BLB&B Advisors, LLC
FINANCIAL GUIDANCE SINCE 1964

MONEY *notes*

National Philanthropy Day (NPD) is November 15, 2023. This special day was first officially recognized in 1986 by President Reagan as a time to celebrate the critically important work done every day by philanthropic organizations and individuals in our community and around the United States. In honor of NPD, this month's BLBB Money Note focuses on two philanthropic giving options you may want to consider to formalize your own philanthropic goals.

How can I create a philanthropic legacy?

If you are like most people, you donate money and also volunteer your time and expertise to one or more local non-profit entities. Over the years, and as your income level has risen, you may have also increased the amount of money you donate each year. Perhaps you are now at a point where you would like to be more purposeful and strategic around your charitable giving. At the same time, you may also be at a point financially where you would like to more deliberately use the charitable gift tax deduction to help offset your federal tax burden. Finally, and as part of your estate planning and personal goals, you may wish to create a philanthropic legacy that exists for future generations of your family.

This article focuses on two popular options: (1) a private foundation; and (2) a donor advised fund (DAF).

What is a Private Foundation and a Donor Advised Fund and how do they differ?

A private foundation is a stand-alone, charitable organization (a tax-exempt legal entity governed by its own set of bylaws, articles of incorporation, and a governing board of directors) often created by a family, individual, or corporation. Among other things, the directors of a private foundation have the responsibility of managing the foundation's assets and making grants to other nonprofit organizations.

A DAF is a giving account that is under the legal control of a public charity (called a sponsoring organization) that is sometimes connected to a financial institution or community foundation. The DAF donor donates assets to their DAF and then recommends various grants be made from it to charitable entities of their choice.

Clients often ask us which of these giving vehicles is "better." There is no one-size-fits-all. Each of these charitable vehicles has its place in philanthropic giving; the answer to this question really depends on what you want out of your giving, who you want to involve, how long you wish to continue giving to charity, and what portion of your assets you wish to devote to philanthropic efforts.

The basic differences between private foundations and DAFs fall into three general categories: taxation, control, and cost.

Tax Differences

Regardless of whether you donate to a private foundation or a DAF, you will receive a tax deduction at the time of the donation. You will not, however, receive another deduction when grants are subsequently made to charities from the foundation or DAF account. When you gift to a DAF, you receive a tax deduction equal to the fair market value of the donated assets at the time you make the gift. When you gift to a private foundation, you receive a tax deduction equal to the asset's cost basis or its fair market value (depending on the asset type).

The income tax deduction limit for assets contributed to a DAF is up to 60% of adjusted gross income for cash contributions and up to 30% for appreciated assets. The income tax deduction limit for assets contributed to a private foundation is much less: up to 30% of adjusted gross income for cash contributions and up to 20% for appreciated assets. While both a DAF and a private foundation are tax exempt entities whose assets may be invested for growth potential, the funds in a DAF can earn investment income without being taxed, whereas a private foundation must pay an annual 1.39% tax on its net investment income. It should also be noted that funds gifted to both types of vehicles are irrevocable gifts.

Control Differences

As a standalone legal entity, a private foundation – like any other nonprofit organization – is governed and controlled by its board of directors. All legal and financial control of a foundation, along with all charitable grant-making decisions, rests with its board. This is quite different from a DAF, which is a giving fund that is legally controlled by another nonprofit (or sponsoring) organization. You, as the person who created and funded the DAF, can "recommend" charitable grants to other public charities, but the sponsoring organization has the authority to either accept or reject these recommendations. In most cases, the DAF donor's grant recommendations are quickly approved and made. Usually, when a grant is delayed or not approved by the sponsoring organization this is due to the recipient organization being in violation of various tax rules and regulations. For example, if the recommended grant recipient is not a registered 501(c)(3) charity, the grant request will be denied. Similarly, a grant may be denied if it is to be used to purchase something of value for the donor, such as tickets to a fundraising event.

Another key control difference centers on what happens after the original donor dies. A private foundation can exist in perpetuity with successive generations (or even outside board members) able to take over control of the philanthropic legacy of its founders. A DAF's succession options, however, are more limited and can vary depending on the sponsoring organization's policies. Many sponsoring organizations allow the DAF donor to appoint one successor beneficiary after which the family's philanthropic legacy ends.

With legal and financial control, private foundations must also comply with more federal regulations than DAFs. One of the most substantial differences between the two vehicles is that private foundations are required by law to meet an annual 5% minimum distribution based on the previous year's net average value of its charitable assets. Private foundations that do not distribute a minimum of 5% of their net average assets for charitable purposes each year risk penalties and potential termination. A DAF has no charitable distribution requirements.

Finally, as a more regulated entity, a private foundation may not distribute its funds anonymously. Although a private foundation may ask the grantee organization to keep its name out of public marketing materials, all private foundations are required to file a publicly-available annual IRS Form 990-PF that lists all their assets, contributors, grantees, and corresponding grant amounts. The charitable gifts by a DAF donor, on the other hand, may be made anonymously because a DAF account has no required state or federal filings.

<u>Cost to Administer</u>

For some, the ability to more directly control your charitable entity would weigh heavily in favor of creating a private foundation; yet, such control comes with a much heftier price tag to administer. These up-front and on-going expenses related to the creation and administration of a private foundation is an important consideration that substantially favors a DAF.

Creating a Private Foundation as a separate tax-exempt legal entity often entails hiring a lawyer to incorporate the entity and create the governing documents. Once established, you must create a governing board of trustees (and a process for how grant and other decisions will be made). In addition, running a foundation may include the following annual expenses and time commitment: oversight and management of the assets (and often investment manager fees); creation and oversight of a grant application, a decision process, and reporting process; verification of legal compliance by organizations that you fund; management and distribution of the grant funds (and often bookkeeper or accounting fees); and accountant fees for tax filings and forms. Setting up and managing a DAF at a sponsoring organization does not require any of these costs or extended time commitment.

As you can see, advance planning for the creation and implementation of your philanthropic legacy is of paramount importance. This is time well spent because it can lead to the creation of the “right” charitable vehicle for you. The next step should include a discussion with your BLBB financial advisor, your tax advisor, and potentially even BLBB’s philanthropic advisor, Nicole Tell, about how your financial and philanthropic goals best align with these (or other) charitable vehicles.

BLBB Charitable Update

This Thanksgiving, the BLBB team will create meal bags for Garden of Health in Lansdale. Garden of Health's mission is to provide healthy, safe food (free of the top eight allergens) for low-income families, including those with dietary restrictions, in Montgomery and Bucks Counties.

BLBB Charitable has also been especially busy partnering with many organizations in the region, including celebrating the opening of three new local environmental education centers that it helped to fund.

- **Wissahickon Trails** completed their renovation of the historic Four Mills Barn that operates as both the organization's headquarters and is now a flood resilient community and environmental education space. BLBB Charitable has supported Wissahickon Trails' environmental education programs for years.
- **Whitemarsh Foundation** recently completed the new ***BLBB Education Pavilion*** that enables the Foundation to substantially increase its educational programming.
- **Pennypack Ecological Restoration Trust** just unveiled its new ***BLBB Charitable Field Station***. This Field Station will serve as a hub for educational activities, workshops, and research, providing a valuable resource for enhancing understanding and appreciation of the natural world in the Pennypack Watershed.

L to R: Robb Parlanti, Ed Barnes, Clif Haugen, John Lawton, Laura Brewer, Dean Karrash, Brian Gallagher, Brianna Barnes March, Nick Bucci, Bob Flood, Chris Perry

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