Stanford PACS
Center on Philanthropy and Civil Society
—
Effective Philanthropy Learning Initiative

Stanford Law School
Law and Policy Lab

Donor Advised Funds: Benefits, Costs, and Questions

Thursday, May 14, 2020
11:30 am – 01:00 pm PDT

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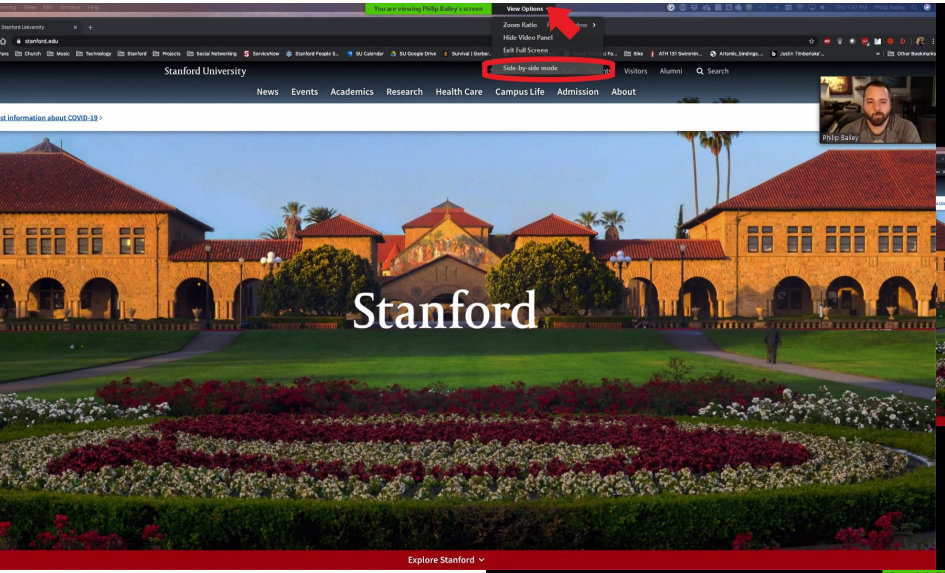
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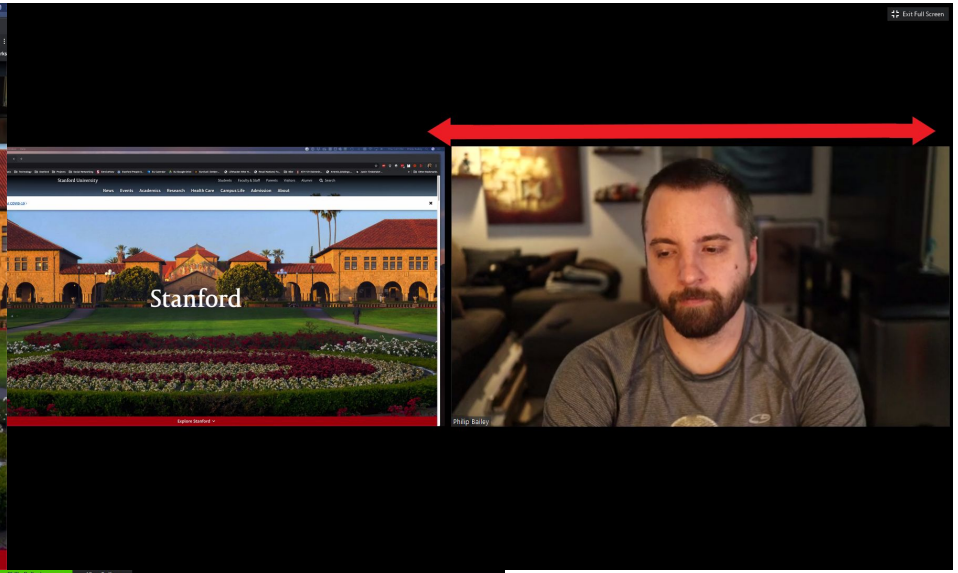
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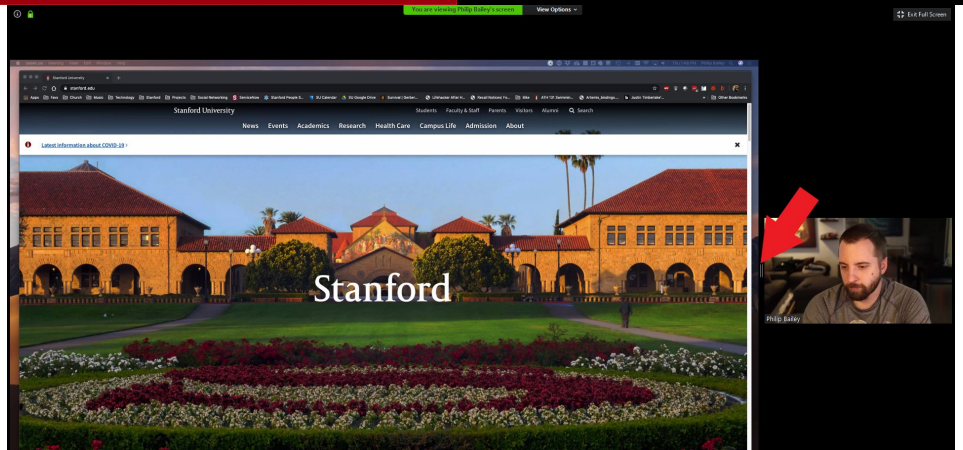
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Stanford PACS Goals

Original Research
Expand the body and reach of quality research on philanthropy, civil society, and social innovation

Scholarship
Increase the pipeline of scholars, practitioners, and leaders in philanthropy and civil society

Practice
Improve the practice and effectiveness of philanthropy and social innovation

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Instructors

Paul Brest
Former Dean
Professor Emeritus
(active)
Stanford Law School

Joseph Bankman
Ralph M. Parsons
Professor of Law and
Business Stanford Law
School

Daniel Hemel
Assistant Professor of Law
University of Chicago
Law School

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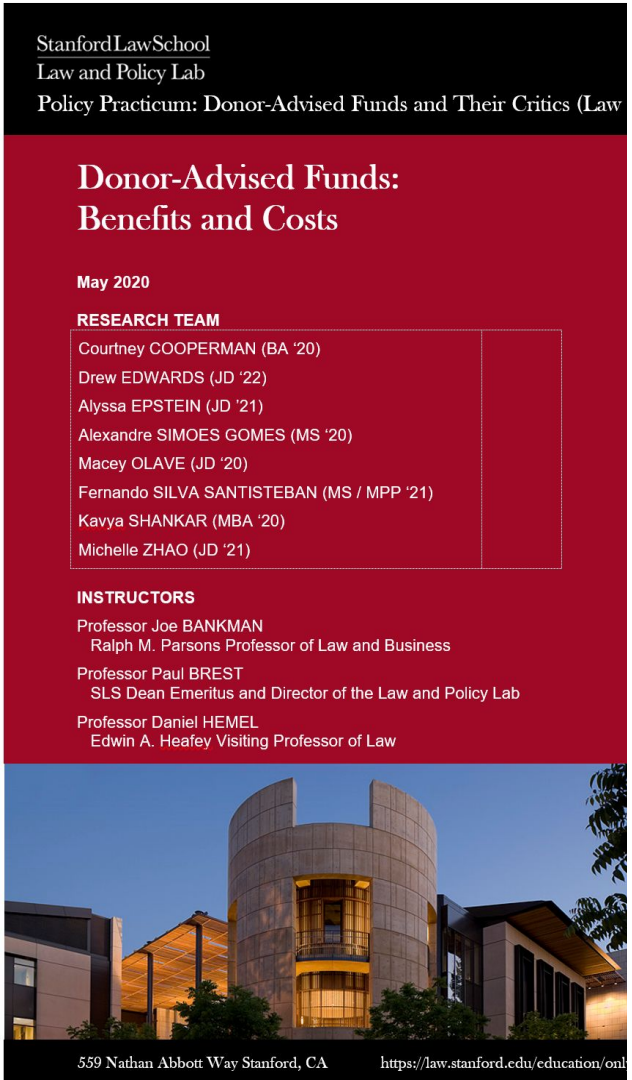

Stanford Law School
Law and Policy Lab
Policy Practicum: Donor-Advised Funds and Their Critics (Law

Donor-Advised Funds: Benefits and Costs

May 2020

RESEARCH TEAM

Courtney COOPERMAN (BA '20)
Drew EDWARDS (JD '22)
Alyssa EPSTEIN (JD '21)
Alexandre SIMOES GOMES (MS '20)
Macey OLAVE (JD '20)
Fernando SILVA SANTISTEBAN (MS / MPP '21)
Kavya SHANKAR (MBA '20)
Michelle ZHAO (JD '21)

INSTRUCTORS

Professor Joe BANKMAN
Ralph M. Parsons Professor of Law and Business

Professor Paul BREST
SLS Dean Emeritus and Director of the Law and Policy Lab

Professor Daniel HEMEL
Edwin A. Heafey Visiting Professor of Law

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Stanford Law School Policy Lab

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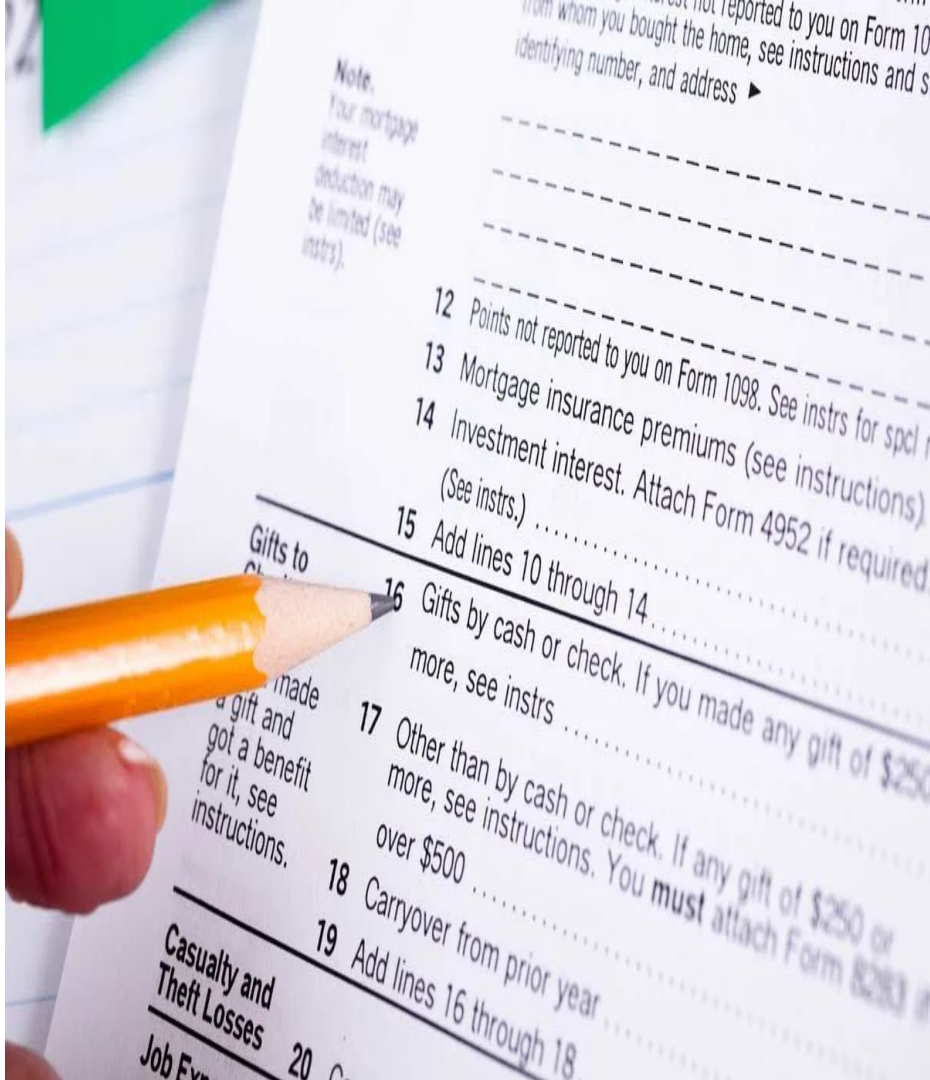
Rationales for the Federal Income Tax Deduction

- Encourages donations to nonprofit organizations that provide services not provided by the private marketplace or by governments.
- Allows taxpayers to direct public funds (tax subsidy) to organizations of their choice, allowing them a voice in the decisions.
- Promotes the social value of giving.
- Supports civil society.



Today's Agenda

1. The timing of deduction and payout rates
2. Gifts of complex assets to DAFs and their valuation
3. The effects of DAF's on charitable giving and on operating charities
4. Value-based investing
5. Advice given by DAF sponsors to donors
6. Restrictions DAF sponsors impose on grantees, and donor anonymity

Timing of Deduction and Payout

Drew Edwards
(JD ‘22)

Alex Simoes Gomes
(MS ‘20)

Timing of Deduction and Payout

- DAF holders receive immediate tax deduction and face no annual payout requirement
- Concern: assets could remain in a DAF forever, without ever going to an operating charity
- DAFs pay out approximately 20% of their assets per year

Rationales for delaying payout

1. Donor effectiveness
2. Cause effectiveness
3. Building a legacy
4. Inertia

Timing of Deduction and Payout (cont'd)

- Additional considerations related to timing
  - Rate of return of philanthropy vs. rate of return of assets in a DAF
  - Social investing
  - Smoothing donations during economic downturns
- Existing proposals
  - Roger Colinvaux and Ray Madoff proposed shifting timing of deduction
  - Nudging DAF holders to recommend grants
  - Requiring DAF holders to make distributions

Gifts of Complex Assets and their Valuation

Michelle Zhao
(JD ‘21)

Gifts of Complex Assets and their Valuation

- DAFs are able to receive gifts of complex assets from donors and distribute those gifts to nonprofits that may not be able to process the complex assets on their own
  - Expanding the pool of donation recipients
- Concern: Tax deduction for a donation may be overvalued
  - Note that this is no different for DAFs than for donations to any public charity

Gifts of Complex Assets and their Valuation (cont'd)

- The IRS has a means of checking on valuation claims
  - The complex asset donor fills out a form on annual tax return claiming a value for the asset (with approval by an independent appraiser)
  - If a DAF sells the asset within three years, must then submit a complementary form stating sale price
- Most litigation focuses on the process behind the claimed deduction rather than the amount claimed
- Among the largest DAFs, complex assets account for just 5% of the total value of all contributions
- Valuation concerns ought not drive public policy toward DAFs

Effects on Charitable Giving and Operating Charities

Fernando Rodriguez Silva Santisteban
(MS / MPP ‘21)

Effects on Charitable Giving

- Direct evidence on the effects of DAFs on charitable giving is inconclusive
  - Limitations of data
  - Empirical studies interpreted based on strong assumptions
- Looking at economic theory gives us a clue of the potential effects

Effects on Charitable Giving (cont'd)

- DAFs may reduce transaction costs of charitable giving
  - Easier to give non-cash assets
  - Less administrative costs compared to foundations
  - Donors can "bunch" their gifts to obtain an itemized deduction
- DAFs may reduce after-tax price of charitable giving
  - Donor's near indifference point of donation have additional incentive
  - Amount donated is also elastic to price
  - Desirability of increased amount is arguable (due to fiscal subsidy)

Effects on Operating Charities

- DAFs change power dynamics between donor and donee
  - Project-specific vs. unrestricted funds
- DAFs make available asset contributions to smaller operating charities
- DAFs potentially influence liquidity of operating charities
  - Could delay contributions to operating charities
  - Could smoothen contributions in times of recession

ESG and Impact Investing

Alyssa Epstein
(JD ’21)

ESG and Impact Investing

- ESG Investing: Values-Based Investing in Publicly Traded Securities
  - Promise market rate returns, but actual returns net of fees are uncertain
  - Rarely have positive impact on ESG companies or negative impact on non-ESG companies
- Impact Investing: Investment in Private Markets designed to advance a tangible social goal (quasi-PRI)
  - Returns may be at or below market
  - Do in fact have impact

ESG and Impact Investing (cont'd)

- Values-based Investment Strategies at DAFs
  - Many DAFs have ESG options
  - Impact options are available at some DAFs, but usually only to very large donors
- Benefits of ESG at DAFs
  - "Clean Hands" Option
  - Advocacy Potential
- Benefits of Impact Investment at DAFs
  - Social Impact + Financial Return
  - Good venue for risk taking

ESG and Impact Investing (cont'd)

Conclusions:

ESG options should still be available at DAFs, but not advertised as providing social impact opportunity

Impact Investments should be more widely available at DAFs

Advice Given by DAFs to Donors

Courtney Cooperman (BA ‘20)

Kavya Shankar (MBA ‘20)

Advice given by DAFs to donors

- Advice is important to DAF sponsors: 1) differentiation; 2) shaping donor decisions
- National, single-issue, and community DAFs are all offering some form of advice today
- Quality of sponsor advice does not appear to be driving donor choices among our sample
- Opportunities exist to benefit both donor and DAF sponsor through enhanced donor education and advice offerings

Restrictions on Grantees and Donor Anonymity

Erinn Andrews
PACS Director of Philanthropy Research and Education

Restrictions on grantees and donor anonymity

- DAF sponsors have absolute discretion; donors have *advisory* privileges
- National sponsors: most take a cause-neutral approach to grantees
  - Might block donations to NPOs under investigation
  - Might flag NPOs with negative press
- Community foundations and special-issue sponsors: more likely to impose restrictions on grants
  - To nonprofits with certain points of view
  - To specific organizations
- Restrictions could be:
  - Disclosed upon opening the DAF
  - Imposed after the sponsor conducts due diligence on an organization

Restrictions on grantees and donor anonymity (cont'd)

- Donor anonymity
  - Anonymity to the public to protect the donor from retaliation
    - Donors can shield preference from public view
  - Anonymity to the nonprofit
    - Recipient organizations worry gift might be "tainted" by donor's conduct/ideology
    - Nonprofits worry about losing the chance to steward the gift
    - Vast majority of donations are not anonymous
    - **Recommendation**: DAF sponsors include donor's name in default setting

Transparency

- Lack of data on individual DAFs impedes research and accountability
- Could sponsors provide de-identified information for the large majority of DAFs without breaching anonymity?

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Discussion

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Q & A

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Thank you!

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DAF-TO-DAF TRANSFERS

IRS Form IRS Form observed	Total grants ($MM)	Grants to Fidelity, Vanguard or Schwab ($MM)	% of total grants
Vanguard Charitable Endowment Program - FY 2017	758.22	17.15	2.26%
Schwab Charitable Fund - FY 2019	1,869.79	19.09	1.02%
Fidelity Investments Charitable Gift Fund - FY 2019	4,798.37	28.24	0.59%