

FPA

Who Needs a Private Foundation?

Presentation for Estate Planning Council of Diablo Valley

November 16, 2011

Teresa Bonner

Supporting Journeys of Generosity

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FPA *Overview*

- Identify issues for consideration in advising clients regarding philanthropy
- Suggest scenarios when a private foundation is the right choice for a client
- Discuss current trends in private philanthropy

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Issues for Consideration

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FPA *The Advisor's Point of View*



"I consider myself a passionate man, but, of course, a lawyer first."


© 2011 The New Yorker

FPA *First Things First*

Understand your client's journey...
...before you recommend their vehicle.

*Where does your client want to go?
 Who do they want to take on the journey?
 What do they want to do along the way?*

(Not all clients are motivated by low maintenance.)



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FPA *Where does your client's journey start?*

- What's the client's motivation to give?
- What's their level of commitment?
- What's your client's personality and style?
- Who else is in the picture? Where are they?
- Where does your client want to take the program – the "business plan" for philanthropy?
- How much money are they planning to contribute?

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Client Motivations Vary

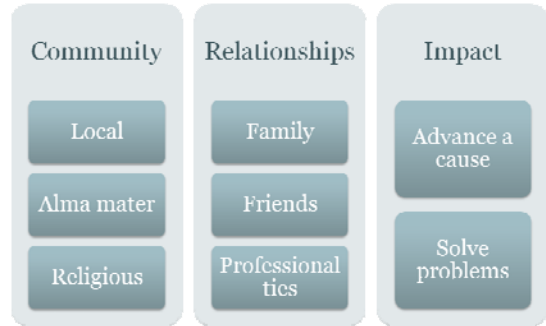


"I contributed a lot to charity when I thought I was going to die."

Source: The New Yorker



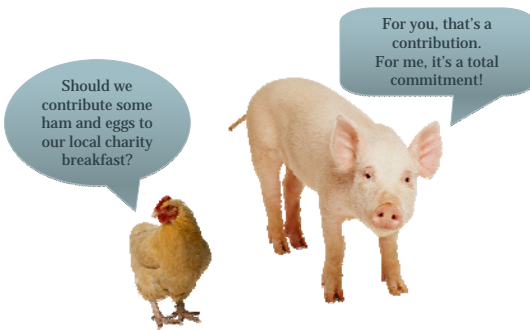
Motivations Often Drive Programs



Source: Leslie R. Crutchfield



Consider Your Client's Commitment Level



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What impact does your client want to have on the world?

- Client's personal passions and interests
- Awareness of community needs
- Linking passions to needs
- What is their "blue sky" for philanthropy?

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What are your client's hopes for their family?

- "Glue"
- "The work"
- Legacy
- Perpetuating values and culture
- Clarifying roles and participation
- Education and engagement of next generation

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What does a private foundation require?

- Separate 501(c)(3)
- Board and governance
- Staff
- Legal and accounting
- Investment management
- Due diligence and compliance
- Filings: 990-PF, state of incorporation requirements

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What's your client's capacity?

- For learning
- For administration
- For due diligence
- For creativity
- Of an advisory team

Help is available!

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Multiple Staffing Models Exist

- Family member(s) as staff
- Consultant and/or bookkeeper
- Build out full staff, rent offices, etc.
- Engage management firm

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The Right Resources Matter



"The Amazingly Inexpensive Moving Co."

Source: The New Yorker

When might a private foundation be the right choice?

[It's about more than asset size.]

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Consider Personality



"Don't listen to her—she's a control freak. Now, let me tell you what you're gonna do."

Source: The New Yorker



Desire for Control

- A private foundation may be the right choice if your client...
 - ✓ Wants a high level of control over activities/process
 - ✓ Is entrepreneurial or an activist
 - ✓ Wants to *personally* impact a cause or issue through investment and/or activity
 - ✓ Wants investment control
 - ✓ Expects major involvement by family members

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Program Directions

- A private foundation may be the right choice if your client...
 - ✓ May want to pursue direct charitable activities – convening, creating special initiatives and programs, creating a prize or award program, etc.
 - ✓ Wants to support advocacy
 - ✓ Wants to make grants to individuals
 - ✓ Wants to give outside the DAF guidelines
 - ✓ Is interested in socially responsible investing or impact investing

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The Journey

- Education of philanthropists
- Development of operating principles and practices
 - Mission
 - Vision
 - Operating policies - board meetings, conflict of interest, travel and expense
- Program development and implementation
 - Priorities
 - Guidelines
 - Process
 - Research, recommendations and due diligence
 - Implementation and evaluation

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Roles and Stages Evolve



Don't assume your client will stay on the first step!

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When is it useful to have a PF and a DAF at a CF?

- When the client wants the control of a private foundation, plus:
 - ✓ Anonymity for some gifts
 - ✓ A separate fund for family members to direct - outside the family foundation structure and control
 - ✓ A way to give "off-mission"
 - ✓ Participation in a community of donors
 - ✓ Education on philanthropy and community issues

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Trends and Topics

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Changes in the Landscape

- Demand for greater social return
- Personal engagement
- Prizes: ArtPrize, XPrize
- Generational: Business schools, social enterprise, Nexus Youth Summit
- Sunsetting ("giving while living")
- The Giving Pledge: 20% of American billionaires
- "The other 95%"

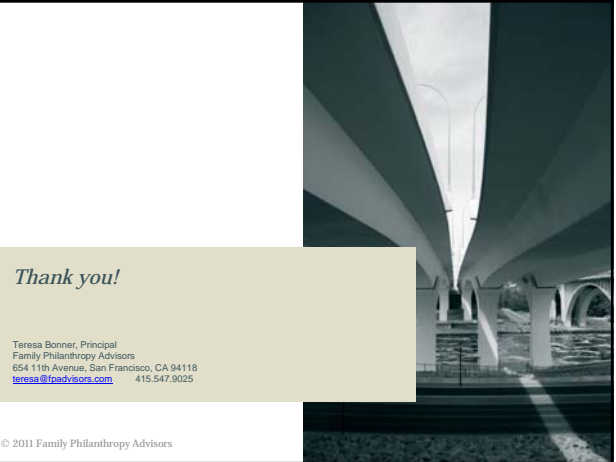
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Examples and Inspiration

- The Bravewell Collaborative
- Family foundation with roots in Ohio
- Durfee Foundation
- Jacobs Family Foundation
- Rosemary and David Good Family Foundation

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Thank you!

Teresa Bonner, Principal
Family Philanthropy Advisors
654 11th Avenue, San Francisco, CA 94118
teresa@fpaadvisors.com 415.547.9025

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EBCF Philanthropic Services

Presented to EPC Diablo Valley

Nicole Taylor, President & CEO

November 16, 2011



www.eastbaycf.org

Community Foundation Legacy

- In 2012, will celebrate 100 years of community trusts/foundations in US
- EBCF is the oldest California community foundation founded in 1928
- Primary role is to strengthen communities via grant making AND working with constituents in providing philanthropic advice and services.
- Bay Area has 4 large and 6-8 smaller CFs and they do overlap their service areas
- Most CFs have a variety of fund types



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EBCF Development/Philanthropic Services

We group our clients into a few scenarios:

- Wealth Incident / Healthy Business
- Planned Gifts / Testamentary Funds
- Multi-Generational Family Philanthropy

We offer several ways to organize philanthropy:

- Supporting Organizations
- Donor Advised Funds, B of A Merrill Lynch DAFs
- Field of Interest Funds
- Agency Funds



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Wealth Incident / Healthy Business

- Types of Events
 - Selling a business
 - Appreciated stock
 - Business success leading to entre into philanthropy
 - Tax planning
 - Inheriting wealth



4

Planned Gifts / Testamentary Funds

- Long term tax planning (CRT, CLT, bequests, ...)
- Documentation of donor intent; with or without successor advisors
- Initial contribution to set-up; small change fee in future if interests change
- Perpetual or term charitable endowments
- Beneficiary of trusts
- Unrestricted gifts to support the work of EBCF



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Multi-Generational Family Philanthropy

- Vision and values facilitation
- Giving framework
- Formal giving plan
- Succession planning for family philanthropy
- Measuring success and impact



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Options for Organizing Philanthropy

- Supporting Organizations
 - ❑ \$5MM minimum
 - ❑ Incorporated nonprofit with a board of directors
 - ❑ Supports EBCF mission
- DAFs
 - ❑ \$10,000 minimum to open
 - ❑ Broad or specific purpose, common entry to philanthropy
 - ❑ Specific services for corporate/business clients
- BAML DAFs
 - ❑ Collaboration with BAML and Community Foundations nationwide
 - ❑ \$25,000 minimum to open

Options for Organizing Philanthropy (con't)

- Field of Interest (FOI) Funds
 - ❑ Multiple donors supporting defined cause
 - ❑ Managed by community foundation staff
 - ❑ Examples:
 - Asset Building Fund – Supports financial skill building for families in our foreclosure pilot program
 - East Bay Fund for Artists - Supports commissioning of new performance art by local artists
- Agency Fund
 - ❑ Usually endowment building for nonprofits

Private Foundation Services

- Philanthropic Advice and Services
 - ❑ Expertise establishing grantmaking programs, identifying effective nonprofits, evaluating impact
 - ❑ Proposal-based projects
 - ❑ Leverage DAFs for 5% payout requirement
 - ❑ Leverage FOI funds/collaborations - network with other foundations, education on key community issues

THANK YOU!

For More Information
www.eastbaycf.org

Giles Miller, Director of Development
gmliller@eastbaycf.org
(510) 836-3223

Federal Tax Law: Overview of Private Foundation Rules

If a charity cannot qualify as a public charity under any provision in Section 509 of the Internal Revenue Code (which describes specific types of organizations like schools, churches, and hospitals; broadly publicly or governmentally supported organizations; organizations which earn income from their charitable activities from many sources; and supporting organizations to publicly-supported charities), it is classified as a private foundation. Family foundations and corporate foundations are typically private foundations, and some split-interest trusts are treated as if they were private foundations for purposes of some of the rules discussed below.¹ In addition to the legal framework applicable to all charities, private foundations must comply with the technical rules of Chapter 42 of the Code. What follows is a simplified summary of these rules, intended to alert the non-specialist to potential problems. This outline is not a substitute for careful analysis of Chapter 42 and the accompanying regulations.

1. **Disqualified Persons.** The disqualified person concept is fundamental to the private foundation regulatory framework. Section 4946 defines a disqualified person² as:
 - a. A substantial contributor, as defined in Section 507(d)(2)
 - b. A foundation manager -- that is, an officer, director, or trustee, or anyone having equivalent responsibilities or powers; also, with respect to any act or omission, any employee of the foundation who has authority or responsibility regarding that act or omission.
 - c. One who owns more than 20% of an entity which is a substantial contributor.
 - d. A family member of anyone described in any of the preceding three categories. "Family member" includes the person's spouse, ancestors,

¹ I.R.C. § 4947.

² A § 501(c)(3) organization is excluded from the definition of a disqualified person. However, for purposes of § 4943, another private foundation is treated as a disqualified person if (a) it is effectively controlled by the same persons who control the foundation in question, or (b) it receives substantially all of its funding from the same donors (or family members of the donors) who funded the first foundation.

children, grandchildren, great-grandchildren, and the spouses of children, grandchildren, and great-grandchildren.

- e. A corporation, partnership, or trust in which persons described in the preceding four categories own more than 35% of the total combined voting power, profits interest, or beneficial interest, respectively.
 - f. A government official as defined in Section 4946(c) is a disqualified person for purposes of the self-dealing rules.
2. Self-Dealing Transactions. Section 4941(d)(1) defines self-dealing transactions, while Section 4941(d)(2) lists certain exceptions to those rules. Detailed regulations amplify the statutory provisions.
- a. Definition. “Self-dealing” includes the following transactions, whether direct or indirect:
 - (1) Sale, exchange, or lease of property between a private foundation and a disqualified person.
 - (a) A disqualified person may, of course, provide the free use of property to a private foundation.
 - (b) An otherwise permissible transfer of property from a disqualified person to a private foundation will be treated as self-dealing if the property is subject to a mortgage which the foundation assumes, or if the property is subject to a mortgage which a disqualified person placed on the property within the 10-year period ending on the date of the transfer.
 - (2) Lending money, or any other extension of credit, between a private foundation and a disqualified person. A disqualified person may loan money to a private foundation if the loan is without interest or other charge and the proceeds are used exclusively for Section 501(c)(3) purposes.
 - (3) Furnishing of goods, services, or facilities between a private foundation and a disqualified person, except:
 - (a) If a disqualified person provides the goods, services, or facilities without charge and the foundation uses them exclusively for Section 501(c)(3) purposes, the transaction is not self-dealing.

- (b) The private foundation may furnish goods, services, or facilities to a disqualified person if it is on a basis no more favorable than that on which they are provided to the general public.
 - (4) Payment of compensation, or payment or reimbursement of expenses, by a private foundation to a disqualified person, unless the compensation is for personal services which are reasonable and necessary to carrying out the foundation's exempt purposes and the amount of compensation (or payment or reimbursement) is reasonable and not excessive. This exception does not apply to payments to government officials, who are subject to separate rules.
 - (5) Transfer to, or use by or for the benefit of, a disqualified person of the income or assets of a private foundation.
 - (6) Agreement by a private foundation to make any payment of money or other property to a government official, other than in the narrow circumstances defined in Sections 4941(d)(1)(F) and 4941(d)(2)(G).
 - b. **Exception for Certain Corporate Transactions.** Transactions between a private foundation and a corporate disqualified person pursuant to a liquidation, merger, redemption, or similar corporate reorganization are not self-dealing if all of the securities of the same class as that held by the foundation are subject to the same terms, and those terms provide that the foundation shall receive no less than fair market value.
 - c. **Penalties for Self-Dealing.** Unfortunately, self-dealing is often discovered after the fact. Prompt correction is essential in order to reduce the significant penalties that will otherwise be assessed. The penalty structure of Section 4941 consists of two tiers: one penalty arising from the fact of self-dealing, and another more severe penalty following if the self-dealing has not been corrected within the statutory correction period. The penalties are imposed on the self-dealer and, in some circumstances, on foundation managers.
3. **Mandatory Distributions.** Section 4942 requires a private foundation to distribute each year, for charitable purposes, an amount equivalent to 5% of the fair market value of the foundation's non-charitable assets.
- a. **Qualifying Distributions.** The following distributions may be counted toward the minimum payout requirement:

- (1) Amounts (including reasonable and necessary administrative expenses) paid to accomplish one or more exempt purposes;
- (2) Amounts paid to acquire an asset used directly in carrying out an exempt purpose; or
- (3) Amounts set aside for specific future charitable projects to be funded within a 60-month period;³

except that distributions to other private foundations (other than operating foundations), commonly controlled entities, and certain supporting organization public charities cannot be counted.⁴

- b. **Excess Qualifying Distributions.** A private foundation may carry forward, for up to five years, any qualifying distributions above the minimum required amount and apply the excess distributions to reduce the subsequent years' distribution requirements.
4. **Excess Business Holdings.** Section 4943 provides that a private foundation and its disqualified persons together may own no more than 20% of the voting or ownership interest in a business enterprise.
- a. **Circumstances Where the Excess Business Holdings Rule Does Not Apply.**
 - (1) The foundation and its disqualified persons may own up to 35% of the business enterprise if a third party effectively controls the management and policies of the enterprise.
 - (2) The excess business holdings rule does not apply at all if the foundation, together with all other private foundations under common control or primarily funded by the first foundation's disqualified persons, owns less than 2% of the voting stock and not more than 2% of the value of all outstanding shares of all classes of stock. This “2% de minimis rule” is an important planning tool.
 - (3) If a split-interest trust is described in Section 4947(b)(3), it is not subject to Section 4943 and, thus, does not have to consider the ban on excess business holdings.

³ Qualifying set-asides are discussed in I.R.C. § 4942(g)(2) and Treas. Reg. § 53.4942(a)-3(b)(1).

⁴ I.R.C. § 4942(g)(1) and 4942(g)(4)

- (4) A business which is functionally related to the exempt purposes of the private foundation is not considered a business enterprise for purposes of Section 4943. Therefore, it is not subject to the excess business holdings ban.
 - (5) If at least 95% of the gross income of a trade or business is derived from passive sources, then it is not considered a business enterprise and the excess business holdings ban does not apply.
- b. Correction; Penalties. A private foundation whose holdings exceed the permitted percentage must promptly reduce its holdings to permissible levels. If it does not comply in a timely manner, excise taxes are imposed.
- (1) If the excess business holdings problem arises other than from a purchase by the foundation or a disqualified person, there is a five-year period in which to dispose of the excess.
 - (2) The IRS may grant an additional five years in the case of an unusually large gift or bequest where the foundation establishes that the facts and circumstances warrant that additional time.
5. Jeopardizing Investments. If a private foundation invests in a manner which is likely to jeopardize its ability to carry out its exempt purposes, the foundation is taxed at 10% of the amount so invested for each year (or partial year) in the taxable period. A foundation manager who participated in making that investment, knowing that it could jeopardize the foundation, is also taxed 10% unless the manager's participation was not willful and was due to reasonable cause. If the investment is not "removed from jeopardy" within the taxable period, additional taxes are imposed.
- a. Program-Related Investments Are Not Jeopardizing Investments. A program-related investment is an investment whose primary purpose is to accomplish one or more charitable purposes, and no significant purpose is the production of income or the appreciation of property. See Section 4944(c) and accompanying Regulations.
 - b. No Investment Is Automatically Improper. Although the statute appears forbidding, in practice it rarely presents problems for foundations. There are remarkable similarities between the Regulations and the Restatement

3rd's prudent investor rule.⁵ Under both schemes, no investment is per se improper.

- c. **Where the Rule Does Not Apply.** The rule applies only to assets which the foundation purchases, not to assets which are donated to it by gift or bequest or which the foundation receives solely as a result of a Section 368(a) corporate reorganization.⁶ Also, Section 4944 does not apply to split-interest trusts described in Section 4947(b)(3).
6. **Taxable Expenditures.** Section 4945 imposes penalties on private foundations which make taxable expenditures and on any manager who, knowingly and without reasonable cause, participates in the making of a taxable expenditure. If the taxable expenditure is not reversed, additional penalties are imposed.
- a. **Definitions.** Taxable expenditures include lobbying within Section 4945(e); attempting to influence the outcome of any specific public election or conducting or funding a voter registration drive, except as provided in Section 4945(f); grants to individuals for travel, study, or similar purposes unless the grant satisfies Section 4945(g); grants to organizations which are not public charities and grants to certain supporting organization public charities, unless the foundation exercises expenditure responsibility over the grant as described in Section 4945(h); and expenditures other than for charitable purposes. Fortunately, the cited statutes and the accompanying regulations allow a significant amount of flexibility.
 - b. **Grants to Individuals.** Under Section 4945(g), private foundations may make grants directly to individuals for travel, study, or similar purposes only where the IRS has previously approved the procedures by which individual grantees are selected. The IRS requires objective and non-discriminatory grant selection procedures in order to rule favorably. This prior approval is not necessary for public charity grants to individuals.
 - c. **Expenditure Responsibility.** Private foundations may fund the charitable activities of organizations which are neither public charities nor exempt operating foundations, so long as the private foundation exercises expenditure responsibility over the grant.⁷ Expenditure responsibility is

⁵ Compare Treas. Reg. § 53.4944-1(a)(2) with Rest. 3rd, Trusts (Prudent Investor Rule), §227.

⁶ Treas. Reg. § 53.4944-1(a)(2)(ii).

⁷ Treas. Reg. § 53.4945-5(b).

also required for grants to certain supporting organization public charities. This oversight requirement — consisting of a pre-grant inquiry, a written grant agreement containing specific terms and conditions listed in the Regulations, and reporting the grant to the IRS on Form 990-PF — is less burdensome than many foundations realize. With the exception of the Form 990-PF reporting requirement, many private foundations already satisfy these criteria in their normal grant documentation.

- d. **Foreign Public Charity Equivalence Determination.** Private foundations may make grants directly to foreign organizations for charitable purposes, either by exercising expenditure responsibility or by determining that the foreign organization is the equivalent of a public charity.⁸
 - e. **Lobbying.** Unlike public charities, private foundations are generally barred from conducting, or paying for, any type of lobbying activity. Many advocacy efforts fall outside the definition of lobbying contained in the Regulations, and private foundations may fund such efforts. Private foundations may grant funds to a public charity for a specific project that includes some lobbying, if the amount of the grant is less than the non-lobbying components of the project.⁹
7. **Excise Tax on Net Investment Income.** Section 4940 imposes an excise tax on the net investment income of private foundations. The amount of that tax is currently 2%, but in certain circumstances the tax may be reduced to 1%.¹⁰

Any tax advice contained in this memo is not intended to be used, and cannot be used, for the purpose of avoiding penalties that may be imposed under federal tax law. A taxpayer may rely on our advice to avoid penalties only if the advice is reflected in a more formal tax opinion that conforms to IRS standards. Please contact us if you would like to discuss the preparation of a legal opinion that conforms to these rules.

⁸ The public charity equivalence determination process, which is discussed at Treas. Reg. § 53.4945-6(c)(2)(ii), was made much easier by the IRS in Rev. Proc. 92-94, 1992-2 C.B. 145. See John A. Edie, *Beyond Our Borders* (Council on Foundations, 1994) for a detailed discussion of the nuts and bolts of cross-border philanthropy.

⁹ For a more detailed discussion of private foundations and lobbying, see Colvin, “A Case Study in Using Private Foundation Funds to Educate Voters,” 6 *Journal of Taxation of Exempt Organizations* 243, 276 (May/June 1995).

¹⁰ I.R.C. § 4940(e).

A Basic Guide to Donor Advised Funds

Stephanie L. Petit
January 2010

This overview of donor advised funds is provided for educational purposes only, and not as legal advice; it is not a comprehensive treatment of the rules relating to donor advised funds, their donors, their advisors, or their sponsoring organizations. Prospective sponsoring organizations should consult legal counsel before implementing a donor advised fund program.

A donor advised fund is a separate fund (though not a separate legal entity) created and held at a public charity. The public charity holder of the donor advised fund is called a sponsoring organization. In practice, the sponsoring organization is often a local community foundation or the charitable affiliate of a financial services provider. A donor (who could be an individual, a company, or a private foundation) contributes funds or assets to the sponsoring organization, which holds them in the donor advised fund. The donor can take a public charity deduction (or, in the case of a private foundation, can count the contribution as a qualifying distribution) in the year in which he, she, or it makes the contribution, because the donated assets upon donation become the property of the sponsoring organization. The donor, or someone appointed by the donor (such as a friend or relative, corporate officer, or governing body, for example), retains the right to advise or recommend charitable grants from the donor advised fund from time to time. Usually, the donor can name the fund (“The Donor Family Fund” or “The Donor Company Fund”) and even recommend how those funds will be invested. For its service, the sponsoring organization typically deducts some small percentage of the fund assets or contributions received on a quarterly or annual basis.

Discretion and control. A donor to a donor advised fund can take a deduction (or qualifying distribution) in the year in which he, she, or it makes a gift to the sponsoring organization, regardless of when the funds or assets are granted out, because the sponsoring organization has “discretion and control” over those assets. In other words, the sponsoring organization, which is the legal owner of the funds, need not heed the advice of the donor. In practice, however, the sponsoring organization will generally do so where possible.

Eligible grantees. Gifts from a donor advised fund *can* be made to most public charities, their foreign equivalents, to another fund of the sponsoring organization itself, or another donor advised fund. Gifts from a donor advised fund can also be made to any other grantee for charitable purposes, *provided* that the sponsoring organization exercises expenditure responsibility over the grants. A donor advised fund cannot make grants to individuals.¹ As a

¹ A fund meeting certain requirements described in Section 4966(d)(2)(B)(ii) can make grants to individuals.

practical matter, some sponsoring organizations are willing to exercise expenditure responsibility and perform foreign public charity equivalency analyses, and some are not. A donor wishing to make overseas grants, for example, should specifically discuss this intention with the potential sponsoring organization before setting up the fund.

No benefit to donors. Section 4967 essentially prohibits a grant from a donor advised fund that “results in” the donor, advisor (if different), certain members of their family, and certain entities related to them, “receiving, directly or indirectly, a more than incidental benefit as a result of such distribution”. Section 4958 heavily taxes any grant, loan, compensation or other similar payment from a donor advised fund to a donor advised fund’s donors, advisors, family members, and certain entities controlled by them. Section 4958 also heavily taxes excessive payments to the investment advisors of sponsoring organizations, their families, and certain entities controlled by them.

As of this writing, the IRS has issued no guidance (including regulations) on either of these rules. Most sponsoring organizations of donor advised funds, however, require an advisor to attest that any grant being advised will not result in a benefit to the donor, advisor, or related persons or entities; that the grant will not satisfy a pledge made by the advisor; and that the grant funds will not be used to pay, even in part, for anything for which the donor or advisor would receive a return benefit.

Size of Funds, Fees, and Grants. Each sponsoring organization creates its own policy for the minimum amount needed to start a donor advised fund. We have seen sponsoring organizations willing to open one for as little as \$5,000 and others requiring as much as \$100,000. Many sponsoring organizations require approximately \$10,000 to \$25,000.

Similarly, each sponsoring organization will differ in the size of grants it will make. Some will make grants as small as \$100. Fee structures also vary greatly, from one-time charges, to recurring annual or quarterly charges. Many sponsoring organizations will reduce administrative fees for larger fund balances, and many charge extra fees for more complicated grants, such as expenditure responsibility grants.

Traps for the unwary. A donor who creates a donor advised fund must understand that the donor gives up legal control and ownership of the assets once given to the sponsoring organization. Gifts from the fund to charities the donor (or advisor, if different) suggests, may be described as “made possible by” the donor, but the donor has not made a gift to, and has no direct relationship with, the ultimate grantee, and no contrary representations should be made by the donor or the grant recipient. Direct attempts by donors to exercise control over how grant funds are spent by the grantee of the sponsoring organization could make the grants appear earmarked directly by the donor to the ultimate grantee, undermining the donor advised fund’s status and resulting in legal outcomes different than the parties intended.

In addition, as of this writing, the IRS has yet to issue regulations on the donor advised fund statutes discussed. Therefore, a donor could take a position arguably permissible under existing law (for example, by advising a grant that yields a very small but tangible benefit

to him or her) that future regulations could ultimately prohibit. Accordingly, during this period of uncertainty, many counselors are giving their clients very conservative advice on what gifts may be made from donor advised funds.

Advantages over direct giving. A donor wishing to make a charitable gift before year end can make a gift to a donor advised fund, take a deduction or qualifying distribution in that year (individual tax circumstances permitting), and decide later how the funds should be spent. (By contrast, a direct gift requires a real-time decision about what charitable purpose and donee to fund.) The sponsoring organization of a donor advised fund can, from funds given by and deductible to the donor, make charitable grants to foreign entities, nonprofits that are not Section 501(c)(3) tax-exempt, and even for-profits, provided the sponsoring organization is willing to exercise expenditure responsibility over these grants. (By contrast, an individual generally cannot take a charitable deduction for direct gifts to any of these.)

Disadvantages over direct giving. The chief disadvantage of a donor advised fund is that the donor legally has no control over assets once contributed; the sponsoring organization could choose not to honor the recommendation of the fund advisor. (By contrast, in a direct gift, the donor retains control over the assets until the gift is made.) Also, a sponsoring organization deducts a small percentage of the fund assets or contribution as a fee; a direct gift would not carry this administrative expense.

Advantages over a private foundation. The cost, time, and effort required to set up and maintain a donor advised fund are a fraction of that required to set up and maintain a private foundation. Non-cash gifts to a donor advised fund are eligible to receive the more favorable public charity deduction, versus the sometimes less-favorable private foundation deduction.

Disadvantages over a private foundation. Through its selection of private foundation directors, an individual can retain, if he or she wishes, near-total control over the assets held by a private foundation. By contrast, an individual loses legal control of any assets donated to a donor advised fund.

Sponsoring organizations. As noted above, sponsoring organizations are faced with a number of policy decisions about how they will operate with respect to any donor advised funds they accept and disburse. Such policies vary, reflecting the sponsor's business model, its donor relations culture, the size and scope of its donor advised fund program, and its tolerance for risk (especially while regulations are still pending), among other things. The rules applicable to sponsoring organizations and their operations are beyond the scope of this overview, although we are happy to provide legal advice as well as data on standards and practices among sponsors on request.

Summary. Donor advised funds can be an effective philanthropic vehicle for an individual or company beginning philanthropy, as they do not require a significant investment of time, money, or effort, and some sponsoring organizations are even willing to help educate their donors about philanthropy and assist them in clarifying their philanthropic objectives. At the

same time, experienced, sophisticated philanthropists also use donor advised funds, sometimes creating very large ones, as sponsoring organizations can provide a buffer between the donor and the ultimate grantee or even anonymity. For sponsoring organizations, providing donor advised funds can be another useful tool for serving their donors' philanthropic needs. Even though sponsoring organizations typically honor the donor's recommendation where possible, some donors may not be comfortable with the idea of not having legal control of assets contributed.

Any tax advice contained in this handout was not intended to be used, and cannot be used, for the purpose of avoiding penalties that may be imposed under federal tax law. A taxpayer may rely on our advice to avoid penalties only if the advice is reflected in a more formal tax opinion that conforms to IRS standards. Please contact us if you would like to discuss the preparation of a legal opinion hat conforms to these rules.