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Time to Convert?

A number of philanthropists are shutting down private foundations and turning to donor-advised funds. Here's why you should—and shouldn't—do it.

By [JILIAN MINCER](#)

Raymond P. Kurlak established a private foundation in 2000 to fund education and literacy programs, joining a growing wave of philanthropy in the U.S. In the wake of the recent turmoil in financial markets, he became part of another trend: He closed the Raymond Foundation about a year ago and rolled the assets into a donor-advised fund.

Mr. Kurlak opened an account with the Schwab Charitable Fund, an independent, nonprofit organization founded by [Charles Schwab Corp.](#) Other funds founded by big financial-services firms include the Fidelity Charitable Gift Fund and the Vanguard Charitable Endowment Program, and there are many other choices as well. As the names suggest, these funds distribute money to charitable causes as recommended by the donors. One of their advantages is that they relieve philanthropists of some of the costs of running a foundation.

Mr. Kurlak estimates that he saves about 10% by using Schwab to administer his account instead of paying for his own lawyers, accountants and office supplies, as he did when he ran his foundation. Those savings are particularly important because of the losses his foundation suffered when stock prices dropped. Cutting back on costs makes his depleted assets go further. "I'm very pleased," he says. "It takes much less time and money" to direct the distributions from his Schwab account than it did to run his foundation.

Privacy and Tax Savings

Cost-cutting is one of the factors driving an increase in conversions from private foundations to donor-advised funds. But there are others that aren't so closely tied to the direction of stock prices. Funds also relieve philanthropists of many of the hassles of running a foundation, like filing paperwork, checking out potential recipients or, for larger foundations, managing a staff. Mr. Kurlak says he spends about two weeks a year on his account's business now, down from two months a year on his foundation in the past. And the funds offer tax advantages and greater privacy for donors, among other advantages.

Making the switch from foundation to fund isn't for everyone. Some individuals may prefer the cachet of running a foundation, or the opportunity it gives them to teach family members about philanthropy. Perhaps most important, foundations give donors total control over their contributions, which can be crucial for those who support causes that are out of the mainstream.

Still, the number of accounts at donor-advised funds climbed 11% last year, to 148,588, following a 13% increase the previous year, according to the National Philanthropic Trust, a charity in Jenkintown, Pa. Conversion isn't difficult, and many of the funds have expanded staff to assist donors with the process.

The Schwab Charitable Fund was fielding so many inquiries about converting that it recently devoted additional

staff to conversions and developed a questionnaire to help individuals decide whether to make the move, says Kim Wright-Violich, the fund's president.

More to Give

"As assets have gotten beaten up, people have gotten really frustrated about not being able to do the same level of gifting," says Ms. Wright-Violich. More philanthropists are realizing, she says, that the money that donor-advised funds can save them in administrative and other costs can go toward the causes they support. In some cases, she says, such funds can cut donors' costs by as much as 50%.

Besides cutting administrative costs, funds can reduce donors' investment fees. Small foundations, because of their limited assets, often pay relatively high fees to the firms that handle their investments. But donor funds, working with a much bigger pool of money from all the accounts they administer, often pay much lower fees to invest donors' money.

Donor-advised funds also have certain tax advantages over foundations. Donors get an immediate tax deduction when they make a contribution to a fund, as they would with donations to their own foundation. But the deductions are more generous: Donors can deduct cash contributions to a fund totaling up to half of their adjusted gross income each year; the limit for donations to a private foundation is 30%. Donors can also deduct up to 30% of their adjusted gross income for donations to a fund of securities that have appreciated in value since the donor bought them; for a private foundation, the limit for such donations is 20%.

In addition, investment gains in an account at a donor-advised fund generally are tax-free, unlike a foundation's investment gains, which are subject to a small excise tax.

The funds also handle all the paperwork and due diligence involved in making donations and investments. That may be particularly reassuring to some givers in the wake of the Madoff scandal, which heightened concerns about investment scams.

Flexibility and Privacy

Donor-advised funds also offer account holders some additional flexibility and help protect their privacy.

There is no requirement for annual distributions from an account at a fund, while foundations are required to distribute at least 5% of their assets each year. That can be especially important when financial markets are tumbling, because many philanthropists may want to hold on to more of their money so that they have a bigger asset base to rebuild from when the markets rebound.

The privacy issue is one that catches some philanthropists by surprise. Many are unaware when they set up a foundation that its tax forms will be made public, exposing details of the foundation's operations and even some personal information. No such information is available for accounts at donor-advised funds. And all donations to a fund can be made anonymously, a strong incentive for many donors to convert, says Sarah C. Libbey, president of the Fidelity Charitable Gift Fund.

James Barnes, chief relationship officer for the Vanguard Charitable Endowment Program, says another reason some foundations are converting is that the founder has died and family members disagree on the direction the foundation should take. Some people in that situation are splitting up a foundation's assets among several accounts at donor-advised funds, and those accounts can then be used for different purposes.

Families also often decide to convert simply because they've grown tired of the time and cost of meeting and of managing a foundation. The economic turmoil of the past couple of years may have helped fuel conversions because philanthropists are having to spend more time tending to their businesses, leaving less time to devote to foundation work.

Giving Up Total Control

Of course, there are some potential drawbacks to consider before switching from a foundation to a donor-

advised fund.

One of the biggest is that with a fund, "you no longer have the independence and the total control" that you have with your own foundation, says Steve Gunderson, president and chief executive of the Council on Foundations, a nonprofit association of about 2,000 grant-making foundations and corporations, based in Arlington, Va.

That may not be an issue for most philanthropists, because it's rare for a fund to refuse to make a donation as desired by an account holder. But Mr. Barnes at the Vanguard Charitable Endowment Program notes that the funds can only write checks to charities. That means they don't allow donors to provide direct support for individuals or for groups that don't qualify as charitable organizations.

Another possible drawback is that contributions to the funds are irrevocable. So while a fund allows for more flexibility in the timing of donations because it doesn't require distributions of at least 5% annually, it limits flexibility in a different way by not allowing a donor to react to circumstances by putting the money to other use.

For those who choose to make the switch, the first step is to contact the state authorities that regulate charities, says Ms. Wright-Violich of Schwab. Each state has different requirements for terminating a foundation. The foundation must also file a final federal tax form. More detailed guidance is available from donor-advised funds.

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