganfoundations.org/resources/faqs-about-fund-agreements>.

fee; the fee structure is established when the fund is established per a written fund agreement document, although this fee may change over time.

- **Legal Oversight and Ownership:** The sponsoring organization has discretion and control over the fund. While a family or committee of individuals may recommend grants or advise a fund, the sponsoring organization has final determination over the activities of the fund (including fundraising and gift acceptance, as well as grantmaking). Once the sponsoring organization accepts transfer of the assets and creates a fund, the assets are then legally owned and held by the community foundation and cannot be returned.
- **Policies and Procedures:** The sponsoring organization sets the policies and procedures for all funds held within the institution, including grantmaking cycles, lifespan of the funds, payout rates, fees, fundraising/gift acceptance policies, data protection and others. While many community foundations within the state of Michigan are certified by the National Standards for U.S. Community Foundations program, which requires certain policies and procedures be put into effect, the exact language used within policies and other procedural documents may vary from one organization to another. Individuals are advised to discuss the relevant policies and procedures that may impact their potential fund with their DAF account's sponsoring organization.
- **Grantmaking:** Although donors and advisors are permitted to recommend grants, the sponsoring organization will vet the proposed grantees to make sure that they meet legal requirements as well as policy requirements of the sponsoring organization and will manage grant distribution and complete any required documentation.

Please note that DAFs are a continued topic of discussion for a number of regulatory bodies, and as such, federal and/or state rules that affect the operation of DAFs are subject to change.

What are the private foundation concepts that apply to DAFs?

With passage of the Pension Protection Act in 2006, many of the private foundation rules regarding tax distributions, jeopardizing investments and excess business holdings apply to DAFs. DAFs are also subject to the excess benefits transactions rules.⁷

Taxable Expenditures: Under IRC Section 4966, DAFs may not make any grants for non-charitable purposes and, unlike private foundations, may not make any grants to individuals, and the sponsoring organization and potentially foundation managers may incur a tax for an improper grant from a DAF. DAFs may only make grants to U.S. public charities (or certain governmental entities) unless they exercise expenditure responsibility (although certain grants to supporting organizations are not permitted). DAFs may make grants to its sponsoring organization and to other DAFs.

Excess Business Holdings: The private foundation rules on excess business holdings in IRC Section 4943 apply to DAFs, except that "disqualified persons" means the donor, any DAF advisor, the family members of the donor or any advisor, and entities of which 35% of the interests are controlled by any of these people.

⁷ IRC Section 4958 and Section 4967.

A DAF and its disqualified persons together can only hold up to a certain amount (typically 20%) of the voting shares or membership interests in a business enterprise, with a limited amount of time to divest their excess holdings. Similar to private foundations, DAFs are required to ask their disqualified persons about their holdings in any securities in which the foundation owns more than 2% of the overall voting shares or membership interests.⁸ The sponsoring organization and certain insiders may incur excise taxes for violating these rules.

Excess Benefits Transactions: IRC Section 4958 and Section 4967 prohibit disqualified persons to the DAF and also investment advisors to the sponsoring organization (including with respect to the DAF) from receiving more than an incidental benefit from the DAF. This is even more strict than the private foundation self-dealing rules. (See "[Can a donor receive any personal benefit from a DAF grant?](#)")

Does variance power apply to DAFs?

Yes. Variance power is a legal means through which a DAF sponsoring organization can modify restrictions on component funds (including DAFs) in the case that the existing structure (fund agreement restriction) becomes unnecessary, unable to be fulfilled or no longer consistent with the charitable needs of the geographic community served by the foundation.

Please note that National Standards for U.S. Community Foundations requires that variance power be noted in each fund agreement, in addition to being included within a community foundation's governing documents.

For more information, see CMF's "Frequently Asked Questions About Fund Agreements," <https://www.michiganfoundations.org/resources/faqs-about-fund-agreements>.

GRANTMAKING

Can a DAF be used to support a scholarship or make a grant to an individual?

DAFs may not be used to make grants directly to individuals, including scholarships. Therefore, a donor wishing to establish a scholarship fund in which they may participate in the decision making must make sure that it complies with the noted exception for DAFs (see "[What is and is not a DAF?](#)"). DAFs may make grants to other organizations, such as schools, universities or community foundations for the purpose of a scholarship program controlled by the charitable institution. However, the DAF cannot make a gift to a university for the benefit of a particular individual, and DAFs cannot be used to satisfy binding pledges.

Depending on a community foundation's policies and procedures, a DAF donor may be allowed to sit on a scholarship fund selection committee. However, the donor, DAF advisors and their respective family members would not be allowed to constitute a majority of those deciding on scholarship recipients for a

⁸ This is a heuristic that most foundations follow, keeping below 2% ownership unless it is a passive investment entity, since the excess business holdings rules only apply to operating, non-functionally related businesses.

fund that they support. This means that the donor (and their DAF advisors/family members) cannot have control over the fund, regardless of whether the funds originate from a DAF or not.

For more information on scholarships, see “Navigating Scholarships and Grants to Individuals” (<https://www.michiganfoundations.org/resources/navigating-scholarships-and-grants-individuals>).

Can a DAF make a grant to a non-501(c)(3) organization?

Grants from DAFs can be used to support non-501(c)(3) organizations, but only for particular charitable purposes (no general operating support grants) and within the guidelines of the DAF sponsoring organization. However, they must exercise expenditure responsibility in compliance with the Internal Revenue Code, comparable to the process required for private foundations.⁹ In these cases, there can be absolutely no tangible benefit back to any donor, advisor, family members or certain other related parties.

Can a DAF make an international grant?

Each DAF sponsoring organization may have an established policy or procedure regarding whether international grants can be made by a DAF or may outline a minimum gift amount. DAFs do have extra requirements for international grants, including either expenditure responsibility or equivalency determination. Additionally, organizations engaged in international grantmaking must follow procedures to comply with OFAC, Patriot Act and similar laws aimed at preventing the funding of terrorism, and they must determine whether withholding of a portion of grant funds is required for tax purposes.

For more information, see CMF’s resource “[Frequently Asked Questions About Fund Agreements.](#)”

Can a DAF be used to support disaster response?

Yes, donor advised funds can be used to support disaster response.

Generally, DAFs can follow many standard rules and restrictions even during a disaster, especially when used to provide support through domestic public charities. Expenditure responsibility may be required for grants to supporting organizations and is required for grants to non-501(c)(3) organizations. Grants to organizations outside of the U.S. may have additional requirements.

Further, there is an exception to the DAF prohibitions for certain employer-related funds established to benefit employees and their family members who are victims of a federally qualified disaster. In the event of a federally qualified disaster (as defined in IRC Section 139), a DAF may make grants to employees and their family members in the following circumstances:

- (i) The fund serves the single identified purpose of providing relief from one or more qualified disasters;
- (ii) The fund serves a charitable class that is large enough so as to be “indefinite”;
- (iii) Grants are selected based upon an objective determination of need;

⁹ For information on expenditure responsibility requirements for DAFs and private foundations, see the Internal Revenue Service website for more information (<https://www.irs.gov/charities-non-profits/private-foundations/grants-by-private-foundations-expenditure-responsibility>).

- (iv) The selection of recipients of grants is made using either an independent selection committee or adequate substitute procedures to ensure that any benefit to the employer is incidental and tenuous (meaning that a majority of its members must consist of persons who are not in a position to exercise substantial influence over the employer's affairs);
- (v) No payment is made from the fund to or for the benefit of any director, officer, or trustee of the sponsoring organization or any member of the selection committee; and
- (vi) The fund maintains adequate records to demonstrate the recipients' need for the disaster assistance provided.

For more information on disaster grantmaking by DAFs and other philanthropic entities, see CMF's ["Frequently Asked Questions About Disasters"](#) resource.

Can a DAF make an anonymous gift?

Under current regulations, DAF accounts are allowed to make "anonymous" gifts. However, the options for anonymity may vary by DAF sponsoring organization. For example, a grant recipient may only know that the gift originates from the DAF sponsoring organization, without specifying the exact DAF account name or donors. Alternatively, the DAF account name may be used, rather than the names of the family/advisors.

Please note that DAF accounts cannot appear to function independently of the sponsoring organization. As a result, most DAF providers have strict policies that outline naming conventions for the acknowledgement of DAF gifts by grantees. For example, a gift from a DAF may appear in a nonprofit's list of donors as "XYZ Donor Advised Fund: A Fund of the ABC County Community Foundation."

May a DAF make a gift to the sponsoring organization?

DAF accounts held by community foundations may make contributions to the sponsoring organization. Contributions to scholarships can only be made to funds where the DAF donor and their representatives comprise less than a majority of the scholarship committee.

May a 501(c)(3) organization that opens a DAF recommend a distribution back to itself?

DAFs are not permitted to provide more than an insubstantial benefit back to the disqualified persons. Whether intentionally or by omission, this prohibition also applies when the DAF donor is itself a public charity. As such, DAFs established by 501(c)(3) organizations or other institutions should be utilized for external grantmaking purposes, such as providing grants to other charitable organizations.

May a DAF be the recipient of a Qualified Charitable Distribution (QCD)?

DAFs do not qualify to receive Qualified Charitable Distributions (QCD). A QCD is a grant made directly from certain types of IRA accounts to a public charity on behalf of a person who has reached a certain age. The benefit to the IRA holder is that the transaction satisfies the mandatory distribution from the IRA yet is not counted as income to that person. (It is also not subject to a charitable contribution deduction.) Otherwise, the IRA holder must first recognize income tax on the distribution and then may

take the correlating charitable deduction, which may be limited depending upon the holder's personal tax circumstances.

SPECIAL ISSUES FOR DONORS AND ADVISORS

What types of assets can be contributed into a DAF account?

Oftentimes, DAFs are established or "refilled" with contributions of cash, cash-equivalent assets, stocks or bonds.

However, forms of non-cash assets may be an option, depending on the rules established by the DAF sponsoring organization. For example, a donor may be interested in contributing a gift of real estate, securities or fine art. These types of assets may or may not fit with the DAF provider's gift acceptance policy, which dictates what types of gifts can be accepted by the organization, oftentimes based on staffing or expertise limitations. In other cases, DAF providers may be large enough in size or sufficiently experienced in accepting non-cash assets that they can easily receive these gifts for the purposes of establishing or growing a donor's DAF account.

In some cases, a DAF donor may need to work with an external group that has the ability to accept a non-cash asset gift, which would then be transferred to their DAF provider of choice, such as their local community foundation. (See "[What is a DAF-to-DAF transfer?](#)")

Can a donor influence the investment strategy of a DAF account?

Depending on the particular DAF sponsoring organization, donors may have options available to them regarding the investment strategy of their DAF account. In most cases, the DAF provider invests the DAF account using the same strategy that applies to their other endowed or spendable funds.

Some larger DAF providers do allow their DAF account representatives to choose from a limited number of options regarding their account's investment strategy. These options vary by DAF sponsoring organization. They may also be limited to DAF accounts of a certain minimum size. In very rare instances, the DAF provider may allow the account holder's financial/investment advisor to advise with respect to the investment strategy of the account. However, the assets become the property of the DAF sponsoring organization, which has ultimate control over the DAF account's asset and investment strategy.

Is a DAF an option for planned or estate gifts?

DAF accounts may be used as a planned giving or estate planning option. This arrangement permits the donor to execute the fund agreement establishing the fund and appointing advisors while providing for the gift to the DAF in the donor's estate plan. However, donors should be made aware of potential long-term limitations of DAF accounts. For instance:

- **Potential Regulatory Changes Impacting DAFs:** DAFs continue to face increased public scrutiny and regulatory discussion. As such, donors should be made aware of the possibility that their DAF account's current structure may be changed at any time to fit with evolving regulations and/or policies of the DAF sponsoring organization.

- **Limited Generations of Advisors:** Practice in the philanthropic field has evolved to limit the number of generations of successor advisors permitted for the DAF account. Depending on the DAF sponsoring organization, DAF accounts created by an estate may or may not count the inheriting advisors as the initial or first generation. DAFs are no longer seen as a perpetual (indefinite lifetime) philanthropic vehicle, as may be the case for a private foundation.
- **DAF Account Structures:** Some DAF providers offer the option for an endowed DAF account, which provides a structure for long-term grantmaking from a single donation (i.e., an estate/planned gift). However, others only offer a spendable structure, which does not provide for an endowed/invested portion of the assets to be used for future (perpetual) grantmaking. Donors and their financial/estate advisors should ensure that they choose a DAF provider and structure that fits with their intended purpose and wishes.
- **Inactive Fund Policies:** Best practice in the field (and as required for accreditation by National Standards for U.S. Community Foundations) has moved toward enforcement of “inactive fund policies.” (See [“What is an “inactive funds policy?”](#)) DAF providers are increasingly enforcing that DAF accounts regularly make grants out to charitable organizations. In the case of planned gifts, the resulting DAF’s advisors would need to quickly coordinate a grantmaking plan and regularly (i.e., annually) meet to ensure that the DAF account makes sufficient grants to fulfill the requirements of the sponsoring organization’s inactive funds policy. DAF accounts are not designed to grow for years prior to making their first grant.

Can a donor receive any personal benefit from a DAF grant?

No. Donor advised funds are subject to excess benefits transactions rules outlined above. (See [“What are the private foundation concepts that apply to DAFs?”](#)) There is a strict prohibition on DAF grants providing more than an insubstantial benefit back to its donors or advisors. For example, a DAF donor or advisor cannot use their DAF to purchase tickets for a fundraising event. Likewise, DAFs cannot be used to satisfy binding pledges.

May a donor be reimbursed for fundraising expenses from a DAF?

No, all distributions to individuals are prohibited (even to independent vendors who happen to be individuals, generally). Sponsoring organizations are typically advised against reimbursing the donor in exchange for the DAF transferring an equal amount to the sponsoring organization. (The IRS generally disfavors activities done through an intermediary that would not be permitted directly.)

Can a private foundation be terminated into a DAF account held by a sponsoring organization?

Yes, private foundations can be terminated into a DAF held by a DAF sponsoring organization, such as a community foundation, though there may be costs involved. To help inform donors prior to making this decision, see CMF’s resource, [“Comparing Philanthropic Giving Structures: Private Foundation or Community Foundation-Based Fund.”](#)

Can DAF advisors be changed or added at a later date?

Depending on the DAF sponsoring organization’s specific policies and procedures, a donor may be able to add or change DAF advisors at a later date. However, the organization likely has an established limit on the advisory period beyond the original donor’s death, frequently limited to one or two generations.

These policies do not permit advisors to be added as a means to extend the donor and their representative's influence over the DAF beyond the limited number of generations. However, there is no legal requirement to limit successor advisors to a DAF or to permit them.

Can a DAF be closed or returned to a donor?

All contributions made to a DAF sponsoring organization (i.e., community foundation, other public charity) are irrevocable, meaning that they cannot be returned to the original donor. The assets become the property of the organization, which has final determination over all grants and activity associated with those assets.

Likewise, a DAF cannot be terminated and given back to the donor in any form, including as a means to set up an alternative charitable instrument or organization, such as a private or family foundation. While DAFs are sometimes advertised as "charitable checking accounts," giving the impression that the original donor has full control over the movement of assets in and out of the fund (including back to themselves), the assets are fully owned by the sponsoring organization. At this point in time, DAFs may recommend grants to other DAFs, but it is important to note that pending legislation may limit, restrict or otherwise prohibit this activity in the future. (See "[What is a DAF-to-DAF transfer?](#)")

Can a DAF be transitioned into a stand-alone private/family foundation at a later date?

Donor Advised Funds (DAFs) are designed to be component funds housed within a community foundation or other public charity. As a result, a DAF cannot function independently of the foundation and the fund agreement put in place with the original donor.

All contributions made to a community foundation (or other public charity) are irrevocable, meaning that they cannot be returned to the original donor. Likewise, a DAF cannot be terminated and given back to the donor in any form, including as a means to set up an alternative charitable instrument or organization, such as a private or family foundation. The assets become the property of the community foundation, which has final determination over all grants and activity associated with those assets.

Families and board members of private foundations that terminate the organization into a community foundation fund, such as a DAF, also cannot reacquire the assets from the community foundation for other purposes at a later date. In the case they wanted to establish a new private foundation, these individuals would need to use a distinctly different set of assets to fund the new charitable entity.

Can a private foundation count a grant to a DAF as part of its required 5% distribution?

Periodically, a private foundation may make a grant to a donor advised fund held by a DAF sponsoring organization. Under current regulations, these grants may be counted toward the foundation's 5% distribution requirement. Best practice in the field recommends that the foundation advise a payout of this grant from the DAF within 12 months. While currently permissible, foundations should seek qualified legal and tax advice prior to engaging in this type of grantmaking. Further, increased scrutiny of this type of grant may lead to future changes in federal and/or state rules that affect the operation of DAFs and the allowance of this type of activity.

SPECIAL ISSUES FOR GRANTMAKERS AND DAF SPONSORING ORGANIZATIONS

What is an endowed or spendable (non-endowed) DAF?

Recent research on donor advised funds¹⁰ has pointed to DAF accounts held by community foundations being most commonly categorized as either “endowed” or “spendable” (non-endowed), based on two distinct strategies and fund agreement types.

An **endowed DAF** is established with the intent of long-term use. A relatively high minimum level must be maintained in the fund to ensure sufficient investment returns. Not all community foundations provide a structure for an endowed DAF.

As an example of an endowed DAF: A donor establishes an endowed DAF at her local community foundation through a large one-time donation, resulting from the sale of her family’s business or a recent inheritance. These funds serve as the basis for the donor’s long-term giving strategy. Each year, the donor recommends a series of grants to her favorite charitable organizations from her endowed DAF. When she dies, her children become new advisors for the DAF and continue making grants from it.

In comparison, a **spendable DAF** is intended to be used for donors to fill the fund and pay out the majority of the fund within a short period of time, down to a \$0 balance. They can then refill and reuse the account regularly to support their charitable donations. These funds could have a payout rate of more than 100%, due to the relatively high turnover in money contained within these funds and the regularity of grants being made out of them. Many community foundations, including a portion of those active in Michigan, provide their donors with this structure for establishing and maintaining a DAF.

As an example of a spendable DAF: A donor establishes a spendable DAF at his local community foundation, starting with a relatively moderate donation. The donor continues to periodically make donations to the DAF and recommend grants be made from the DAF to charitable organizations in his community at a relatively similar size and rate as his contributions.

What is an “inactive funds policy”?

A DAF may be considered “inactive” if no grants are made from the fund after a set period of time, oftentimes 2-5 years. Community foundations that participate in the National Standards accreditation process are expected to have an inactive funds policy which outlines how inactive funds are handled by the organization. Such policies also provide a mechanism for the foundation to enforce that donors actively advise grants from their DAFs held at the foundation. These policies do allow for donors to have years in which they do not make grants, but ensure that the fund remains active in grantmaking to charitable organizations over time.

¹⁰ For more information, see [“Analysis of Donor Advised Funds from a Community Foundation Perspective.”](#)

What must the charitable contribution acknowledgement letter say regarding a contribution to a DAF?

The charitable contribution acknowledgement letter must state that, “no goods or services were provided” in exchange for the contribution (unless it is a quid pro quo). Gifts of property may require additional documentation. Unless the gift is cash, the value of the gift should never be stated by the recipient organization. Contributions to DAFs must also state that the foundation has “exclusive legal control” over the assets contributed.

Can another fund at the community foundation be transitioned into a DAF?

Generally, other fund types (i.e., designated fund, field of interest fund) held by a community foundation should not be transitioned into a DAF, as that would increase restrictions on the fund and ultimately increase (rather than decrease) donor control. However, it may be appropriate to agree to transition a DAF into other fund types over time, such as a designated fund (if the fund only contributes to a single charitable entity) or a general or field of interest fund (after the predetermined number of advisor generations passes – which is usually spelled out in the DAF policy or fund agreement).

For more information about fund agreements, see CMF’s resource, “[Frequently Asked Questions About Fund Agreements.](#)”

What is a DAF-to-DAF transfer?

Recent regulatory discussions have called attention to the phenomenon known as “DAF-to-DAF transfers.” These transfers take place between two DAF accounts held by the same or different DAF sponsoring organizations.

DAF-to-DAF transfers can be a questionable practice, especially as public scrutiny focuses on anecdotal cases where DAF grants ultimately return to the account of the original donor or advisors, rather than benefiting charitable entities. However, DAF-to-DAF transfers serve an important accounting and/or legal purpose within the field.

The following are examples of DAF-to-DAF transfers:

- A local community foundation does not have the ability to accept a donor’s contribution of property (real estate, artwork, etc.). However, a separate DAF provider has the infrastructure to accept this form of gift. A DAF-to-DAF transfer may be used where one provider accepts the gift and then transfers it to the community foundation in the form of a DAF, with the original donor serving as the primary advisor on the account. This structure permits the donor to utilize one organization’s infrastructure to accept gifts of property, while maintaining their DAF within their local community foundation.
- A donor opens a DAF account within a DAF sponsoring organization (i.e., community foundation, national DAF provider). Due to their relocation or need for alternative arrangements for their DAF account (i.e., additional grantmaking options, closer office location, different administrative fees), they request that their DAF account be transferred to a different DAF provider. With the permission of the board, the DAF account is transitioned from one DAF sponsoring organization to another.

In the case of internal (within the same organization) transfers, these grants are likely not captured on the Form 990 of the sponsoring organizations. In the case of transfers between two separate DAF sponsoring organizations, this grant between DAFs would be included in the overall DAF activity on the Form 990.

Are there proposed DAF regulations that may impact DAFs in the future?

Proposed DAF regulations¹¹ provide, generally, that a sponsoring organization will not be held liable if a DAF is used to satisfy a binding pledge so long as there is not mention of a pledge in the grant agreement. This does not mean that DAFs may now be used to satisfy binding pledges; rather that the sponsoring organization is not held responsible to police whether this is the case. Among other things, these proposed regulations would look through the DAF to the donor when calculating the public support test of recipient charities (so that donors would not be able to avoid causing a charity to “tip” into private foundation status with a large grant by passing the grant through the sponsoring organization). Various other pieces of DAF legislation have been discussed or even proposed.

RECOMMENDED RESOURCES

- Council of Michigan Foundations. “An Operations Checklist for Foundation Compliance.” 2022.
<https://www.michiganfoundations.org/resources/operations-checklist-foundation-compliance>.
- Council of Michigan Foundations. “Choosing a Corporate Philanthropy Approach.” 2021.
<https://www.michiganfoundations.org/resources/choosing-corporate-philanthropy-approach>.
- Council of Michigan Foundations. “Comparing Philanthropic Giving Structures: Private Foundation or Community Foundation-Based Fund.” 2022.
<https://www.michiganfoundations.org/resources/comparing-philanthropic-giving-structures-private-foundation-or-community-foundation>.
- Council of Michigan Foundations. “Frequently Asked Questions About Disasters.” 2022.
<https://www.michiganfoundations.org/resources/faqs-about-disasters>.
- Council of Michigan Foundations. “Frequently Asked Questions About Fund Agreements.” 2022.
<https://www.michiganfoundations.org/resources/faqs-about-fund-agreements>.
- Council of Michigan Foundations. “Fund Agreements Sample Documents.” 2020.
<https://www.michiganfoundations.org/resources/fund-agreements-sample-documents>.
- Council of Michigan Foundations. “Navigating Scholarships and Grants to Individuals.” 2021.
<https://www.michiganfoundations.org/resources/navigating-scholarships-and-grants-individuals>.
- Council of Michigan Foundations. “Options for Your Financial Giving.” 2021.
<https://www.michiganfoundations.org/resources/options-your-financial-giving>.
- Williams, J. and Kienker, B. *Analysis of Donor Advised Funds from a Community Foundation Perspective*.
Council of Michigan Foundations. 2021.

¹¹ [IRS Notice 2017-73](#).

<https://www.michiganfoundations.org/resources/analysis-donor-advised-funds-community-foundation-perspective>.

ABOUT ASK CMF

This document was authored by Brittany Kienker, Ph.D., Knowledge Insights Expert in Residence for the Council of Michigan Foundations (CMF). Legal aspects of this document were reviewed by Jennifer Oertel, outside legal counsel to CMF. CMF members can find answers to their most pressing questions through CMF's Knowledge Insights division, including Ask CMF, the Knowledge Center and the Sample Documents Hub. Ask CMF is a free service to CMF members, available through the "Ask CMF" link on the CMF homepage or by visiting <https://www.michiganfoundations.org/practice/ask-cmf>.

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