



## Navigating the Quid Pro Quo Trap – How It Affects QCDs and DAFs

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Qualified charitable distributions (QCDs) and donor-advised funds (DAFs) are lucrative sources of philanthropic dollars available for current use. Donors often use QCDs and/or DAFs to make tax-advantaged annual gifts. In addition, donors make tax-smart major or even principal gifts from one of these sources. However, both QCDs and DAF grantmaking rely on donor and charity self-reporting to comply with the rules regarding permissible gifts from these sources.

It is hornbook law<sup>1</sup> that a QCD to charity will only qualify as a QCD if the “entire distribution would be allowable under Section 170”<sup>2</sup> as a charitable deduction. Likewise, it is universally understood that using a DAF to make a grant for a quid pro quo donation is also prohibited. A DAF grant cannot provide a “more than incidental” benefit to the donor.<sup>3</sup> Therefore, both DAF donor advisors and QCD donors cannot enjoy quid pro quo benefits that exceed the insubstantial value rules applicable to these gifts.

Neither DAF grants nor QCD distributions are entitled to an income tax charitable deduction. However, when a donor makes DAF or QCD gifts, the tax law relies upon the donor’s good faith in making the gift and the charity’s proper treatment in accepting and using the donor’s gift. Failure to follow these quid pro quo rules is unlikely to attract IRS attention unless an improper gift is discovered in the course of an IRS audit. Following tax

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<sup>1</sup> A legal principle so well understood that it is considered self-evident.

<sup>2</sup> Internal Revenue Code Section 170 governs the tax deduction for charitable contributions.

<sup>3</sup> Internal Revenue Code §4967

law, even when the IRS isn't looking, establishes the credibility and philanthropic motive underlying the preferential tax treatment of charitable gifts.

## **Key Principles**

The Internal Revenue Code establishes the principle that when a person receives something of value in return for a donation, it creates a quid pro quo transaction. In exchange for a DAF grant, the donor may not receive a “more than incidental” benefit. A quid pro quo benefit is more than incidental if its fair market value exceeds certain annually adjusted low-cost thresholds.

If there is any quid pro quo benefit to a QCD donor, the entire QCD is disqualified not just the benefit portion. Therefore, a DAF grant or QCD that would otherwise be non-deductible or not fully deductible is not permissible.

## **More Than Incidental Benefit**

Donor benefits for DAF grants and QCDs are only permitted if the benefit is of insubstantial value. The rules for what constitute insubstantial value are updated annually for inflation. For the 2025 tax year, charitable gifts are considered insubstantial if the fair market value of all benefits received is no more than 2%<sup>4</sup> of the donor's payment or \$136, whichever is less or if the donor's payment is at least \$68.<sup>5</sup> Token items such as mugs, calendars, or keychains are considered of insubstantial value.

## **Non-deductible Gifts**

Neither DAFs nor QCDs may be used to make non-deductible charitable gifts. Non-deductible gifts under Internal Revenue Code Section 170 include gifts made to an educational institution that entitle a donor to purchase tickets to an athletic event. Any benefit received from the charity in exchange for any “goods or services” is a non-deductible gift except those gifts of insubstantial value that the IRS allows to be disregarded.

## **Gifts Not Fully Deductible**

A gift is not fully deductible if the donor's gift exceeds the fair market value of the goods or services received. For example, if a donor pays \$500 for an event ticket with a fair market value of \$100 and intends to give more than the ticket's value, the deductible amount is \$400.

Other examples of gifts that are not fully deductible, and therefore ineligible for QCD treatment, include tickets for raffles, bingo games, or lottery-based drawings at a

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<sup>4</sup> IRS Revenue Procedure 1992-102

<sup>5</sup> IRS Revenue Procedure 2024-40 Section .34 (2)

fundraiser. If a donor pays a membership fee, it is only deductible to the extent the gift portion exceeds the benefits the donor receives.

### **Bifurcation of Gifts**

The IRS prohibits a donor from paying for the non-deductible portion of an event ticket or sponsorship with their personal funds while using a DAF grant for the deductible portion. This was explicitly addressed by the IRS in Notice 2017-73, which stated that such an arrangement still provides a more than incidental benefit to the donor. While Notice 2017-73 specifically applied to DAFs, it is logical to conclude that the Notice also applies to QCDs. The guidance in the Notice establishes that the IRS considers bifurcated gifts to provide a more than an incidental benefit.

### **Don't Ask, Don't Tell: Satisfying Pledges**

IRS Notice 2017-73 also offered advice on handling grants from a DAF that fulfill a personal pledge of a donor advisor. A pledge, even a legally binding pledge, will not be treated as a "more than incidental benefit" on three conditions. First, the DAF administrator may not refer to the existence of the charitable pledge. Second, the DAF grant can't provide more than incidental benefit to the donor advisor. Third, the donor advisor may not claim an income tax charitable deduction for the DAF grant. The IRS Notice provided that donor advisors and DAF administrators could rely on the guidance relating to fulfillment of pledges immediately upon publication of the Notice.

IRS Notice 2017-73 implies that QCDs may be used to satisfy personal pledges under the same conditions applicable to DAFs. On its face the Notice applies to only DAFs. Nonetheless, the IRS seems to be signaling that satisfaction of pledges is not more than an incidental benefit and therefore fully deductible to the donor. Under that logic, using a QCD to satisfy a pledge seems to be permissible. Due to the uncertainty, consult your legal counsel before allowing a donor to satisfy a pledge with a QCD.

### **Acknowledgement of QCD Gifts and DAF Grants**

A charity is not required to provide an acknowledgement or a receipt upon receiving a grant from a DAF. The tax deduction was already claimed by the donor when they made their initial contribution to the DAF.

By contrast QCDs are only valid if the donor obtains a written acknowledgement from the charity indicating that no goods or services were received in return for the contribution. The charity should acknowledge the amount of the distribution and that no goods, services, or benefits of any kind were provided. The acknowledgement should not make any reference to the deductibility of the gift. (Do not include language such as "Your gift is deductible to the full extent of the law.")

It is best practice for a donor to notify the charity that they intend that a QCD distribution from an IRA should be treated as “qualified charitable distribution.” Likewise, DAF donors should let the charity know they should expect a grant. Nonetheless, donors often fail to inform the charity that a gift is intended to be a QCD or that the donor is making a grant from their DAF. Frequently, charities receive checks from DAF and IRA administrators with no identifying information. DAF and QCD marketing materials should emphasize their gifts can only be credited in accordance with the donor’s intent if they notify the charity to expect their QCD or DAF. Also, if the charity isn’t expecting the gift, it may be impossible to even thank the donor for making a QCD or DAF grant.

### **Managing Donor Expectations**

Charitable gifts cannot be exchanged for goods or services. The charitable amount of a donation will be reduced by any benefits received by the donor, such as meal vouchers or event tickets. Donors cannot receive quid pro quo benefits for gifts from QCDs or DAFs. A QCD could be reclassified as a taxable distribution if the donor receives any benefit. Gifts funded by DAFs cannot include any benefit to the donor that is more than incidental. Charities should share these rules with donors to avoid any unwanted penalties or tax consequences.