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Putting the "Family" in Family Philanthropy

How families may use philanthropy as a vehicle for transmitting values and working together multigenerationally

Key points

- Charitable planning involving multiple generations starts with the family's needs, interests, assets, and goals
- A family needs to think not only about its portfolio of assets, but also its portfolio of interests
- With open channels of communication, you can help create a philanthropic legacy for multiple generations, engaging the family and benefiting the causes the family supports

For many individuals, philanthropy is one of the more gratifying parts of estate planning. Adding in a multigenerational component can make it even more meaningful and compelling. Just as every family is unique, so is their philanthropic approach, and there is no single way to involve a family in philanthropy.

What is multigenerational philanthropy?

In some respects, multigenerational philanthropy is defined by what it is not. It is not the senior generation showing younger generations how to engage in philanthropy, what we might call the "Watch Grandpa Give Wisely and Well" model. Rather, it is the family acting together collaboratively on philanthropy that engages the family as a whole. Because a family may have complex dynamics, so too may family philanthropy.

From a tax perspective, the charitable contribution deduction continues to provide tax savings for taxpayers who can itemize. Even though lower tax rates generally bring lower tax savings from deductions, some families will see greater deductions, as the 2017 Tax Cuts and Jobs Act eliminated the phase-out of itemized deductions applicable to higher-income taxpayers (through 2025).[1] For 2023 through 2025, cash gifts to public charities are deductible to the extent of 60% of adjusted gross income (AGI), and returning to 50% after 2025.[1] For families of considerable wealth, the estate tax remains in place, providing yet another tax incentive for charitable giving. For donors who can't itemize every year because of the increased standard deduction, there are strategies to bunch deductions so that they can make deductible gifts in some years.

[1] Source: www.irs.gov

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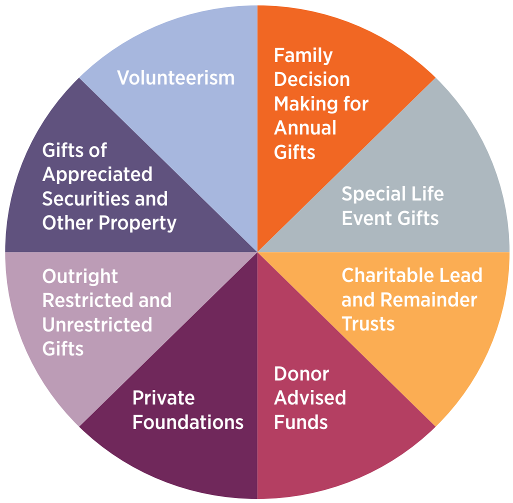
Organizing your family philanthropy



> "Giving should be entered into just the same careful way as investing. Giving is investing."
>
> — JOHN D. ROCKEFELLER

Philanthropic giving, however, is about much more than tax mitigation. From an emotional and family values perspective, many families are looking at issues such as: What is the right amount of wealth to leave the next generation? And how can parents or grandparents prepare the next generation to inherit not just assets, but also the family's values? For a family at any wealth level, charitable planning can be important part not only of managing income and estate taxes, but of resolving these personal concerns about transmitting family wealth and values in a meaningful way.

Where does a family begin?

Like all planning, charitable planning involving multiple generations starts with the family's needs, interests, assets, and goals. Charitable planning really is like investing: a family needs to think about its portfolio of assets, but also its portfolio of interests. Some assets are more tax-effective than others for funding charitable gifts, and different structures will be more effective for different assets and different philanthropic goals. A family with income needs and highly appreciated securities as its principal assets will approach things differently than a family that does not need additional income, but whose principal asset is a closely held business. And families that want to benefit a specific charity will be looking for a different solution than a family that wants to create a grantmaking entity for the long term. As a family develops its own philanthropic portfolio, it needs to consider what assets work best for family philanthropy, and which assets may be best for personal philanthropy or kept for family investment. But even as they think about the assets to give, families also need to think collectively about their philanthropic interests.

Communication is key

Nothing is sadder than watching a charitable gift unravel, bringing disappointment and loss to both charity and family. In addition to the technical aspects of deciding the right structure and the right assets for funding a multigenerational gift, there are enormous communication needs. More even than with other charitable gift planning, there needs to be communication within the family. A multigenerational gift entirely structured by the senior generation and force-fed to the next generation is likely to fail. Donors cannot assume that family members will share their passions or want to be involved in the family's charitable endeavors. And surprising the family at death can be a big mistake that can lead to hurt feelings, confusion, family quarrels, and perhaps even litigation.

And as with every charitable gift, there is a need for clear communication with the charity. It is important to make sure that a charity is in a position to accept a gift and that it is not surprised by it. For example, a museum that you feel would be the perfect recipient of your prized Picasso may not even be able to accept the painting because it cannot afford to store and insure it. With advance communication, you could seek out a different charity or endow a fund to maintain the gift.

What forms of philanthropy are right for your family?

Successful multigenerational philanthropy is not giving by example, it's giving by collective family decision making. Together, you need to first determine what level of philanthropy is right for your family now, and also how that might evolve as your family evolves.

Gathering the family around year-end giving and for life cycle events

For some families, simply writing a check to a charitable organization that supports causes the family believes in may be the right level of philanthropy. Attending charity-sponsored fundraising events may also be a good fit. Using a holiday

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Caveat to families: Tax planning is complex

Gifts to charity are deductible from federal income tax under fairly complex rules, so it is always important to seek tax advice and to run the actual numbers. Under current law, your income tax savings from a particular charitable gift will depend on your adjusted gross income, the kind of asset given, the nature of the charitable recipient, other charitable gifts made during the same year, the total amount of your other deductions, your tax rate, and whether whether you are subject to the alternative minimum tax (AMT).

Furthermore, gifts of more than $250 must be acknowledged to be deductible. Finally, state tax rules may be different from federal rules.

For more information visit www.irs.gov.

when the family is gathered together, such as Thanksgiving, to hold an annual family philanthropic meeting can help facilitate discussion on what causes to support over the year. Engage your children in the process by encouraging them to use a portion of any financial gifts they receive for birthdays, holidays, Bar/Bat Mitzvahs, weddings, and other events to support a charity that they care about. The important part is to encourage children to think about their own causes, creating a culture of giving early on that can extend through multiple generations.

Volunteerism

Volunteering time as a family and making a commitment to a charitable organization can be a great way to integrate philanthropy into a family. Seeing first-hand how contributions help those in need can have a powerful impact on children's desires to give back to their community. Older family members may also want to volunteer to serve on a board or participate in the operations of a charitable organization.

Planned gifts and philanthropic structures

Some families may wish to make a formal philanthropic effort in the form of planned gifts, such as establishing a scholarship fund at a school that has special meaning to their family. Or, you may want to consider vehicles such as private foundations, donor advised funds, and charitable lead trusts, which offer opportunities for long-term gifts that engage the family for generations and also provide potential tax-saving benefits.

- **Outright, unrestricted gifts**
  Not all multigenerational gifts need to be complex vehicles. A family can make an outright gift to charity as a multigenerational gift simply by having family members agree on a charity they care about and each making a separate contribution to it. Each contribution can reflect tax planning appropriate to that family member. For example, a parent might make a fairly large gift of appreciated securities held for more than a year, mitigating capital gains tax on future sale of the securities and potentially obtaining an income tax charitable deduction for the full market value of the gift. On the other hand, a young adult child might simply make a gift of cash, and most likely on the internet.

- **Restricted gifts**
  Often a family can carry out its values effectively by making a restricted gift to a charity. For example, a family might support a local community organization but limit its gift to specific programs for local conservation. In some cases a simple restriction can be accomplished just by a cover letter or even a notation on a check. However, sometimes a family may want a fund established at a charity to carry out a specific purpose permanently, for example a scholarship fund at the college or university attended by many family members. Many restricted gifts will require a gift agreement between the donor and the charity, clarifying not only the purpose of the gift, but what will happen in the event that the charity can no longer fulfill that purpose.

- **Private foundations**
  Private family foundations are grantmaking entities that provide a way to foster a family's values and provide a focus for charitable giving. They encourage intergenerational involvement by sharing values and decision making within the family while establishing a long-term legacy for the family. They can also create an endowment to fund future giving, while offering income, estate, and gift tax advantages.

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A private foundation can be created as a nonprofit corporation or a charitable trust, and it's important to remember that it is a separate tax-exempt entity. Your family must be motivated enough to accept the complexity of the entity and the responsibility that comes with running it. It's very easy to fall into the "documents are in the drawer" syndrome and simply write checks as the primary function of your private foundation. Family communication and involvement are key to creating a true endowment that reflects your family's unique values and engages the family to carry out its philanthropic vision.

A private foundation can also provide a training ground for the next generation on corporate governance, investments, and philanthropy. A family can adopt a trustee or director structure, providing the next generation with the opportunity to serve on committees, such as an investment or grantmaking committee, before becoming a full board member with a full vote. A family can also create different tiers of board members, so that the senior generation has more voting rights than the younger, inexperienced family members.

Of course, the complexity of a private foundation means that it carries several disadvantages as well, such as the time and cost associated with running it. As a tax-exempt charity, it is regulated by the Internal Revenue Service (IRS), as well as state charitable law. It must file an exemption application and an annual information return with the IRS, and must pay out at least 5% of the fair market value of its assets annually to charity.[1] Private foundations are prohibited from self-dealing and engaging in certain activities, such as lobbying and political campaign activity, and are subject to limitations on holding business investments. The deduction rules applicable to contributions to private foundations are also less favorable than those for "public" charities. For example, a donor's deduction for a gift of closely held stock to a private foundation is limited to the donor's basis (the initial investment, with some adjustments).

- **Donor advised funds**
  Some benefits of a private foundation can be achieved by establishing a donor advised fund (DAF) through a sponsoring charity, such as a community foundation. By law, donors may only recommend charities to receive distributions of donated funds, but in most cases sponsoring organizations follow those recommendations. DAFs can be a good option for smaller but still significant donations, as they are simpler and less expensive to establish than private foundations. Some DAFs will also allow the donor to select his or her own investment advisor to manage the funds.

  Because a DAF is maintained by a public charity, the deduction limitations and operational restrictions that apply to private foundations generally do not apply. And, donors can contribute appreciated property, such as closely held stock, to a DAF and still receive a full fair market value deduction (The DAF is subject to the private foundation restrictions on holding business investments.). A DAF can also be a good vehicle for donors to "bunch" deductions, so that they make large enough gifts in some years to be able to itemize deductions, while in other years they limit charitable gifts and take the standard deduction. But they can keep their charitable support at a steady pace by making distributions from the DAF every year to the causes they support.

  While a DAF can be an attractive solution for many philanthropic families, it has some disadvantages. First and foremost, the donor does not retain control over the fund. The donor and his or her family will be subject to the policies and procedures of the charity maintaining the fund, including its grantmaking and investment policies. If the donor wants the fund to be invested in certain investments, for example, that may not be possible. Further, the opportunity to have family members involved as advisors for multiple generations may vary from one DAF to the next. If a family wants to establish a long-term advisory vehicle, it should discuss the DAF's policy in advance.

  Just like a private foundation, a DAF is as good as you make it. Engage the family in the process and communicate regularly about what you hope to achieve from your DAF or it too can become a "document in the drawer."

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- **Charitable lead trusts**

  A charitable lead trust (CLT) is a less common vehicle for multigenerational philanthropy, but for some families it can offer the benefits of a structure providing for family collective charitable distribution decisions along with the benefits of long-term wealth transfer to the family.

  A CLT is a trust that provides an annual payment to one or more charitable beneficiaries for a period of time, with the remainder interest going to family members. A CLT pays an annuity or unitrust payout, and there is no minimum or maximum payout requirement. The family can be the decision makers for the trust, although the trust creator cannot be, allowing the family to gather annually to make collective decisions on the charities it wants to support. The CLT can make charitable distributions to a DAF or private foundation, creating a funding stream for a long-term family philanthropic structure.

  Unlike a private foundation, a CLT is not a tax-exempt entity. But it can provide gift and estate tax benefits, as it permits the transfer of any appreciation in excess of the IRS benchmark rate to a family, free of gift, estate, and generation-skipping transfer taxes. This type of trust is particularly attractive in a very low interest rate environment. A CLT also provides income tax benefits; depending on how it is structured, either the grantor or the trust itself will receive a charitable income tax deduction. If the CLT is a "grantor" trust, the grantor will be entitled to a charitable income tax deduction in the year the trust is created, subject to the limitations applicable to all charitable gifts by individuals. However, the grantor must include the trust's income in his or her taxable income in subsequent years. If the CLT is a "non-grantor" CLT, the trust will have an unlimited charitable contribution deduction for the annual distributions of income to charity, and the grantor will not include the trust income in his or her taxable income in subsequent years.

  In some respects a CLT can provide the benefits of a private foundation—annual grantmaking to a charity of the family's choice—with the benefits of family wealth transfer.

The payoff of family philanthropy

Family philanthropy can be hard work, but is also immensely rewarding. When a family takes the time to work together to identify its philanthropic goals and to collaborate on where and how to give, it can create a meaningful philanthropic legacy for multiple generations.

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