
# What's Right for You: A Donor-Advised Fund or a Private Foundation?

MORGAN STANLEY GLOBAL IMPACT FUNDING TRUST

Donor-advised funds and private foundations both provide individuals and corporations with a dynamic charitable giving vehicle. A donor may contribute assets to a donor-advised fund (DAF) or a private foundation for an immediate tax deduction and later decide which charities will benefit.

**WHAT IS A DONOR-ADVISED FUND AND HOW DOES IT WORK?** A donor-advised fund provides a flexible way to make donations to charities and other non-profit organizations. As donor, you make an irrevocable, nonrefundable contribution of cash or securities to the fund. You can then recommend how grants are to be made from the account, including the organizations receiving grants, the amount of grants and when grants should be paid. Assets from a donor-advised fund are typically managed by a professional investment advisory firm. This removes administrative burdens and provides the opportunity to increase the value of your contribution, resulting in potentially larger grants.

**WHAT IS A PRIVATE FOUNDATION AND HOW DOES IT WORK?** Private foundations are charities (either corporations or trusts) that are typically formed and funded by a single individual, family or company. Most private foundations fulfill their charitable missions by making grants to public charities. Funds not paid out are invested either by the board or by advisors that they hire. Unlike DAFs, private foundations provide the donor with a high level of oversight and control over all of the foundation's operations.

**HOW ARE DISTRIBUTIONS HANDLED?** Distributions from a private foundation are controlled by the foundation's directors or trustees. The board votes on which charities receive grants and the amounts paid. The donor to a private foundation may serve on the governing board and may select the other members, thus giving the donor a strong say in the selection of grant recipients.

A donor to a DAF may recommend distributions from the account to any qualifying charity. However, ultimate legal control resides with the board of directors of the DAF's sponsoring organization (the charity that created the DAF), which must approve all grant recommendations.

Private foundations generally must make annual distributions of at least 5% of their assets for charitable purposes and must pay an annual excise tax of 1%–2% on investment income. By contrast, DAFs are not subject to the 5% minimum distribution rule, and their investment income is not taxed. As a result, DAFs, unlike private foundations, are not forced to make any set distributions during down markets. This may help to preserve the funds for later grants to charity.

A private foundation typically has greater flexibility in the kinds of grants that it can make. For example, a private foundation can make payments directly to individuals for charitable purposes, subject to certain requirements. Federal tax law, however, flatly forbids charitable grants from DAFs to individuals. A private foundation also may be more attractive to a donor who wishes to make gifts that are restricted to a particular use (such as to fund a particular project at the recipient charity). A private foundation's board is usually better able to monitor and enforce a complex restriction placed on a gift. A DAF generally will allow donors to place only minimal restrictions on grants that they recommend.

**WHAT COSTS ARE ASSOCIATED WITH START-UP AND UPKEEP?** Donors who want a private foundation must create the entity and obtain tax-exempt status from the Internal Revenue Service. Donors who run their own private foundations are responsible for making investment choices, vetting grant recipients, satisfying minimum distribution requirements and making all necessary tax filings. Additionally, they are responsible for day-to-day operations and must consider the administrative and legal costs involved.

Donors who contribute to DAFs are not subject to the duties, responsibilities and expenses associated with private foundations. The legal, accounting and administrative responsibilities are handled by the DAF's sponsoring organization.

**HOW DOES THE TAX TREATMENT OF CONTRIBUTIONS DIFFER?** Contributions to both DAFs and private foundation are tax-deductible. However, because DAFs are classified as public charities for federal income tax purposes, they are subject to more favorable rules.

Generally, with DAFs the federal tax law limits an individual's income tax charitable deduction to 50% of the donor's adjusted gross income (AGI) per year for contributions of cash, or up to 30% of AGI for contributions of long-term gain property. Deductions for donations to private foundations are capped at lower limits of 30% for cash donations and 20% for long-term gain property. In each instance, donors may generally carry forward charitable deduction in excess of these limits for up to five successive tax years.

Another important distinction is that, except in the case of qualified appreciated stock, the deduction for long-term gain assets contributed to a private foundation is limited to the donor's basis in the property. Accordingly, donors of closely-held or restricted stock may be entitled to significantly higher deductions for gifts to a DAF, where the deduction for the contributed stock would be based upon the stock's fair market value. Gifts to both DAFs and private foundations are fully deductible for purposes of the federal estate and gift taxes.

**ARE THE PRIVACY CONSIDERATIONS DIFFERENT?** Privacy is a consideration for many donors. Sponsoring organizations of DAFs and private foundations both file annual information returns with the Internal Revenue Service that are publically available. However, DAFs provide greater privacy because they only list donors on their annual federal information returns who give the greater of $5,000 or 2% of the sponsoring organization's contributions for the year.

In contrast, donors who give more than $5,000 to a private foundation are identified in the foundation's information return, which lists all grants made during the year by the private foundation. Also, annual reports and information about board members of private foundations may be accessed on the Internet.

**FOR MORE INFORMATION** about Morgan Stanley GIFT and its donor-advised fund program, please consult the Donor Circular and Disclosure Statement or your Financial Advisor or Private Wealth Advisor.

| | DONOR-ADVISED FUNDS | PRIVATE FOUNDATIONS |
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| Start-Up Time: | None | Weeks or months |
| Start-Up Costs: | None | Legal and other fees |
| Tax Deduction Limits for Cash Gifts: | 50% of adjusted gross income | 30% of adjusted gross income |
| Tax Deduction Limits for Gifts of Securities Held at Least 1 Year: | 30% of adjusted gross income | 20% of adjusted gross income |
| Required Annual Distribution: | None | At least 5% of net assets |
| Tax on Investment Income: | None | Up to 2% of annual investment income |
| Responsibilities: | Donor recommends grants to specific charities or causes.<br>Donor selects investment options offered by sponsoring charity. | Record keeping, asset management, state and federal tax return filings, compliance with corporate formalities and local law governing charities. |
| Special Considerations: | Subject to more favorable tax rules<br>Less costs for start-up and maintenance<br>Offers greater privacy | Offers higher level of oversight<br>More control over distributions |



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