

KEY TAKEAWAYS

# Charitable Giving Tax Benefits 101: **FAST FACTS**



**U**nderstanding the differences between private foundations, donor-advised funds (DAFs), and fiscal sponsorships—and how each can be used to maximize tax-efficient charitable giving—is essential for donors and their advisors. **Foundation Source’s Chief Legal Officer Jeffrey D. Haskell** recently presented a webinar covering the fast facts on charitable giving vehicles and their tax benefits. These are the key takeaways from that presentation.



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# Know Your Giving Vehicles

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Each of the three popular charitable giving vehicles—private foundations, DAFs and fiscal sponsorships—has a distinct structure and purpose:

## Private Foundation:

- An independent 501(c)(3) legal entity with its own tax ID, formed as a trust or corporation.
- Must apply to the IRS for exempt status within 27 months of formation.
- The donor can serve on the board and maintain control—either alone (depending on state minimums) or with trusted family, friends, or colleagues.

## Donor-Advised Fund (DAF):

- A giving account held within a sponsoring public charity. Donors receive an immediate tax deduction and then recommend grants over time.
- The sponsoring organization—not the donor—legally controls the assets, though recommendations are typically followed.

## Fiscal Sponsorship:

- An arrangement between a public charity (the sponsor) and a non-501(c)(3) organization or project seeking to raise charitable funds.
- Donors give to a restricted fund at the sponsor charity. The sponsor retains discretion over how funds are ultimately applied to ensure tax deductibility.
- It is typically used when a charitable project—domestic or foreign—lacks its own 501(c)(3) status.
- This arrangement arises out of necessity rather than strategic preference.

# Control Is the Defining Feature of Private Foundations

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Private foundations offer flexibility, authority, and control. Unlike a DAF or fiscal sponsorship, a foundation donor retains direct authority over:

- How charitable assets are invested.
- When, how, and to whom grants are distributed.
- Whether to run their own direct charitable programs (known as direct charitable activities, or DCAs) in addition to making grants.

Foundation board members and staff may also receive compensation for certain work or services provided to the foundation (if it's reasonable and necessary) and reimbursement for foundation-related expenses—an option not available with DAFs or fiscal sponsorships.

## Tax Deductibility: AGI Limits Matter—But Less Than You Might Think

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When comparing giving vehicles, discussions often focus on the AGI percentage caps for charitable deductions. Public charities (including DAFs and fiscal sponsors) generally offer higher AGI caps than private foundations. However, in practice:

- It is relatively rare for a donor's contributions to exceed the applicable AGI limit in a given year.
- Even if a donor exceeds the limit, excess deductions can be carried forward for up to five years.
- Donors can also “stack” contributions—giving up to the allowable limit to a private foundation and then contributing additional amounts to a public charity to take advantage of the higher caps.

All three vehicles provide an immediate tax deduction upon contribution, and all contributions are irrevocable.

## Grantmaking Flexibility Varies Significantly

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Private foundations offer the broadest grantmaking capabilities, including:

- **Grants to individuals** (e.g., scholarships, hardship grants, emergency assistance), with the foundation designing and controlling the eligibility criteria and selection process, provided that applicable IRS rules are followed.
- **Grants to foreign organizations**, provided that special procedures are followed.
- **Grants to for-profit entities**, provided the grant serves a legitimate charitable purpose and appropriate oversight is exercised.
- **Operation of direct charitable programs (DCAs)**, such as running a soup kitchen or publishing educational materials.

DAFs are typically used to make straightforward grants to U.S. 501(c)(3) charities. While some sponsoring organizations permit grants to foreign organizations or private foundations, many have internal policies against such distributions due to the additional due diligence required. Grants to individuals from DAF accounts are not permitted, though a DAF can grant to a public charity that runs its own individual assistance programs.

Fiscal sponsorships are used under specific circumstances—when a non-501(c)(3) organization seeks to receive tax-deductible donations for a charitable project. Funds typically pass through quickly, provided that the sponsoring charity is satisfied with the sponsored project's execution of the charitable program. However, earmarking of grants for re-granting to a specific named organization is prohibited.

## Guarantee of Funds Reaching The Intended Recipient

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An important but often overlooked consideration: only direct out-of-pocket giving and private foundations guarantee that funds reach the intended recipient. DAFs and fiscal sponsors are generally very faithful in following donor wishes—but they are not legally obligated to do so. Donors who need assurance that a specific organization or individual will receive the funds should factor this into their vehicle selection.

## International Grantmaking Requires Proper Procedures

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When a private foundation grants to a foreign organization, it must follow one of two IRS-compliant paths:

### **Expenditure Responsibility (ER):**

- A multi-step process involving a pre-grant inquiry, a written grant agreement, separate bookkeeping by the grantee, annual progress reports, and a special disclosure on the foundation's 990-PF tax return.
- IRS compliance here is especially rigid—even a single missed step can result in a 20% penalty on the grant, as though ER was never exercised at all.
- Foundation Source strongly encourages working with advisors or outside counsel when exercising ER.

### **Equivalency Determination:**

- The foundation (or a qualified tax practitioner—attorney, CPA, or enrolled agent) determines in good faith that the foreign grantee would qualify as a U.S. public charity.
- Under the “special rule,” a written opinion from a qualified practitioner is accorded special credence by the IRS. Such opinions must generally be refreshed every two years.
- This approach avoids the mandatory restrictions on fund use that come with ER—but it may not always be achievable if the foreign organization doesn't meet U.S. public charity standards.

## Direct Charitable Activities: Foundations Can Do More Than Grant

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Like public charities, private foundations can run their own charitable programs—known as direct charitable activities (DCAs). Examples include:

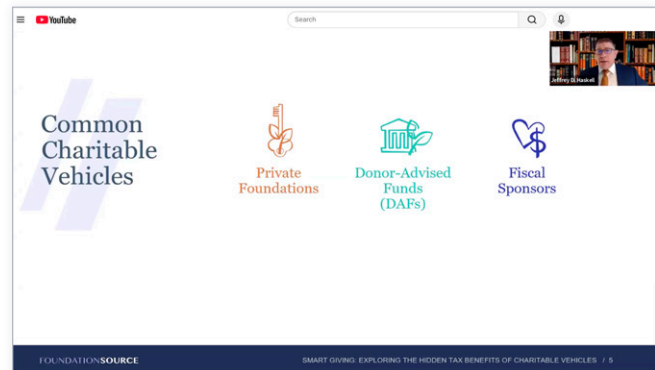
- Operating a soup kitchen or food pantry.
- Publishing educational literature or conducting research.
- Running job training programs for disadvantaged youth.

DCA expenses count toward the foundation’s annual 5% payout requirement, just like grants. Reporting DCAs clearly on the foundation’s tax return is important for transparency—without proper explanation, significant operational expenses might appear inconsistent with charitable purposes. As always, self-dealing and private benefit rules apply and must be considered before undertaking any direct charitable activity.

## Action Steps

- Assess whether a client’s charitable goals are better served by a private foundation, a DAF, a fiscal sponsorship arrangement, or a combination of vehicles.
- For clients with private foundations making grants to entities (domestic or foreign) other than U.S. public-charities, ensure that proper ER or equivalency determination procedures are in place before any grant is made.
- Remind clients that foundation grantmaking and DCA activities should be clearly documented on the 990-PF to avoid the appearance of misaligned charitable purposes.
- Consider whether any current or planned giving activities could benefit from the control and flexibility of a private foundation—particularly for clients who want to make grants to individuals or run their own charitable programs.

To learn more about these key takeaways and other important insights, [check out the full conversation here.](#)



## HAVE A QUESTION?

Call 800.839.0054 or send us an email at [info@foundationsource.com](mailto:info@foundationsource.com).

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