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Benefiting From a Private Family Foundation

A PRIVATE FOUNDATION CAN BE A REWARDING PHILANTHROPIC ALTERNATIVE FOR YOUR FAMILY TO CONSIDER.

For many families, budgeting a percentage of their assets for charitable donations each year has always been a way of life. Typically, they would select a few charities that appeal to them and simply send in a check. However, in recent years people have increasingly moved away from this "checkbook philanthropy" and instead have set up their own private family foundations to achieve their philanthropic goals.

According to the Foundation Center, a New York-based tracker of nonprofit philanthropic organizations, a foundation is defined as "a nonprofit corporation or a charitable trust, with a principal purpose of making grants to unrelated organizations or institutions or to individuals for scientific, educational, cultural, religious, or other charitable purposes."

They also state that the most common distinguishing characteristic of a private foundation is that most of its funds come from one source—such as a family—whereas a public foundation derives its funds from numerous donors. In 2004 there were 31,347 family foundations, an increase of 28% over four years. Three-fifths of family foundations actually have less than $1 million in assets.

IS A PRIVATE FOUNDATION RIGHT FOR YOU?

Susan Price, managing director of Family Foundation Services at the Council on Foundations in Washington, D.C., says that starting your own foundation is not always easy. Foundations "aren't for everyone," she says. Running your own foundation can be costly. Before you make a single donation, it's likely you'll lay out at least $10,000 in start-up costs. Once created, foundations require a lot of work, and families usually decide to hire one or two full- or part-time employees to keep up with the heavy workload.

The benefits, however, usually outweigh the cons. "If people want more control over where their philanthropy dollars are going, and if you want to have a way for your family to work together on gift making, a private foundation is a good vehicle to consider," says Price. One of the biggest criticisms of checkbook philanthropy is that you have few ways of measuring your dollars' effectiveness. Many charities have high overhead costs, and people who simply write checks to these organizations without looking into where their dollars go might unwittingly be feeding this trend. Having your own foundation allows you to better assess the impact of your giving since you can monitor how every dollar is used.

Putting your money into your foundation also creates an instantaneous deduction on your personal income tax return. Donors can take the fair market value of their gift and deduct as much as 30% of adjusted gross income for cash gifts and 20% for gifts of property. A foundation's assets are also exempt from government taxation. Private foundations are required to give away at least 5% of net assets each year to charitable causes, but

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Managing Director of Family Foundation Services at the Council on Foundations in Washington, D.C

the assets that are not immediately donated to charities are typically invested in stocks, bonds and real estate. Gains on these investments are exempt from both federal and state taxes, allowing them to grow faster.

Another potential benefit of setting up your own private foundation is the opportunity to involve the entire family in philanthropy. It allows you to create an avenue for your charitable giving legacy within your family, and lets you involve your children and perhaps your grandchildren in the execution of that legacy. Running your own family foundation will require you to perform on-site visits to organizations to which you are considering pledging money, providing an opportunity to bring along your children and walk them through some of your own questions: Is this a worthwhile cause? How is this charity influencing people's lives?
It's also important to consider your children's ages before assigning them a role in the foundation. For younger children, consider splitting their allowance into two parts—one for spending and one for giving. Then, let them decide on their own to what kind of organization they would like to donate their money. Teenagers should be asked to join in on foundation meetings with their parents or grandparents. Encouraging them to give input into potential gifts will keep them interested in the family's philanthropy in the future.

GETTING STARTED

Once your family decides that a private foundation is a good fit, it's important to meet with an advisor to help walk you through some important first steps.

Find a Focus. Deciding how you want to donate your foundation's money is important. According to the Foundation Center, in 2004 almost 30% of dollars granted by family foundations went to health-related charities. However, you can use your foundation's assets toward a wide array of charitable causes, such as setting up a scholarship fund or helping build a local center for the arts.

You will need to provide a mission statement when filing the initial paperwork, but you can usually be quite general. "A mission that says, 'We will donate to organizations that further the causes of health, education and science' is broad" and won't pigeonhole your philanthropy, says Price.

Funding. When putting money into your foundation, be sure to consult a financial professional to discuss how to maximize your foundation's return on investment. It is important that the assets grow while they are not being granted to charity. It is also a good idea to have your accountant oversee the donations to make sure you receive the maximum tax benefit.

Stay Compliant. As with any tax-exempt organization, extensive paperwork is constantly required when running a private foundation. It's important to seek the counsel of an advisor or attorney who knows the ins and outs of foundations to make sure you don't miss important steps. To comply with state and federal regulations, foundations must keep detailed documentation of all grants they make, and to attain and keep their tax-exempt status, foundations must donate 5% of net assets each year. Foundations must also file an IRS Form 990-PF every year; this is known as the tax return of private foundations.

Once created, private family foundations can provide long-lasting benefits for a family that can be passed on to many future generations. If you are interested in setting up a family foundation, you should seek proper guidance from your financial advisor so you can achieve maximum results for your philanthropic and investment goals.

The information provided herein is not intended as legal or tax advice. Please consult a qualified attorney and/or certified public accountant with respect to the legal and tax ramifications involved in setting up and maintaining a private family foundation.