Philanthropy and Private Foundation Readiness

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Contents

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"It is more difficult to give money away intelligently than it is to earn it in the first place.

- Andrew Carnegie

The literature available on private or family foundations[1] primarily – and rightly – focuses on charitable mission.   The emphasis has been on effective granting, charitable programs, and evaluation, as well as the related issues of foundation management, family involvement, and succession planning. The assumption in this body of work is that the foundation already exists and philanthropic programs are established.[2]

There are also extensive resources on how to create a private foundation, primarily specific to the laws of their respective countries.[3] Far less has been written about the establishment of private foundations in terms of suitability – to the founders (typically husbands and wives), their family, and to the intended philanthropic mission. What happens at that moment of transition when affluent individuals have the funds and motivation to make a large charitable gift? What happens when they are considering their philanthropic options?

This chapter addresses that moment of altruistic transition. Our intention is to provide perspective to advisors about "how" and "why" private foundations are established. What are the issues and options that need to be addressed at the moment of transition? Just as important, we want to examine the question of "who" should establish a private foundation and what the foundation should look like.   Advisors often see the planning utility of private foundations, and can sometimes miss the message and core values.

[1] We use the terms 'private foundation' and 'family foundation' interchangeably throughout.

[2] An excellent example is Gersick, Kelin F., Generations of Giving, Lexington Books, 2004.

[3] First Steps in Starting a Foundation, 5th Edition, Council on Foundations, 2007; Starting a Foundation, Philanthropic Foundations Canada, 2004.

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Therefore more attention needs to be paid to the future success of the foundation as vehicles of 'mindful philanthropy'™.[4]

We provide a brief summary of the private foundations and philanthropy at the time of writing to provide a context. The decade since 2000 has been characterized by a period in philanthropic activity worldwide not seen since the beginning of the 20th century in the United States, with extraordinary wealth being created and dedicated to philanthropy.

Although private foundations remain the philanthropic standard for affluent individuals and families, often they are not the right choice. If that is the case, other options should be explored, and consequently we have provided a brief review of the alternatives. The heart of this chapter is 'The Private Foundation Readiness Checklist', a ten-question tool for advisors and would-be private foundation philanthropists to assess readiness. Throughout the chapter we have included anecdotal case studies to provide a counterpoint to the main text. Some of these case studies address the creation of a private foundation, and others deal with the downstream issues that emerge within family foundations over time. Finally, we should note that we are Canadian advisors, and although we do draw upon international sources, the majority of our data and experience is with Canadian philanthropists and business owners. We hope advisors and philanthropists in other countries find our Canadian experience to be valid and helpful.

Philanthropy in Context

Philanthropy in the industrialized world reflects trends in demographics, wealth, and family makeup. The same phenomena driving the global wealth management business are influencing philanthropy:

- Greater wealth is more concentrated in fewer hands.
- Families are smaller in the industrialized world, leading to situations where there is excess wealth for family needs.
- The nexus of individualism and consumerism has (perhaps) weakened social bonds and increased the desire for personal expression. While this seems like a strange point to make in this context, large-scale private philanthropy often has strong elements of wanting to shape and express a personal vision in the public

[4] A philosophy of giving developed by Burrows and Pervin 2008.

sphere. If taxes are an anonymous way to participate in and contribute to society, philanthropy is a highly personalized public action – even when done quietly.

- There has been a material reduction in tax rates in the major industrial countries, and in many jurisdictions, a corresponding increase in tax incentives for charitable giving. U.S.-style tax incentives – tax deductions, extra savings for donating certain asset classes, and increase contribution or claim limit – have become more prevalent internationally. The United Kingdom, for example, eliminated capital gains tax on public securities donated to charity and introduced hybrid structures, such as the community interest company. Canada has overhauled its Income Tax Act since 1996 to provide more than 20 new incentives to promote donations of assets. Singapore has a generous double-deduction system.

- Philanthropy has become a powerful ideal. Embodied by examples such as Bill Gates, Warren Buffet, and Li Ka-Shing, philanthropy is being held up as the socially responsible path and, for many affluent individuals, a way to express their values through their wealth and to make a lasting contribution to the betterment of the world. 'Philanthrocapitalism' has arrived, and although there will be ongoing debate about its aspirations, appropriate role, and failings it is a concept that is likely to stay and thrive long-term.[5] And, of course, there will be numerous lower profile and more traditional private foundations that reflect this trend.

These factors have driven a decade long growth in charitable giving that is unprecedented in recent memory. For example, from 1995 to 2006, Canadian tax receipted giving increased from C$3.6 billion to C$8.5 billion, an increase of 133% over an 11-year period. By comparison, the Canadian economy, which has been one of the stronger G8 economies, grew at half the rate.[6] The number of Canadian donors has been in decline, dropping to 24.7% of tax-filers in 2006 from 25.1% in 2004. In summary, there are fewer donors giving more – and many of those donors are giving disproportionately large gifts from business assets. The global financial crisis of 2008 may affect elements of this dynamic, but the general trend is likely to persist over the long term.

[5] Edwards, Michael, "Just Another Emperor? The Myths and Realities of Philanthrocapitalism", Demos: A Network for Ideas & Action and The Young Foundation, 2008.
[6] Canada Revenue Agency

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The Philanthropic Moment

There are two pockets from which we can give to charity: the income pocket and asset pocket. The income pocket funds donations from cash flow or annual income. It is the source most people draw upon when donating to charity. Income donations will range in value in proportion to the donor's income. Typically, there are a number of charities a person supports, and for many of these charities the support is recurring. Gifts from income are the most common kind of donations, but they are not typically the type of donations that fund private foundations. In some cases, the model of giving from income is so entrenched that it is hard for donors to imagine utilizing their capital to support charities.

Second, there is the asset pocket, which is funded by net worth. These are the assets that people live on and live in, and for business families they are often tied up in an operating business. Far fewer people give from the asset pocket, and when they do they do, it is often connected with major life events, such as retirement, sale of a business, or death. In the words of David Dunlop, one of the pioneers of major gift fundraising for education in the United States, these donations are "ultimate gifts".[7] A donor of a significant gift from assets, such as a bequest, needs to be more mindful about the donation, both in terms of personal planning and intended effect and outcome. The philanthropic moment is the time of transition, when assets are released and become available for redeployment. Frequently this philanthropic moment occurs later in life, often after the building and acquisition phase. Despite the media focus on a generation of young philanthropists who have come out of high tech, the more typical first-generation philanthropist with a private foundation is aged 55 years or older.

The worldwide philanthropic growth over the last decade has primarily been funded by the deployment of business assets. Private foundations have always existed along side family businesses, and many have been funded by annual donations, which typically represented a portion of annual profit. This cash-flow model of funding private foundations, however, is being supplanted by event funding – major infusions of capital often at times of maximum liquidity, such as a business sale. These sums are often considered to be too large to contribute to a single charity, hence the desire to establish a holding entity that will enable the future funding of many charities. Often these sizeable asset donations create endowments that are invested to produce annual income to fund grants.

[7] David R. Dunlop. "Major Gift Programs" in Educational Fund Raising: Principles and Practice, ed. Michael J. Worth (Oryx Press/American Council on Education, 1993), pp 97-116

One of the biggest challenges for would-be philanthropists is moving beyond the model of annual funding and beginning to think about charitable giving as an integral part of their estate. The lifelong habit of giving income often fosters a transactional mindset, while dedicating capital to charity, especially a private foundation, requires a strategic mindset. A significant asset donation will impact the overall estate plan and family wealth, and it also raises the stakes for philanthropy.[8]

Philanthropic Options

Significant philanthropy can be divided into two categories: direct gifts to charity and gifts to intermediary charitable containers, such as private foundations and donor advised funds.

Direct Gifts:

It is important to recognize in any discussion about philanthropy that direct gifts to operating charities represent the majority of donations. Donors give directly to the charities that are doing the work. Deep trust and confidence exists and no mediation is required. Direct gifts perhaps reflect a mode of giving that is typically more spontaneous than foundation giving and reflects a strong personal relationship or psychic attachment between the donor and the charity. Witness the increasing prevalence of seven-to-nine figure gifts to institutional charities, especially universities. Internationally, there have been headline-grabbing gifts like the C$1.5 billion U.S. bequest by Joan Kroc, widow of McDonald's founder Ray Kroc, to the Salvation Army in 2006. What limits the value of direct gifts is often the capacity and perceived accountability of the charity. Large gifts are donated to established capable organizations. If the intent is to seek out smaller, younger charities, the methods of engagement change and the gift size shrinks. Often the intended gift is simply too large to give away effectively at one time. There may also be concerns that the gift is irrevocable and, once given, cannot be significantly modified.

Charitable Containers:

'Charitable container' is a generic term for entities, such as donor advised funds and private foundations. These are intermediary entities that exist to receive and manage charitable funds and, typically, they serve as funders of 'doing' charities. (Of course, not all private foundations are limited to granting, a purpose that we address below.)

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[8] Interestingly, this describes the beneficial essence of our 'mindful philanthropy'™ advisory service.

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Charitable containers are ideal for long-term philanthropy because they typically allow the donor and his/her family to continue to be involved in charitable decisions after the gift has been made. From a planning perspective, charitable containers are invaluable because they separate funding (the gift or gifts) from the ultimate use or distribution of charitable funds (grants). Containers provide planning certainty and time to develop a long-term strategy. Containers are useful when the gift is of a relatively large value to the donor and there are multiple charitable goals to achieve or charities to fund. They also separate the gift from the ultimate charitable use, buying time for thoughtful distribution of funds.

CASE STUDY 1: SHIFTING MOTIVATIONS – FROM CORPORATE TO FAMILY FOUNDATION

> My family company was very visible – both in our industry and the community. For years we had given personally to major charities, and our company underwrote a college training program that was industry specific and provided skilled workers to the firm. The founder, my father, began searching for additional ways to minimize the amount of tax he had to pay to the government. Our advisors suggested a private foundation. For fifteen years, the business-integrated stories about the company and the foundation appeared interchangeable. The foundation never held any money; rather, it was funded based on business commitments and corporate profits, and the money was disbursed annually. When Dad died he made a significant bequest to capitalize the foundation. Soon after I remember John, Mom and Dad's lawyer, explain the gifting policy: "when the request folder was two inches thick, it was tax planning time". Out of the six of us, I was the only family member working in the business, so it made sense for Mom to separate the business giving from the family giving. She wanted to continue the informal way of responding to community needs, but away from the firm. Mom had never participated with Dad in this gifting process, and I had only been at one meeting. So, the seven of us decided to develop a focused mission for the foundation. Although we are making some headway in creating our own direction, I recently overheard Mom tell Aunt Jane that this foundation has been helpful in providing unity to her family. Interestingly, my siblings and I might describe the situation differently: "we are intimidated from speaking due to the constant presence of John, Mom's lawyer. His interest in protecting Mom seems to undermine our participation, but we are getting better at managing the old coot and directing the money to projects that we think are worthy."

Donor-advised funds (DAFs) are to private foundations what mutual funds are to the traditional segregated investment portfolio. They offer similar benefits, such as donor direction and flexibility, and because they are offered through public charities, they also offer ease of establishment and management. As the name implies, the donor advises the master foundation on the use of the funds (and sometimes the investment), but does not have legal control over the entity. Often donor-advised funds are promoted as offering all the (obvious) benefits of a private foundation without legal costs or the administrative burden. With minimum donations of as little as C$10,000, the donor-advised fund is a democratic structure that enables long-term, self-guided philanthropy.

In the North American environment, community foundations and commercially sponsored foundations have criticized private foundations in order to market donor-advised funds. Casting private foundations as the straw man to sell another philanthropic option is unfortunate, and occasionally quite misleading. In many cases, the donor who is considering a donor-advised fund should not be considering a private foundation. The scale, structure and responsibility are different, despite certain functional similarities. Implicit in the endowed donor-advised fund model at a community foundation is the assumption that the founding family will not be around to guide granting in the future hence there is a default to the mission of the foundation. That said, a donor-advised fund is an excellent solution for a large number of donors. Some donors are seeking the granting insight and collective vision of community foundations. Others value the service and convenience. New models that offer the ability to create a limited-term container may serve the specific goals of sophisticated philanthropists better than private foundations. Indeed some philanthropists utilize donor-advised funds in coordination with private foundations. If there is a congruence of goals and values between the donor and the foundation holding the donor-advised funds, the gifts can be as great as those to a private foundation or a large institution.

Private Foundations

Private foundations are an outgrowth of medieval charitable trusts. In most common law jurisdictions, a foundation can be formed either as a corporation without share capital or as a trust. Typically, they are standalone charities where the majority of directors or trustees are not at arm's length from each other and the funding has come from a single source. Legal control of the assets by the directors or trustees is attractive to the business owner or executive, or indeed anyone who desires a high level of engagement with the philanthropic activities of the entity. Private foundations are an individual, as opposed to communitarian, model of philanthropy.

Perhaps because of the legendary U.S. private foundations such as Rockefeller, Ford, Mellon and more recently Gates, private foundations are considered the 'gold standard' of charitable structures for wealthy individuals.[9] In the United States, it has been estimated that 75% of the 400 wealthiest families have private foundations.[10] In

[9] Silk, Roger D. and Lintott, James W., Creating a Private Foundation, Bloomberg Press, 2003, pg. 1
[10] Ibid, pg. 1

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Canada, private foundations have been the fastest growing category of registered charities in the past decade. Although less than five percent of registered Canadian charities, private foundation hold C$13.14 billion in assets or 19.3% of the total assets in the sector. Private foundations have also been the recipient of 22.5% of new investment assets in the sector between 2002 and 2006.[11]

What are the qualities of a private foundation that no other charitable structures offer? Private foundations have the following primary characteristics:

- They are separate legal entities.
- They are typically tax-exempt registered charities operating within the laws of a particular national jurisdiction.
- Many jurisdictions offer tax benefits for donating to charity, including private foundations.
- The funding derives primarily from a single source.
- The directors or trustees are normally not at arm's length. In many cases, they are family. Directors/trustees are typically related to the primary donor, and in the case of the first generation, the donors are often also the director/trustees.
- They provide a high level of control for the donor within a regulated environment. ('Control' may be translated as compliance and individual oversight.)
- They may be both grantor and/or operating charity. In other words, private foundations may fund other charities as well as operate their own charitable programs.

When reviewing these characteristics it is easy to see similarities with family businesses. Often the qualities necessary to be a successful entrepreneur translate to the social sector and to private foundations. The experience of operating a business, dealing with family dynamics, and identifying markets are applicable to private foundations. They also provide a structure to transfer and segregate wealth in the family. The ownership structure shared by family businesses and private foundations, although not entirely analogous, is characterized by a strong sense of personal responsibility. A private foundation requires active management, and unlike other charitable structures cannot survive on trust and passive participation. This is one of the reasons retiring business founders often see their private foundations as their next business venture.

[11] Canada Revenue Agency

At the progressive end of the spectrum, some entrepreneurs are attracted to the concept of 'social entrepreneurism', a concept pioneered by Bill Drayton and the Ashoka Foundation, which applies the energy and focus of the business entrepreneur to social problems.[12] In a family foundation context, sometimes this approach takes the form of strategic granting – searching out and backing promising and passionate social entrepreneurs – and other times the foundations aspire to do the work itself. This kind of iconoclastic, deep engagement is best suited to a nimble, high control structure such as a private foundation. Typically the goal is high impact rather than longevity. The Young Foundation in the United Kingdom is a current leader in the social innovation field, and also an example of a foundation that operates its own activities, notably applied research and The Michael Young Prize for excellence in social science. [13]

CASE STUDY 2: VISION AND COMMITMENT

> I set up our private foundation seven years ago at the suggestion of my accountant. We had always made annual donations from our family business, and Ralph suggested one year that it would be good to have a foundation for tax reasons. The lawyers did their work and the foundation was established, and we put $400,000 into it. It was invested in mutual funds with my broker and soon forgotten. We still gave significant amounts annually to charity from the company, but the foundation wasn't part of the picture. We never bothered to have board meetings, as it just didn't make sense to be wasting valuable time over such an insignificant amount of money. Not surprisingly, after a while I began to wonder why it existed. To make matters worse, one year we forgot to complete the regulatory filings and almost lost our charitable status, which in retrospect might have been a good thing. Recently, we have been revising our wills and our lawyer asked if we wanted to "create a legacy" with our foundation. While this is a vaguely attractive idea, we think our legacy is our children and grandchildren – and the business, of course. It strikes me as ridiculous to have some big vision for our family foundation when it is only one of many corporate vehicles that we own. The local hospital is having a capital campaign and we're being hit up for a big gift – maybe we should clean out the foundation once and for all.

In a more classic model, private foundations excel as structures for long-term philanthropy, focusing on certain issues and causes to effect change over time. An excellent example of a 'legacy' foundation that has been effective in long-term giving is

[12] See Bornstein, Daniel, How to Change the World: Social Entrepreneurs and the Power of New Ideas, Oxford University Press, 2007 (revised edition).
[13] http://www.youngfoundation.org.uk/

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The J. P. Bickell Foundation in Toronto, Canada. Founded in 1953 by Toronto-businessman John Paris Bickell, the Foundation started with $13 million in capital from a bequest. It has a defined granting mandate with a 60% focus on medical research. This seems conservative after 55 years, but you have to imagine the state of medical research in the early 1950s. Medical research was embryonic in Canada, and the need of local hospitals in the post-war period was capital for new buildings. Bickell made a strategic bet on research, not bricks and mortar. The primary beneficiary has been Toronto's Hospital for Sick Children, which has received ongoing Bickell Foundation support and has gone onto become the largest medical science research institute in Canada and world-renowned in fields such as genetics and immunology. As of 2007, the Foundation has granted C$118 million to charities, and the capital has grown to C$115 million. And the legacy continues with annual distributions of C$4 million. Bickell could have made outright gifts to charities (although most of the beneficiaries to date were not in existence when he died), and if he did the capital would probably have been well spent within five to ten years. Instead, he chose to create a perpetual, dynamic legacy that meets the ongoing needs of society. Models like the Bickell Foundation are very attractive to certain philanthropists, especially entrepreneurs who see their family business and community engagement as a source of legacy.

The Private Foundation Readiness Checklist [PFRC]

We have explored in our practices how the professional designation of the advisor affects the planning process. For example, to the family accountant, a private foundation is often primarily an exercise in tax minimization (depending upon the jurisdiction) and ongoing compliance. At the other end of the professional spectrum, a family business advisor/philanthropic consultant views the challenge in terms of strategic philanthropy for the family or public benefit. Returning to our focus on the business owner at the moment of transition to serious philanthropy, what does he/she need to consider?

The following checklist was developed as a quick assessment tool for professional advisors to determine whether a private foundation is an appropriate philanthropic structure for a client.[14] It examines what we believe are the key attributes or characteristics of a successful private or family foundation, and the readiness of your client to embark upon one.

The checklist is purposefully simplistic and agnostic and may be used by advisors (and would-be philanthropists) from a variety of backgrounds. The questions are of the "yes/no" variety, and the scoring is straightforward. In our view, a score of 7 or more "yes" answers out of 10 questions indicates that a private foundation is a suitable structure for the individual or family. A score of 6 or fewer "yes" answers suggests that

CASE STUDY 3: FAMILY DYNAMICS AND LEADERSHIP

We were asked to assist in the leadership transition for an established family foundation. When we interviewed the foundation members, it appeared that the outgoing 85 year-old founding autocratic leader was characterized by the saying, "he has his tongue to speak and his words to hide his thoughts". This culture of deceit was reinforced through oppressive family interactions. "He's the master of the double bind – we can never win with him. And, he doesn't understand that his criticisms and put-downs or complaints censor us and separate us. He thinks he is helping us grow and become strong, competent foundation members". Rather than address the presenting problem, and possibly hurt the founder, we decided to focus on the desired outcome and develop a respectful resolution.

We explored the family history using a genogram and unearthed many positive origins of collaboration, respect, trust and philanthropy. We built on these bonds of connection and mutuality and developed a constitution and governance system that clarified the vision, mission, commitment, culture, values, communication, dispute resolution mechanism, decision-making style, grant-making process and methods to keep the peace. As the team emerged, the family became more cohesive and emotionally connected. And, you guessed it, the founder became more comfortable and trusting of the new approach, and the next leader was someone who demonstrated empathy and sensitivity and valued positive relationships in all areas, and also had a passion for community service. It doesn't happen often, but in this situation, we were pleasantly surprised that a positive foundation experience was the catalyst to repair a damaged family experience

[14] Although we present the information for professions in the wealth marketplace to use at a meeting, we have also had success by providing the questions to our clients ahead of time, especially husbands and wives, and suggesting that they meditate on the possible responses as preparation for the meeting.

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a further discussion of philanthropic options is required. For example, you may wish to suggest that a direct gift to charity might be more appropriate, or a donor-advised fund. Alternately, if tax is a potent motivator, it may make sense to explore tax planning strategies that have nothing to do with charity.

While many successful private foundations have been founded by individuals and families who would have scored low on this assessment exercise, the comprehensiveness of the questions is intended to provide clues about appropriateness and fit.

The checklist questions are designed to call attention to key emerging themes that can be explored in greater detail at a future meeting where a more open-ended, collaborative examination-style is beneficial.

Underlying each inquiry is a commentary for illustrative purposes which should help the advisor start a dialogue with the client. These themes and topics are not intended to be rigid rules that will restrict what foundations can do, as we happily acknowledge that the greatest philanthropists have a talent for shattering traditional models in pursuit of public good. Rather, the information presented is intended to provide indications as to whether the clients – and their end purposes -- would be better served by another approach to philanthropy.

The ten questions in the Private Foundation Readiness Checklist are intended to help the would-be philanthropist and the advisor to be mindful about the philanthropic choices.

10 Questions: Discover Whether a Private Foundation is for You!

Private foundation readiness checklist (PFRC)

Question	*Yes*	*No*
1. Do you have an existing or intended charitable purpose?	☐	☐
2. Do you donate 5% or more of your net income?	☐	☐
3. Do you want to be in the business of philanthropy?	☐	☐
4. Will your foundation ultimately have C$4 million in capital?	☐	☐
5. Do you want to be directly involved and collaborate with the causes you support?	☐	☐
6. Do you plan to involve/include family members?	☐	☐
7. Will your foundation be active in 25 years?	☐	☐
8. Do you have the skills, talent and appetite to operate a philanthropic business?	☐	☐
9. Do you enjoy being in control?	☐	☐
10. Do you think charities should be accountable to funders?	☐	☐
TOTAL	☐	☐

If you or your client answered YES to at least 7 questions, a private foundation may be the structure to consider.

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The Private Foundation Checklist: Background Information and Assumptions

1. Do you have an existing or intended charitable purpose?

This question assesses if your client has given any thought to charitable objects or mission. Private foundations are charities, not just another personal trust or holding company, and there should be some glimmer of charitable intent at inception. Especially in jurisdictions where tax incentives are significant, there is a danger that the private foundation will be sold as just another tax exempt investment account. A foundation without charitable intent is like a yacht without a rudder.

The charitable vision does not need to be grandiose or well articulated. There is an inherent danger in defining the purpose of the foundation too narrowly at the time of inception. Ideally, private foundations should be dynamic entities that respond to the world around them. Foundations that are defined before they are tested often end up being at odds with the evolving interests of the founding generation, as well as the vastly different perspective of future generations of family directors. When coaching your client, it is often better to encourage him/her to have broad objects that can be refined and adjusted over time. For example, the foundation might consider being able both to conduct its own charitable programs and grant to other registered charities. Or the objects may be restricted to 'big-tent' purposes, such as international development, education, or the environment. We prefer that the legal structure of the foundation provide the framework for philanthropy, but never inhibit the activities. If the foundation is funded by will, it should honour the legacy of the founders, but not be so inflexible that progress is stalled. Put another way, it is better to be guided by board policy – informed by family values and social need – than limited by law and a compliance mindset.

2. Do you donate more than 5% of your net annual income?

This topic identifies existing philanthropic behaviour. It is based on the assumption that a foundation is an outgrowth of established personal priorities and actions. The best indicator of future behaviour is typically past behaviour. The 5% figure is the average amount of net income donated annually by affluent U.S. and Canadian individuals.[15] The 5% benchmark is low for philanthropic individuals and families, especially those raised in religious traditions that tithe at the 10% level. It is also a low level for many

[15] Charities – An Emerging Opportunity, Investor Economics, pg 29, Summer 2008

high net worth individuals. Canadian tax data shows this higher rate of participation. In 2006, 24% of all tax filers claimed a donation, compared to 61% of individuals earning C$100,000 to C$150,000 and 74.5% of those earning over C$250,000.

Sometimes higher rates of giving among the affluent are because of personal engagement in social sector issues, but for others it is reflection of their social circle. The wealthy are constantly being solicited and are often pressured into attending, or at least supporting, galas and, therefore, some give more out of social expectation than genuine commitment. That being said, 5% of net annual income is a significant enough level to indicate that charitable giving is a priority. The annual practice of making donations helps to provide the engaged individual with a sense of how charities operate, the causes, and best practices. Even a limited experience with charitable giving provides helpful preparation for the more intensive experience of a private foundation. Often regular giving inspires individuals to contribute in a more fulfilling and engaged fashion than they have in the past, hence the choice of a private foundation.

Paradoxically, there is a group of clients who embrace private foundations without a history of giving. Some of these individuals are philanthropists by accident[16] or personal circumstances. For example, the individual or couple without children may bequeath their entire estate to a private foundation without having a history of giving during life. The challenge can be particularly great with clients who are essentially deeply frugal at heart. Although they may be attracted by the idea of legacy and ensuring that their money does not go to family or government, they are reluctant to give their money to individual charities during life. In cases like these a private foundation provides a conceptual solution for an estate plan – and enables the client to put their affairs in order – but the actual good work of the foundation cannot begin until the donor has actually died.

3. Do you want to be in the business of philanthropy?

Private foundations are in the business of philanthropy. They exist to carry out charitable programs or to give money to other charities – year in, year out. Once a private foundation is established and funded, your client loses the ability to decide if he/she wants to give. Although the situation remains personal, it is the foundation that is in the public arena and the assets may no longer be used for personal purposes. The foundation will be solicited by charities, who will find it through online resources like Guidestar. The foundation will be solicited by friends and business colleagues. Conversely, the foundation structure and grant-making process can also regulate solicitations by putting policies, clear guidelines and an application system in place. The foundation may adopt a pseudonymous name and operate with a low profile, but there is no avoiding the core

[16] Look for an upcoming article in STEP entitled “The Accidental Philanthropist” by Burrows and Pervin.

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business. Does your client have the philanthropic maturity and seriousness to commit to a new business venture? If not, consider another giving option.

To some extent, this question is meant to be provocative. There is a popular perception, some might call it a myth, that private foundations are fashion accessories for rich people. Making a foundation analogous to a business is meant to raise the tone of the undertaking, especially for people who have run businesses. The question ideally separates the dilettantes from the engaged. Many private foundations are established at the time a family business is sold or an executive retires; often the foundation is seen as a replacement activity. Think of the high profile example of Bill Gates who was challenged by Warren Buffett to turn his attention full time to The Bill and Melinda Gates Foundation and relinquish his day job at Microsoft.

4. Will your foundation ultimately have at least C$4 million in capital?

Minimum funding amounts are one of the most frequently debated aspects of private foundation planning. Why C$4 million and not C$10 or C$20 million? The minimum value cut off can seem very arbitrary. The question is intended to test for personal commitment and self-sufficiency of the foundation after it is established. This question is often linked to question #1, namely existing or intended purpose.

The question of personal commitment is the harder of the two dialogues to explore and especially to pin down. On the emotional side, we tend to listen for passion as well as compassion, as an individual relates his/her views on altruism, social activism and sustainable directions. These people often discuss leadership and continuity at the onset, as they can often visualize the outcome with great clarity. On physical side, wealth varies greatly, and there is no ideal amount a family should dedicate to its foundation. There will be clients who devote all their wealth to a foundation and others who dedicate ten percent. To a wealthy family, C$4 million can be a rounding error – pocket change not worth mentioning and easy to leave behind without a thought. The point of the question is to examine whether the amount being considered is material. With these guidelines in mind, do not hesitate to translate this figure into your local currency or to adapt the figure to the appropriate threshold for individual clients. The amount should be significant enough to inspire the client to be focused and engaged, and to get them to think beyond a single transaction. A benchmark figure helps the client to commit to a personal goal.

The second concern relates to the self-sufficiency of the foundation, which is an issue for entities that either by design or accident often outlive the founder. Does the foundation have enough money to do some real good as a standalone entity? Is the capital base (and/or the annual contributions) significant enough both to pay for professional support and maximize charitable benefit? A small capital base will drive up costs in relative terms to a point where it becomes an ethical issue: too much is being spent on administration and too little on charitable purpose. Perhaps in these situations a donor-advised fund that is cost-effective may be more appropriate. These questions should be considered, especially if the intent is perpetual. The most efficient way of creating a neglected and ineffective foundation is to provide negligible one-off funding.

5. Do you want to be directly involved and collaborate with causes you support?

In most cases, the existence of a foundation will change the way the founder engages with charities and the community. The foundation is more likely to have a well articulated mission and to initiate strategic grants in areas of interest, whether this is formally documented or not. The foundation has the ability to operate its own charitable activities. The foundation can choose to engage in granting partnerships. While some foundations continue to give in the same way as the founder did before, charities almost always interact with foundations differently than with individual donors. The expectation is that a foundation will be a knowledgeable "funder", not just a trusting "donor". This is reflected in the greater responsibilities foundations have in law and to charity regulators.

Being a charity rather than an individual opens up opportunities for engagement with other charities and with the social sector as a whole. Private foundations provide a platform for a heightened, more formal interaction with charities. Clients should be aware that having a healthy private foundation prompts greater social responsibility and market awareness in the area of grant making and, therefore, greater interaction with society, not less. This question tests for that appetite and awareness. It also filters out the hermits.

6. Do you plan to involve/include family members?

"Feelings of worth can flourish only in an atmosphere where individual differences are appreciated, mistakes are tolerated, communication is open, and rules are flexible – the kind of atmosphere that is found in a nurturing family."

- Virginia Satir

Private foundations are synonymous with family. This question raises the issue of family engagement, while helping the founder consider just who will be involved and when the involvement will begin. Especially in the context of family business, private foundations often provide a way to engage family members not involved in the business, as well as those who are. In an ideal sense, private foundations provide a vessel (with a rudder) through which a family can act on its values and transmit those values as a legacy to future generations. Private foundations are attractive to some business families as a type of paedagogical trust where the next generation can learn about business practices, as well as philanthropy, through hands-on practice. For example, a founder may want to enable his/her children to gain experience with governance, organizing community projects, strategic decision making, managing wealth, examining risk/benefit characteristics, interacting with professional advisors, and community profile. Many founders – especially those who have been so busy with business that family has taken a back seat – aspire to ignite a 'kitchen table' style family discussion about priorities and

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community engagement. A private foundation is a living structure that requires active and often passionate engagement. It requires a different style of competency, and for many family members, it has fewer emotional and physical risks than the family enterprise.

CASE STUDY 4: COMPETENCE AND PARTICIPATION

It might have been my cousin's outburst twenty years ago, "how hard can giving away money be?" that made me concerned about giving equal access to every family member. Growing up, I always perceived him to be less competent and somewhat entitled – not a taker, but definitely not that dedicated to collaboration. At the same time, my thoughts raced to my grandfather's tendency towards inclusion and informal participation in order to embrace the broadest range of grantmaking. My grandparents were both dead and my Dad and his two siblings were trying to continue the family foundation tradition, and things were not going well. My aunt never learned how to read financial statements or comprehend investment strategies. This added tension to some of the meetings and caused tears at times. To her credit, she had passion and compassion but often lacked objectivity; she was great with people but appeared to miss many of the details and nuances, which contribute to teamwork, relationship building and collaboration; she became confused at times over the need for results and direct action rather than facilitation; and, she seldom performed any individual research into any of the organizations we supported. It's now our turn and there isn't room for 18 cousins and siblings around the table. We started to make sense of the situation and came up with the notion that it's a privilege to serve on the foundation board; it's not a birth rite! At the same time we decided that there should be a minimum level of learning attained to participate. We're getting better at this and can rely on each other in new and wonderful ways. We decided that understanding change is the core competency and that the key for change is effective communication. It looks like family unity and our giving legacy will be preserved.

The caveat about family is that there is no standard model; each family is different. Despite the romantic myth of private foundations being a place to share and reconnect around core values, it can just as often be a place where family members are shunned and excluded. In our experience, foundations often begin with the founder retaining legal and/or effective control of the foundation. The intended and sometimes mumbled plan is to include the next generation at a "later date", which is perhaps defined as when they get through the teenage years, are "old enough", or in all to many cases, after the founder is dead.

Experience confirms that reluctance to consider the role of family is often a good indicator that a private foundation might not be an appropriate structure. Please also note that this is not the only, or the most definitive, clue. But, we strongly suggest that it should cause you to pause and explore the situation in greater detail with your client, as a private foundation may make perfect sense once a better understanding of family is reached.

7. Will your foundation be active in 25 years?

As previously discussed, a classic characteristic of private foundations is longevity. Foundations frequently aspire to be perpetual. Perpetuity is an untested concept, as few foundations or endowments have survived for more than a hundred years, but it is promoted by charities and popular with donors. (In discussions with clients about the concept of perpetuity, consider defining perpetuity as at "least 100 years". It is more concrete.) Alternately, foundations can be time-limited by design. Some have best-before dates of 25 or 50 years, which may reflect a desire to maximize the foundation's resources for public benefit and/or wisdom on the part of the founder about the natural life cycle of human entities. For example, The R.S. McLaughlin Foundation in Canada had a 50-year time limit imposed by the original donor. It functioned as a granting foundation for the prescribed period, and in the early 2000s the directors went through an intensive period of granting out C$100 million for strategic purposes.

The private foundation is a structure for long-term philanthropy. As a normally tax exempt holding entity, it can build an endowment efficiently over time through investments. It can take on multi-year causes, changing strategy as it goes. It is also a long-term planning structure able to receive money over a number of years – during life and through an estate. If your client is going to take the trouble to set one up, he/she should be encouraged to define how long it will be active.

Why then test for a 25 year plan?

Our benchmark of 25 years suggests that the foundation will exist for more than a single generation. It challenges the founder to think beyond the circumstances of inception and imagine a future – to consider continuity as a family legacy. Shorter-term goals can probably be better dealt with through direct gifts or a short- or mid-term donor advised fund.

8. Do you have the skills, talent and appetite to operate a philanthropic business?

As previously discussed, in question #3, private foundations are philanthropic businesses. While it is easy enough to get administrative, professional and investment support to operate them, the directors or trustees still have a fiduciary duty to ensure they operate well. It is no accident that private foundations are typically the philanthropic choice of business owners or executives. People who have created and operated businesses typically have the skills to run a private foundation. They are more likely to be able to conduct a board meeting, read a balance sheet, and make strategic decisions.

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The other factor is appetite, which is another word for engagement. Does the founder really want to run another active entity, even one that will be significantly less taxing than the family enterprise?

The final topic is talent, which is harder for the founder to self-assess. Often the talent question applies best to the next generation of family directors or trustees. Private foundations established by people who have neither the skills nor the appetite to run them have limited success.

This topic requires you to use your intuition and provide aware, caring and respectful feedback to your client. In some situations, it is better to use a more passive philanthropic structure such as a donor-advised fund.

9. Do you enjoy being in control?

The desire for control is considered an anti-social impulse in the charitable world. That being said, control is a key feature for private foundation founders.[17] Charitable giving involves the relinquishment of control, as a donation is freely given without consideration. Control is perhaps a provocative way of asking whether the donor wants legal direction – both responsibility and authority – over his/her philanthropy. Many executives, entrepreneurs and business owners have always had a high measure of control over their business life, and could not imagine entering into a philanthropic structure where this was not the case. Private foundations need directors and trustees who provide vision and energy to fulfill their charitable mission. Excessive need for personal control will, at times, conflict with the charitable purpose of the foundation and the ethos of the charitable sector.

A related psychological dilemma that often accompanies large donations is anxiety. In its worst form, we have encountered entrepreneurs who experience panic attacks at the philanthropic moment, often just prior to the actual transition stage. Yes, altruism is a deep-rooted impulse and most philanthropists see social value in what they are doing, but there is something inherently counter-intuitive about donating millions of dollars and getting nothing in return. For clients who have spent a life in business the transition to making major donations can be very difficult. In business succession situations, we have often found that business owners feel the loss of their company. This compounds feelings of anxiety, and is often combined with a depressed state due to mourning the loss of the enterprise and the historical lifestyle and prestige.

[17] For more information, see *The Many Faces of Control Freaks* by Pervin; also visit library at pervinfamilybusiness.com

A private foundation with the founders as directors or trustees provides a philanthropic middle ground – a structure for giving that resembles the family business or the company's advisory board. They are donating their beneficial interest but retaining legal control. They take comfort in knowing they will control the foundation as they have controlled their business. Especially in business succession scenarios this knowledge enables owners to make the most significant donation of their life, often giving larger amounts than they would have to any public charity. For better or worse, private foundations sometimes serve as an important transitional step that is essential in getting charitable dollars into society.

CASE STUDY 5: PHILANTHROPIC ANXIETY OR NARCISSISM?

In our first meeting, Bruce meticulously explained his existing community work with detached passion. As only a patriarch can relate, he reported that he would send a note to the charity that read, "Enclosed please find our cheque. We will call in a few weeks and tell you what it's for". He also shared his current entrepreneurial midlife reappraisal of unfulfilled dreams and shaky career identity in a rather jocular fashion. He described in amazing detail how this current existential crisis required him to find some new 'situation' to conquer and control. He also reported on episodes of anxiety and depression brought on by feelings of vulnerability and loss of control. Bruce was not exceedingly wealthy, but he had done quite well. He (and his wife) wanted to start a foundation for a few reasons – he was motivated by tax savings, keeping passive wealth out of the hands of his adult children and an interest in effecting positive change (read: control) in the community, which experience confirms is often a suitable outlet for narcissistic tendencies. Bruce had proudly built his business from nothing to C$25 million on his own and struggled with the fundamental philanthropy concept we presented that states: "the moment the funds are foundation assets, it's not your money anymore! It's public money!" To his credit, Bruce eloquently provided a rebuttal and explained how the funds for donations come from one source – business profits. He described how the idea of putting his money in the foundation was the same as giving his money to the foundation. He explained how he and his family would give up potential dividend income for the sake of a charitable cause – something he may find easier to do if he could preserve ongoing control and oversight. It was clear he needed action in his philanthropic endeavours. People like Bruce often end up working on site with the people and community effort they fund.

10. Do you think charities should be accountable to funders?

Within the charity system, grantors (like private foundations) provide checks and balances. Private foundations are separate funders, often providing significant support, that are typically not tied to a single charity. They can grant on the basis of outcomes or

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effectiveness. They can increase funding to the exceptional charities and cut off funding to those that are less successful. By contrast, large gifts to public charities often end up being endowed, which creates a perpetual income stream and sometimes little accountability on the part of the internal recipient. (It makes little practical or legal sense for charities to be rigidly accountable to the original donor many years after the donation was made, although large institutions are becoming adept at keeping donors informed and involved.)

CASE STUDY 6: CLARITY OF MISSION CREATES THIRD GENERATION DREAM

As the last second-generation foundation Chair, Harry knew that it was time to discuss grant-making continuity with the clan. He understood that it was critical to allow the original foundation direction to maintain its rightful place in the family legacy while the third generation foundation members re-focus the philanthropic direction. Harry discussed this situation with everyone for months and then presented the meeting theme and some additional questions:

- What is the future of our family's giving? Simply: why are we doing this and why am I participating?
- How can we better plan our work?
- How can we improve implementation activities?
- How can we track progress towards our collaborative goals?

Whether you visualize your philanthropic direction as a "dream"[18] or establish your private foundation by "beginning with the end in mind"[19], the most skilled, intelligent and sensitive leaders in each generation are able – or quickly learn how – to manage and negotiate both the personalities of the family members and the priorities of the foundation initiatives. The positive family foundation culture and a clear strategic mission serve to unite the family, reinforce its identity and preserve its values.

While it is important to have sustaining support for institutions such as universities, hospitals and museums, some philanthropists are concerned that this institutionalized internal source of funding creates an indolent bureaucracy. There is a school of thought that one of the structural issues with the charitable sector is that certain charities outlive their effectiveness, but because of historical support they don't outlive their support base.

[18] Kelin Gersick, *Generations of Giving* (2004) Lexington Books.
[19] Stephen Covey, Habit #2 in *The Seven Habits of Highly Effective People*, Free Press, 1989.

This question tests for the level of trust and confidence a client has in charities. Those individuals who have a high level of trust and do not expect long-term accountability should be encouraged to give direct gifts. A private foundation would be a better structure for individuals who wish to reserve the right to change their mind about their favourite charities, or wish to use strategic or venture funding to foster change, or believe that recourse and consequences are important tools in a funding relationship.

Conclusion

Margaret Thatcher was once asked to comment on the most important aspect of communication and her response was "the pause". The PFRC [Private Foundation Readiness Checklist] presented here was developed to benefit advisors in their dialogue with clients who have expressed an interest in philanthropy.

For wealthy clients at key life stages, a private foundation is often settled upon as a solution by default. Over the years, we have found that when our client is facing that moment of philanthropic transition, our technical acumen can sometimes get in the way and possibly undermine the intent or message being presented by our client. We offer that "pause" in the form of a framework or a model for understanding more about the needs of the client. We suggest that best practice would have us be less of an expert and more of a listener. In addition, the 'yes/no' script of our 10 questions allows us to suspend our own need to analyze the situation too deeply. It is more useful than using a Socratic approach and open-ended questions at the onset, as it provides the opportunity to have an insightful conversation about suitability. Truly, the outcome is to provide the philanthropic result that matches the values, priorities and dreams of the client and his or her family and to help make this legacy concept of the philanthropic planning process more 'mindful'.

Finally, we are reminded of a statement made by the author, Alex Haley: "In every conceivable manner, the family is link to our past, bridge to our future." In our words, we stress that each advisor must manage the intangibles. Do not be fooled into thinking you should only worry about what you can touch and measure. Managing the intangibles is often more important to the success of the philanthropic direction than many of the tangible goals.

This chapter merely provides a brief overview of philanthropy and an indication of the appropriateness of one option – the private foundation. The PFRC [Private Foundation Readiness Checklist] is a proven base from which an advisor may develop his/her own script – one that benefits the particular client and his/her family – and commence the sensitive and 'mindful' dialogue of philanthropic transition. In fact, it is important that the advisor help his/her client ascertain what would be a good 'fit'. Failure to mesh skills, values, priorities and experience with personal requirements, especially in relation to intangibles such as culture, commitment and style, can be counterproductive at best, disastrous at worst.

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He is on the editorial board of the quarterly journal, *The Philanthropist*, and the contributing editor of the monthly publication *Gift Planning in Canada*. In 2008, his team was short-listed for the international Society for Trust and Estate Practitioner (STEP) Best Philanthropy Team award.

As a leader in the field of philanthropy in Canada, Malcolm has contributed to new rules for gifts of public securities, donation tax shelters, and private foundations and helped create "Charitable Options", a category of stock options for charitable giving adopted by the Toronto Stock Exchange.

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