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Donors Leave the Details to a Fund

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FIDELITY, the giant investment company, suggests that of the two options for charitable giving, donor-advised funds offer several advantages over private foundations — larger tax deductions, simplicity and more privacy. Fidelity has good reason to make that recommendation: its Fidelity Charitable Gift Fund is the nation's largest such fund, with a \$4.7 billion in assets, and much of that is invested in Fidelity's own funds.

Still, Fidelity may have a point.

Even some people in the foundation business rely on a donor-advised fund for their own charitable giving. Laurance R. Hoagland Jr., chief investment officer of the William and Flora Hewlett Foundation, which has \$8.5 billion in assets, said he used Vanguard's donor-advised fund for his personal giving, because the amount he donates "is not meaningful enough to justify the expenses and hassle of a private foundation." A man who does his own tax returns, he said he had "enough administrative inconveniences in his life" without overseeing a foundation of his own.

In a donor-advised fund, donors make an irrevocable contribution to the fund and receive an immediate tax deduction. The fund invests the money in an account the donor creates from a menu that offers different mutual funds. Donors only recommend which charities should receive their contributions. The fund makes the actual grants.

Some experts say donor-advised funds are particularly appealing for people giving \$1 million or less, because the costs of using such a fund are generally less than running a private foundation, particularly if its arrangements are complex. In the current economic downturn, when investment returns are generally not rising, funds have been aggressive in trying to control costs.

"Starting last summer, we had more calls coming to us: clients wanting to switch money from private foundations to donor-assisted funds," said Sarah Libbey, president of the Fidelity Charitable Gift Fund. "We are finding that private foundations can be too burdensome for many donors who are trying to accomplish pretty simple objectives."

The number of new accounts at Fidelity's donor-advised fund so far this year is in line with last year, Ms. Libbey said, but with the markets' downward spiral, contributions to existing accounts fell 40 percent in the first six months of this year from the comparable period in 2007.

Some investors like the privacy of donor-advised giving. "If you create a foundation, there are tax filings that make it easier for people to find out how much money you put in a foundation,

but they cannot find out the individual's contribution to the donor-advised fund," said Daniel Jick, of the High Vista Endowment fund, which manages money for endowments, families and foundations. Mr. Jick uses a donor-advised fund himself because he likes the privacy.

Of course, private foundations offer advantages, most notably control. Donors can create their own board, choose investments from across the entire financial spectrum and give with equal ease to foreign and domestic charities. "A foundation allows you the full range of flexibility and control," said Tim Walters, head of the Association of Small Foundations.

Another characteristic of private foundations is how they can grow over time. Most foundations give away about 6 percent of their asset value every year (the law requires them to give away at least 5 percent); donors in donor-advised funds generally give away 20 to 30 percent of their asset value each year, experts say.

At Fidelity, Schwab and Vanguard, for example, most investors must choose among a collection of the company's own funds. Only when donations reach certain levels are investors permitted to select outside investments.

At Vanguard, for example, donors with \$1 million or more in Vanguard's charitable fund can choose to have that money managed by the Investment Fund for Foundations, which manages money for nonprofits through a strategy that invests in a variety of entities beyond stocks and bonds. They may include some of the best-known hedge funds.

At Fidelity, donors who put up more than \$1 million can select their own managers, although they have to be vetted by Fidelity.

But in surrendering control of investments, you may reap larger tax benefits at donor-advised funds.

Donors can contribute and deduct up to 50 percent of their adjusted gross income a year when they donate cash to a donor-advised fund or public charity. If the cash gift goes to a private foundation, the limit is 30 percent. (With gifts of appreciated stock, the percentages are lower in both cases.)

A donor also pays an annual excise tax of about 2 percent on any income a foundation generates.

As for continuing costs, Ben Pierce, executive director of the Vanguard Charitable Endowment Program, said managing a \$1 million donation to Vanguard costs roughly \$7,700 a year, which includes about \$5,700 in administrative fees and the balance in investment fees.

Mr. Pierce and others point out that setting up a foundation typically costs about \$5,000. Creating and managing a complex foundation can cost much more. But "if you keep it simple and handle the investments yourself, the only expenses are setting it up and doing the tax returns," said Margaret Sager, a trust and estates lawyer and partner at Heckscher, Teillon, Terrill & Sager in Philadelphia.

Some companies provide services to help streamline the operations of more complex foundations. Foundation Source, a company in Fairfield, Conn., handles the administration of foundations online. Its annual administrative fees for a foundation with \$1 million in assets are roughly \$8,000, according to its chief operating officer, Andrew Bangser, who said customers get a range of services, including the vetting of charities. Foundation Source charges a one-time fee of \$4,900 for setting up a foundation.

John E. Lane III, who runs the \$1.3 million Edward H. Lane Foundation in Roanoke, Va., said that while Vanguard offers a product that frees the hands of the small foundation operator from administrative details, he preferred to set his foundation's investment policy on his own. "It is the difference between outsourcing and doing it yourself," he said, adding that the foundation's expenses are below \$3,000 a year because it does not do much trading.