Executive development through family foundations

By Sandra J. Champion

In the United States, private foundations are mandated to distribute 5 percent of their fund's annual monthly average to financially support public charities. The Internal Revenue Service (IRS) classifies both entities as 501c3 tax exempt organizations, but they are managed very differently.

Prior to 1969, private foundations fell under a great deal of public scrutiny for a variety of reasons. Most of those reasons centered around the assumption that wealthy families protected their financial assets from taxation by creating foundations that allowed their assets to grow in an exempt manner. Tax reform in 1969 split the world of charity into two distinct categories: public and private. As a result, three long-used terms, fund, foundation and charity, no longer had any specific meaning. The post-1969 way of thinking about charities is that the way an organization functions will reveal the true nature of the organization.

In the case of public charitable organizations, the IRS does not regulate the financial amount they can distribute each year because these organizations are thought to be created for the good of society. The Bill, Hillary and Chelsea Clinton Foundation, which lists its mission as working "to improve global health & wellness, increase opportunity for women & girls, reduce childhood obesity, create economic opportunity & growth, and help communities address the effects of climate change," is an example of a public charity. Consequently, under the IRS mandate, it is not required to make a charitable distribution.

Rules are different for private tax exempt organizations. In an effort to control or monitor the wealth of private charitable entities, the IRS mandates that every year they must distribute 5 percent of the annual monthly average of their fund to a charitable activity. In effect, private "foundations" exist to provide financial resources to public charities.

This raises several important questions: Where is the need for a private family foundation? How does the structure serve the family beyond check writing?

The use of a private family foundation structure is much more useful to the family than simply financially supporting charitable activity. While the charitable activity can create a 'feel good' sense of accomplishment, there is benefit greater than merely writing a check. The family foundation is a perfect place to groom the next generation for business leadership.

In the foundation structure, the family learns to discuss a series of items, sometimes agree, sometimes disagree and often to agree to disagree. These discussions fall into

four primary areas, each of them critically important to properly managing both a business and a private foundation. The areas are:

1) Financial investment management.
2) Governance and oversight.
3) Administration.
4) Charitable investing/grant making /the business of philanthropy.

Once the decision is made to create a family foundation the challenge to keep the balance between the family and the foundation begins. It is important to engage all members of the family. The wealth creator of the family, whether patriarch or matriarch is often the most forceful voice of the family. The voice the family has grown to provide guidance. Both unfortunately and fortunately the wealth creator seldom fully understands how to managed a private foundation for impact. Charitable activity may even seem counter intuitive.

Here, it is worth noting that gifts and grants are different. Gifts, which are often given from parents to children, are offered with no expectation of anything in return. A grant from a family foundation, however, is 'granted' with expectation. Foundations, after all, seek ROI.

While the family leader understands ROI in business, charitable ROI is different. Because family leaders often lack a full knowledge of processes that govern giving to 'charities', they often feel a sense of insecurity when they become involved in charitable giving. Because these feelings of insecurity had not existed previously and because each member of the foundation often contributes in ways that had previously not been considered, robust conversation and personal development are certain to result.

Several years ago, a business leader who had sold his company for a substantial amount of money was quoted six months later as having said, "How many homes can I buy? How many cars can I drive? How many times can I travel around the world? With some many years dedicated to my business, what have I done to my family?" Creating a family foundation allowed him the opportunity to reconnect with his children and truly enjoy the fruits of his labor. By working together, his children became more aware of sacrifice and hard work. They also experienced success as a family. While their charitable family accomplishments were exceptional, each would agree the greatest impact from their foundation was truly connecting with each other.

The bottom line is that by creating a private family foundation, families can overcome some initial obstacles and learn and grow together and create substantial impact by engaging in the families' signature philanthropy.

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