

WEBINAR

Top Tools for HNW Philanthropy



The vast majority of affluent households participate in charitable giving, but most have never received formal guidance on best practices for doing so effectively. That creates an opportunity for advisors to deliver real value for their clients in an area that's important to them.



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Foundation Source's Josh Stamer recently sat down with Darren Henderson, a partner at Corient Capital Partners, to discuss how to be most effective in helping wealthy families with charitable planning — as well as how philanthropy can be a tool to enhance your high-net-worth relationships.

Josh Stamer: Advisors are sometimes uncomfortable approaching the topic of charitable planning with clients. How do you approach it?

Darren Henderson: We start with a framework discussing the four things that high-net-worth families can do with their wealth: You can spend it, leave it to your heirs, give it to charity, or pay it to the government in taxes. All of estate and financial planning is about pulling those four levers. Then we'll ask clients to rank each of them and what they want to accomplish.

Often, they want to leave money to their children, but cap it. So then we're talking about maintaining enough money in the estate and on the balance sheet to live a great lifestyle and do all the things they want to do. Then, the remainder is a tradeoff between tax and a charitable platform. When you can marry the charitable-planning aspect with the tax-minimization aspect, then it becomes even more interesting.

We start talking about what they want to achieve and whether they have identified a particular charitable cause or institution they would like to support. Usually, they want to support certain initiatives but don't know where to start. They have this general desire to be helpful, but they haven't really crystallized anything yet. Of course, the answers to these questions often change over time.

Then we drill in on the timing of their gifts and how they would like to help. What we're trying to really drive at is, do they have the desire to do something immediately from a giving perspective, or simply later in life or at death? Then, depending on the answers to those questions, we'll drill in on the tax implication of a gift. A client can certainly donate money over time to get a tax write-off and support all the things they care about by giving over time, but the challenge with that is that it's not very thoughtful. It's also not ingrained in broader aspects of estate planning and tax planning.

Stamer: That's a great way to start the conversation. We all know we are in the midst of the largest generational wealth transfer ever on record. Depending on the source, somewhere between \$60 trillion and \$70 trillion is going to change hands, generationally, over the next 20 years, and a good chunk of that is going to transfer through charitable giving and philanthropy. Which charitable-giving vehicles do you discuss with clients?

Henderson: We like to talk about all the options available and then start to eliminate the ones that don't make sense. So, we're talking about charitable remainder trusts (CRTs), charitable lead trusts, donor-advised funds (DAFs), and private foundations. We used to see a lot more trusts decades ago, when you had a lot of stock-to-stock transactions with high gains.

With a CRT, for example, the donor or other beneficiaries receive an income stream until the donor's death, when the remaining assets go to the designated charity. That was a great vehicle for donors who wanted to maintain cash-flow in the near term but do something on the back end. Obviously,

now with interest rates rising, the value of that deduction will be impacted. We have explored the CRT three or four times in the last few years with clients that had major stock positions. All of them decided against it for one reason or another, and they went with either a private foundation or a donor-advised fund. Both vehicles work very well from a tax-minimization perspective but they have important differences, and there are benefits and disadvantages to each strategy.

Stamer: A private foundation is its own legal entity, governed by an individual, family, or a business, while a donor-advised fund is sponsored by an independent organization advised by the donor. How do you help clients decide between a DAF and a private foundation?

Henderson: There are several factors that help determine whether a DAF or a private foundation makes more sense for an individual or family. For starters, we look at their initial donation level. If it's \$50,000 or less, that's typically too little to warrant the fees and other expenses that come with setting up the foundation. But you no longer need \$20 million to endow a foundation. Many of them have assets of \$500,000 or less.

We also talk about their future plans and how committed they are to this strategy. It's not a huge lift to switch from a foundation to a DAF, but you can't switch from a DAF to a foundation. Private foundations can exist in perpetuity, while there are some limits to the number of successors in a DAF.

The DAF might make sense for clients who have fewer charitable dollars to give or who give exclusively to U.S. charities, since it can be harder to make international donations with a DAF. DAFs also offer complete anonymity in grantmaking.

Stamer: Do you talk about the level of involvement or control that the donors want? We often hear from clients saying that they want to administer their own scholarship fund or want to incur charitable expenses or engage in other creative strategies that you unfortunately can't do within a DAF.

Henderson: Yes, that's one of the key elements we talk about. Private foundations typically require more involvement than DAFs, but they also provide more control over the investments and the grantmaking, which appeals to some donors, particularly those who are more entrepreneurial. With a private foundation, the donor determines the governance structure and the bylaws, and it can exist in perpetuity.

Everybody says they want ultimate control, but you must press them on it and ask, "Do you want to vet organizations? Do you want to have your own strategy, or do you want to just give money?" Usually, the clients that opt for the DAF just want to hit the easy button. They don't want to think about it or really have their family involved. They can, but they don't have to.

But with DAFs, we also frequently see issues around what you can do and where you can give. The grantees must be 501(c)(3) organizations, for example, and there is a limited but growing ability to make international gifts.

DAFs also have guidelines and restrictions on what you can and can't invest in. Our clients tend to like alternative investments a lot and, depending on the supporting organization, alternative investments may not be permitted with DAFs.

Foundations, on the other hand, can really embrace and utilize alternatives in a very big way. However, they also must distribute at least 5% of their corpus every year, while there is no annual distribution requirement for DAFs. Since private foundations must publicly record their grants on an annual tax return, it's harder to give anonymously.

Stamer: Many of today's donors want diversification in their philanthropic approach, just like they have a diversified financial portfolio. So sometimes the answer isn't just one of these solutions, but a combination of multiple vehicles. Are you seeing more interest from donors who want to use both foundations and DAFs?

Henderson: Yes, and this is a strategy that we are seeing become increasingly common. About 30% of our clients have both foundations and associated DAFs.

Having both a DAF and a private foundation can provide even greater tax benefits and flexibility. Often families will give their first tranche of contributions to their foundation, with the overflow going to a DAF. Donors can also use their foundation as a central holding vehicle for their charitable assets, and then use it to give grants to board members of their family's DAF, with such grants counting toward the foundation's required 5% minimum annual distribution. Such a strategy gives the donor additional time to decide the best way to use their charitable funds.

Clients who have both charitable-giving vehicles have more tools to use to achieve their philanthropic goals. They can use the private foundation to enter into grant agreements with recipients and personally present checks, and their DAF to facilitate anonymous giving.

Stamer: Both private foundations and DAFs have tax advantages. They provide donors with a current-year tax deduction for gifts made in the future, and they allow them to avoid capital gains taxes on appreciated securities. Assets in both vehicles grow tax-free and are exempt from gift and estate taxes. So how do taxes figure into your conversations with clients about their charitable giving?

Henderson: A lot of tax planners and lawyers start with the assumption that minimizing taxes is always the most important thing. While it is usually extremely important to most clients that we have, it's not always the most important thing.

You mentioned many of the similarities, but there are also important differences in the tax treatment. For private foundations, you can deduct up to 30% of your adjusted gross income (AGI) from your taxes for cash and up to 20% of adjusted gross income for long-term appreciated stock. The limits are higher for DAFs. You can typically contribute up to 60% of your AGI in cash, or up to 30% in other assets.

For both DAFs and private foundations, there is a five-year carry-forward for contributions that exceed the AGI limits.

Taxes often come up in conversations around private company stock, where donors are considering moving private stock from their company into a private foundation or a DAF prior to the liquidity event and then let it be realized inside the entity. Usually they decide against doing anything pre-transaction when they realize that there are some cases where you can only deduct the cost basis for a donation to a private foundation. That might not be clear until you get into the weeds of the structure of the private company, whether it's an S-Corp or a C-corp.

Stamer: You've been doing this for more than 20 years, and DAFs have changed a lot in that time. Having a foundation now is as easy as having a DAF. While traditional foundations were complicated and expensive to set up and required time-consuming administration, new model foundations offer automated back-office systems, real-time compliance monitoring, and online access to donors and advisors. What have been the changes from your perspective?

Henderson: Early in my career, the foundation option was much more onerous than it is today. It took a lot longer. You had to go engage an attorney and draft it, review it, and file it. The client had to manage that process themselves. But now, with companies like Foundation Source, it's almost turnkey from the client's perspective. Soup to nuts, I'd say we can get it done now in two weeks, 10 full business days.

There's also a much lower entry point for setting up a foundation. It used to be off the table for anyone who wasn't going to contribute \$20 million or \$30 million. Now, we're seeing it as a much more viable option at a lower entry point.

Stamer: When we work with clients, we work with their wealth advisor and their CPA to help determine the best timing, and whether it makes sense to set up a foundation pre-liquidity or post-liquidity. When do you bring in other partners?

Henderson: Very early in the process, we connect with our client’s current advisors or help them build the team to make it happen. That includes an accountant, a tax attorney, their trust and estate attorney, and specialists like Foundation Source. The quality of the outcome for clients that engage in strategies like this is dependent on the quality and experience of the team around them.

Interested in viewing the full conversation between Josh and Darren?

You can watch a replay of the webinar [here](#).



HAVE A QUESTION?

Call 800.839.0054 or send us an email at info@foundationsource.com.

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