

TIMELY UPDATES ON PRIVATE FOUNDATION GIVING MATTERS

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FOUNDATIONSOURCE

Your Partner in Giving

Who We Are

FOUNDATION SOURCE is the nation's largest provider of management solutions for private foundations.

- Founded in 2000
- National footprint
- **2,000+** private foundation clients
- ~225 employees
- **97%** client satisfaction
- Administers **\$22+ billion** in foundation assets
- **8,000+** users of Impactfully[®] technology
- Facilitated **530,000+ grants** totaling more than **\$12 billion in charitable aid**
- Planned giving solutions for nonprofits & financial institutions



How We Partner with Investment, Tax & Legal Advisors



- We help advisors provide expert charitable giving & philanthropy guidance to their clients.
- We work behind the scenes or directly with the client.
- We have an extensive online Resource Hub that advisors can access for educational materials to share with clients.
- For clients interested in private foundations, we can handle specifics and complexities such as foundation set-up, compliance monitoring & daily administrative tasks.
- For clients needing planned giving assistance, we can help with the details of charitable gift annuities, pooled income funds, charitable trusts, bequests & endowment sub-accounting.

Agenda

- Philanthropy Update
- Private Foundations and Donor-Advised Funds (DAFs)
- Legislation Update: Proposed DAF Regulations
- Charitable Investing



Philanthropy Update



Philanthropy
is increasingly
important.

It's an
opportunity
for advisors.

- Over the past 40 years, **US GIVING HAS INCREASED 9x*** from ~\$50 billion to ~\$450 billion annually
- **88.1% OF AFFLUENT HOUSEHOLDS** give to charity
- **ULTRA-WEALTHY WOMEN RANK PHILANTHROPY AS THEIR TOP INTEREST** (over art, education, sports, etc.)
- **80% OF WEALTH INHERITORS** (younger generations) **expect to increase their involvement in philanthropy**

Private Foundations and DAFs

**SIMILARITIES AND
CONSIDERATIONS**



Similarities of PFs and DAFs



Some of the underlying advantages to these giving vehicles are the same.

Contributions generate a **CURRENT-YEAR INCOME-TAX DEDUCTION** for charitable gifts that are made in the future

CAN AVOID CAPITAL GAINS TAXES on appreciated securities that are donated to the private foundation or donor-advised fund

EXEMPTION FROM GIFT AND ESTATE TAXES on donated assets

TAX-ADVANTAGED ASSET GROWTH

CONTRIBUTIONS to a DAF and private foundation **ARE IRREVOCABLE**

Structure

A donor's vision for his/her philanthropic goals often defines which giving vehicle is best suited for the purpose.

PF



AN ORGANIZATION:

An independent legal entity that is governed by an individual, family, or business

- Can be set up as a corporation or a trust
- Has its own tax ID number
- Files for tax-exempt status with the IRS
- 66% of all private foundations have assets of less than \$1 million (IRS data)

AN ACCOUNT:

A giving account that is housed within and governed by a public charity.

MINIMUM INITIAL CONTRIBUTION:

\$5,000 - \$25,000
(varies by organization)

DAF



Control

When control is important – due to the behavioral makeup of the individual or intended philanthropic outcomes – this can also help inform the decision.

PF



- Donor determines governance structure and bylaws
- Donor can govern the foundation alone or can select family members and others to serve on the board.
- Donor maintains complete control over grantmaking and investment decisions
- Can pay reasonable compensation to insiders
- Can exist in perpetuity

DAF



- Donor recommends grant recipients to the sponsoring organization's governing board
- Donor recommends investment selections to the governing board
- Each named “advisor” can act independently to recommend gifts
- Limits on number of successor advisors
- Cannot compensate insiders

Differences in deductibility are rarely the deciding factor when choosing between these two giving vehicles.

Tax Treatments

- There is a five-year carry-forward for any contributions that exceed these limits.
- Donors can max out the deduction to a private foundation, then make additional tax-deductible contributions to a public charity up to the higher limit, which could include the individual's donor-advised fund.



	PF	DAF
CASH DONATIONS:	30% of AGI	60% of AGI*
LONG-TERM APPRECIATED STOCK:	20% of AGI	30% of AGI
Generally deductible at:	FMV	FMV
OTHER LONG-TERM APPRECIATED ASSETS:	20% of AGI	30% of AGI
Generally deductible at:	Cost Basis	FMV

**Up to 50% AGI if a combination of cash and non-cash assets or a combination of PF and DAF gifts.*

Investments

May have an impact on the family's wealth preservation and transfer plans.

PF



- Can hold nearly any type of asset in the foundation:
 - Cash & mutual fund shares
 - Publicly traded bonds and securities
 - Private equity and closely held stock
 - Partnerships
 - Real estate
 - Tangible assets (art, jewelry, collectibles)
 - Stock options
 - Intangible personal property
- Donor works with existing financial advisor to manage the foundation's investments

- Typically, a standardized selection of mutual funds or limited menu of proprietary pooled investment options
- Donated assets often liquidated (unable to hold stock XYZ, alternative assets, tangible assets); may incur additional transaction fees
- Some DAFs offer the flexibility of a separately managed investment account when over a certain size. (**could result in penalties if proposed legislation passes**)

DAF



Grantmaking

IRS rules dictate inherently different granting capabilities, so donors need to evaluate both short-term and enduring goals.

PF



- All types of nonprofits, including public charities
 - International grants
 - Grants to individuals for disaster relief/economic hardship
 - Scholarships, awards, prize programs
 - Direct charitable activities (coat drive/soup kitchen)
 - Program-related investments
 - Grants to for-profit entities when they support the foundation's mission
- Annual 5% minimum distribution requirement

DAF



- Primarily to 501(c)(3) public charities in the U.S.
- Primarily for “no frills” or routine financial support
- Limited, but growing ability to make international gifts
- Cannot make grants to individuals
- No annual distribution requirement

Convertibility

CLIENTS SHOULD CHOOSE CAREFULLY:
the decision of which vehicle to set up cannot always be undone.

PF



A PRIVATE FOUNDATION:
may grant all its assets to a donor-advised fund and then shut down

DAF SPONSORS
have rules that make it all but impossible for a DAF to convert to a private foundation

DAF



Why Your Clients Might Want a DAF



Grantmaking needs are simple and straightforward.

HAVE FEWER CHARITABLE DOLLARS for initial contribution

Give exclusively to **U.S. PUBLIC CHARITIES**

Don't care about **PERPETUITY** (i.e. pass through)

Want **COMPLETE ANONYMITY** for granting

Plan to fund primarily with **REAL ESTATE OR APPRECIATED PERSONAL PROPERTY DUE** to tax treatment of these assets

Why Your Clients Might Want a Foundation



They want access to the full capabilities allowed by the IRS to a private foundation.

FULL OWNERSHIP AND CONTROL over investment and grant decisions

Choose their **OWN BOARD AND COMPENSATE DIRECTORS**, if desired

DO MORE WITH THEIR PHILANTHROPY than grants to U.S. public charities

DONATE TANGIBLE ASSETS that won't be sold (e.g., art, antiques)

HAND DELIVER grant checks

CREATE GRANT AGREEMENTS for major gifts

PASS DOWN TO FUTURE GENERATIONS in perpetuity

HIRE STAFF, including family members

Reasons to Have Both



Complete Anonymity in Giving



PRIVATE FOUNDATIONS MUST RECORD THEIR GRANTS

on their annual tax return, which must be available for public inspection.

DAF SPONSORING ORGANIZATIONS ARE NOT REQUIRED TO SHOW WHICH GRANTS are associated with which DAF accounts.

When making donations to a controversial or politically charged issue, the donor could grant funds from the foundation to the DAF and make anonymous grants from there. This strategy can also be used to **AVOID A FLOOD OF GRANT REQUESTS FROM ORGANIZATIONS** similar to the ones being supported.

Avoid Mission Drift and Confusing the Charitable Community



Foundations often have **A DEFINED MISSION** that informs their grantmaking and the organizations they support

Some foundations, however, give board members a portion of funds to grant as individuals. When these grants are **OUTSIDE OF THE FOUNDATION'S MISSION AREA, IT CAN CAUSE CONFUSION** as to what the foundation actually stands for.

Instead, the foundation could **SET UP INDIVIDUAL DAFs** for board and family members that are used for these side projects.

Assists in Strategic Deployment



A private foundation may be nearing the end of the year and still not have met its 5% minimum distribution requirement.

Rather than make a flurry of hastily considered grant decisions, or incur a penalty for missing the distribution requirement, the foundation can **GRANT THE OUTSTANDING AMOUNT TO HIS/HER DONOR-ADVISED FUND** to satisfy that requirement.

This gives the donor additional time to decide how best to use those charitable dollars.

Donor Scenarios



Having Both a PF and a DAF

GIVING BENEFITS

Donors get a complete toolkit for achieving philanthropic goals:

- PF can enter into grant agreements with the recipients
- PF allows donors to personally present grant checks
- DAFs let the donor make anonymous grants to competing organizations



FINANCIAL BENEFITS

Donors can maximize tax benefits and reduce fees

- “Stack” contributions to maximize deductibility
- Donate alternative assets to PF



SUSTAINABILITY BENEFITS

Donors Can “Future Proof” Their Giving

- DAFs allow limited advisor succession
- PFs can exist in perpetuity
- Convertibility is a one-way street

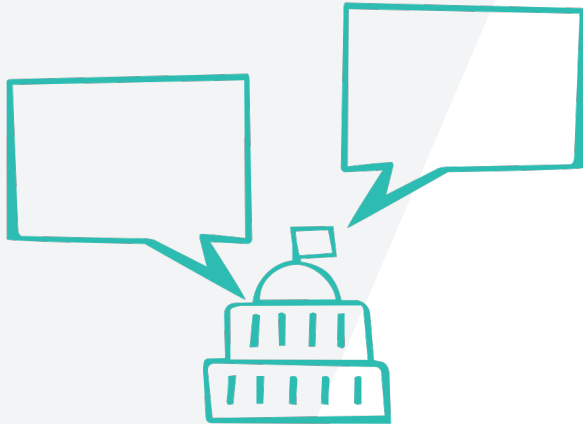


Legislation Update

Proposed DAF Regulations



DAF Discussion



There has been considerable discussion on **Capitol Hill** as to whether DAFs should be held to some of the same rules as private foundations.

Should individual DAF accounts have an **ANNUAL PAYOUT REQUIREMENT?**

Should **INCOME-TAX DEDUCTIBILITY** be the same for DAFs and private foundations?

Proposed Regulations on DAFs



In November 2023, the IRS issued proposed regulations for DAFs. Key elements:

- Ability to use compensated personal investment advisors for DAFs effectively precluded
- Broad definitions of “DAF” and “donor-advisor” could extend DAF restrictions to funds not previously thought to be DAFs
- Potential threat to donors’ income tax deductions
- Anti-abuse rule

Charitable Investing

How Savvy Foundations Maximize
Impact and Tax Benefits



Agenda



Charitable Investing:

- Putting the program related investment (PRI) into context
- Knowing a PRI when you see one
- Coordinating the PRI with other private foundation (PF) rules
- Consequences of a “failed” PRI
- Common PRI myths
- Where does the mission related investment (MRI) fit in?

Foundation Investment Basics



Jeopardizing Investments

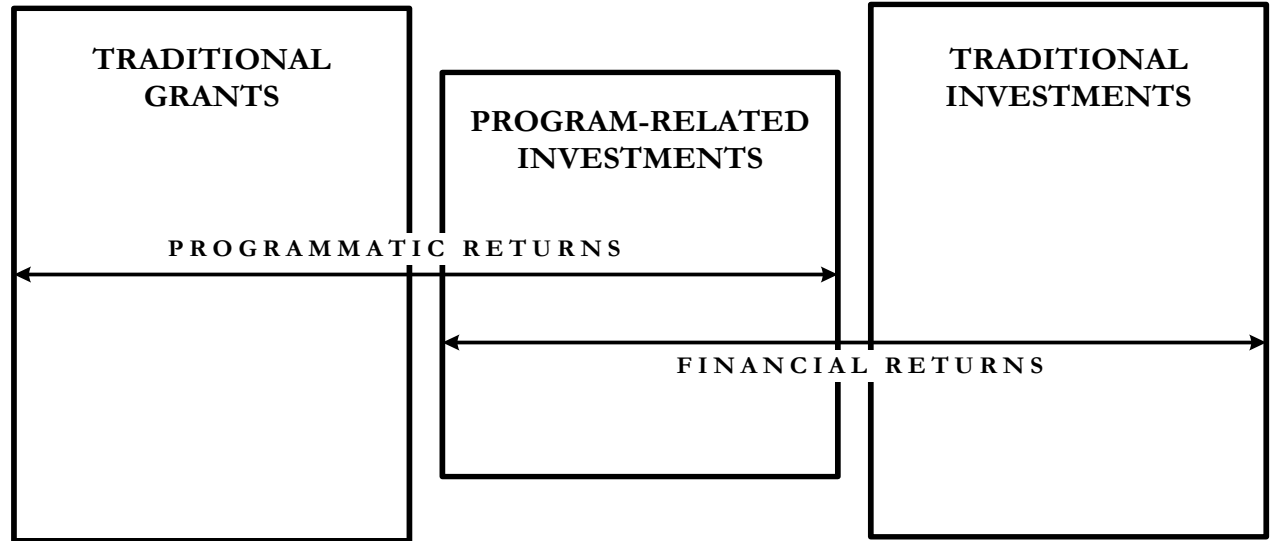
- Lack of reasonable business care and prudence
- Investment-by-investment
- Evaluating the portfolio as a whole
- Factors that may be considered
- Compliance determined at the time of investment
- 10% penalty

PRI in Context



- Reasons for private foundation investments
- PRIs are not subject to the jeopardizing investment excise tax
- PRIs are not subject to normal prudent investment standards
- PRIs are mission-driven investments
- PRIs are more like grants than investments for legal purposes

Hybrid of Grants and Investments



PRIs OCCUPY A MIDDLE GROUND BETWEEN TRADITIONAL GRANTS AND INVESTMENTS

Source: PROGRAM-RELATED INVESTMENTS A TECHNICAL MANUAL FOR FOUNDATIONS, CHRISTIE I. BAXTER (1997).

Forms of Investments



- **Direct loans**
- **Loan guarantees**
- **Equity investments**

Is the investment a PRI? (1 of 3)

TEST #1



THREE TESTS MUST BE SATISFIED:

The primary purpose of the investment must be to further an exempt purpose

- The “significantly further” sub-test
 - Validity of Section 501(c)(3) purpose
 - Compatibility with private foundation’s purpose
- The “but for” sub-test: having the right *intentions*

Is the investment a PRI? (2 of 3)

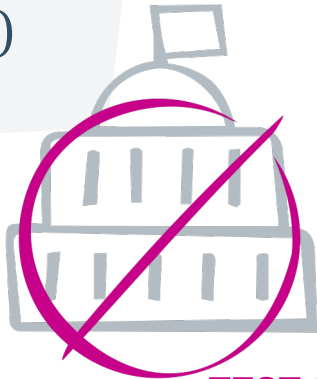


THREE TESTS MUST BE SATISFIED:

The production of income or the appreciation of property must not be a significant purpose of the investment

- The fact that an investment pans out and produces significant income or appreciation does not automatically invalidate the PRI
- Would commercial investors find the deal terms unattractive?

Is the
investment
a PRI? (3 of 3)

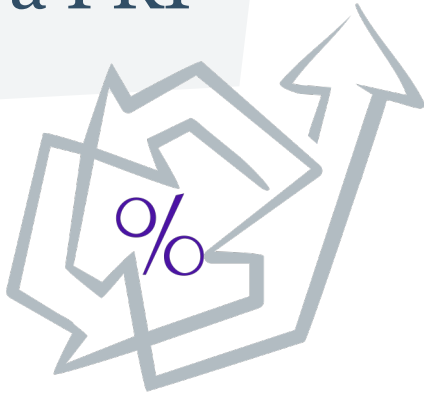


TEST #3

THREE TESTS MUST BE SATISFIED:

*The PRI must not be used to fund
electioneering or lobbying activity*

Benefits & Tax Implications of Making a PRI



- Advances the private foundation's mission
- Permits leveraging of assets and recycling of limited resources
- Tax implications:
 - Counts as a “qualifying distribution” in the year made
 - PRI's value is excluded from the 5% payout asset base
 - Nominal excise tax on interest, dividends, capital gains
 - Repayment of principal creates a “recovery”
 - Special oversight procedures may be required

Consequences of a Failed PRI



- The investment will not be a qualifying distribution
- Under-distribution penalties may apply if relied upon to satisfy the minimum 5 percent payout requirement
- The investment is factored into determining the minimum 5 percent payout requirement
- If imprudent could be a jeopardizing investment
- If an equity investment, the excess business holdings rules apply

Two Common Misconceptions



MYTH #1
A foundation needs
IRS advance approval
to make a PRI

False. Advance IRS approval is not required, though it may be desirable if the investment is especially large, complex, or unusual.

MYTH #2
A foundation needs
an opinion letter from
counsel to make a PRI

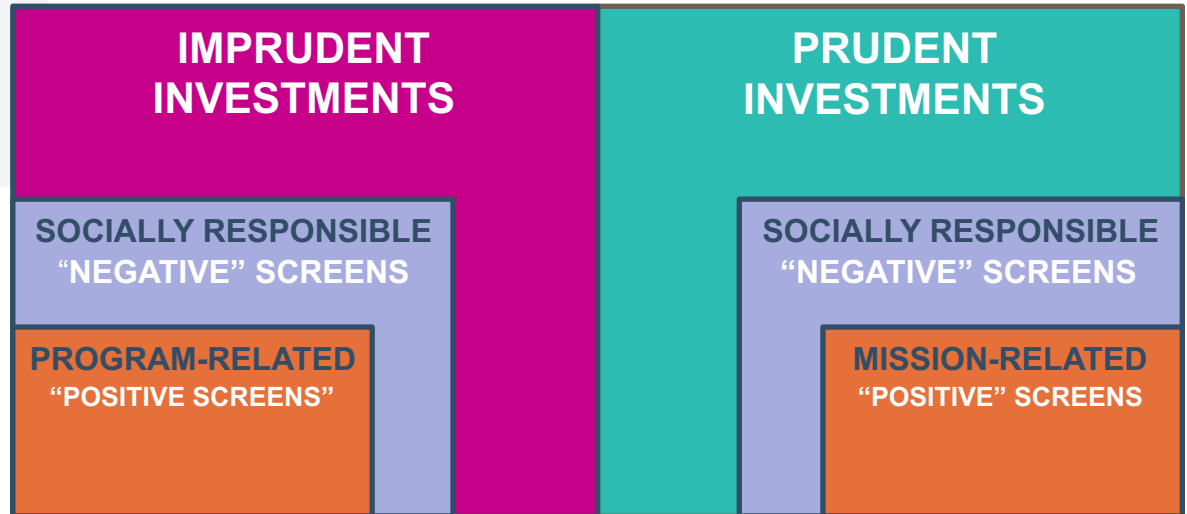
False. However, a legal opinion may shield a foundation's officers and directors from personal liability.

Mission Related Investments (MRIs)



- Seeks dual return
- Does not satisfy PRI tests
- Jeopardizing and prudent investor rules DO apply
- MRIs are not Socially Responsible Investments (SRIs)
- Treated the same as traditional investments for tax purposes
- Updated rules make MRIs less risky

The Investment Universe: PRI vs. MRI



A New Twist on Traditional Legal Forms



- Constituency statutes
- Benefit corps
- “Hybrid” entities
- L3Cs
- Certified B corps (metrics)

QUESTIONS?



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Thank You.

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