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KEY TAKEAWAYS

SMART GIVING: Exploring The Hidden Tax Benefits of Charitable Vehicles

Philanthropists often give through charitable vehicles such as private foundations, donor-advised funds (DAFs), or fiscal sponsors to achieve both tax efficiency and charitable impact. In a recent Foundation Source webinar, our **Chief Legal Officer Jeffrey Haskell** and **Deputy Legal Officer Jennifer Bruckman-Gorak** shared valuable insights into these vehicles and how they can be structured for tax-advantaged giving. Here are the key takeaways from their presentation.

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1. Private foundations, donor-advised funds, and fiscal sponsorships offer distinct structures and tax benefits.

Each of these giving vehicles offers tax-deductible giving, but they differ in structure and control.

A ***private foundation*** is a standalone legal entity with its own tax ID and IRS-recognized 501(c)(3) status. The donor and their family can serve on the board, direct investments, and oversee grantmaking. A private foundation also offers a lot of flexibility and donor control. Its donor can determine investment strategy, select grantees (including individuals and international organizations), and even operate direct charitable activities (DCAs).

A ***donor-advised fund (DAF)*** is a giving account housed within a public charity that serves as the sponsoring organization. Donors receive an immediate tax deduction and can recommend—but not direct—how funds are granted and invested. They allow donors to receive an immediate tax deduction for their charitable contribution and then recommend grants from the fund over time. The sponsoring charity that houses the DAF account will charge fees for administration, record keeping, and philanthropic services, which will pull from those accounts.

A ***fiscal sponsorship*** is an arrangement between a public charity, the sponsor, and another domestic or international organization without US public charity tax status (i.e. the “project”). It can provide a useful workaround when donors want to support charitable work that otherwise would not qualify for deductible contributions, though the sponsoring charity retains control of the funds raised.

2. Private foundations and DAFs provide opportunities for tax-advantaged asset growth.

Tax-deferred growth is generally applicable only with foundations and DAFs, since assets contributed to these vehicles can be invested and appreciated over time. By contrast, fiscal sponsorships tend to be short-term, pass-through arrangements.

Donors can also combine vehicles strategically by stacking donations. For example, they may contribute up to the allowable limits to a private foundation and then give additional funds to a DAF or public charity to take advantage of higher adjusted gross income (AGI) caps applicable to public charities. Excess contributions can be carried forward for up to five years, offering flexibility to optimize tax deductions across multiple vehicles.

All three options, including fiscal sponsorship, provide a donor with an immediate tax deduction and contributions to all of these vehicles are irrevocable.

3. Private foundations uniquely allow tax-deductible grants to individuals (GTIs).

Of all three vehicles, only a private foundation may make grants directly to individuals (versus a charity) and still provide the donor with a tax deduction. These granting-to-individuals (GTI) programs must serve a charitable purpose – such as alleviating hardship, advancing education, or providing emergency relief – and must exclude any disqualified persons (insiders or family members of substantial contributors). To maintain compliance, foundations must establish clear eligibility criteria and document their selection processes to ensure fairness and nondiscrimination. Grants should meet only basic needs and be based on objective evaluations of need.

4. Advance IRS approval is required for certain GTIs.

When a grant involves travel, study, or similar activities, a private foundation must obtain advance approval from the IRS to avoid a tax penalty. These programs typically include scholarships, fellowships, and certain prizes or awards. Foundations may request approval during their initial exemption process (Form 1023) or later via Form 8940. Once the request is filed, a "45-day rule" allows foundations to begin making grants after 45 days even if the IRS has not yet issued formal approval. Regardless of timing, strong documentation and post-grant reporting are essential to ensure that funds are used as intended.

5. Expenditure responsibility ensures charitable use of grants to non-charitable entities.

When making grants to organizations that are not recognized US public charities, private foundations must exercise expenditure responsibility—a set of IRS-mandated procedures designed to confirm that funds are used solely for charitable purposes. This process involves conducting a pre-grant inquiry, executing a written grant agreement with specific terms, obtaining annual and final reports from the grantee, and reporting the grant on the foundation's 990-PF. Noncompliance with any step can result in the IRS treating the grant as a taxable expenditure. Alternatively, a foundation can perform an equivalency determination to establish that the grantee meets the standards of a US public charity, though this method can be time-consuming and complex.

6. Direct charitable activities (DCAs) enable foundations to operate their own programs.

Like public charities, private foundations can carry out their own charitable programs – known as direct charitable activities (DCAs)—in addition to funding other organizations. Examples include publishing educational materials, running job training programs, producing documentaries, or hosting charitable events. Conducting DCAs allows donors to take a deduction for contributions that fund hands-on charitable work while maintaining full control of the activity. DCA expenses count toward the foundation's 5% annual payout requirement and can help donors directly engage in their missions while maximizing the value of their charitable dollars.

To learn more about these key takeaways and other important insights, check out the full conversation here.

HAVE A QUESTION?

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