Wealth Transfer and Philanthropy

A Moderated Panel with Douglas Box and Clint Haggard

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Introduction

- There is a long tradition of family businesses working for the common good. But many family businesses underestimate how powerful an instrument philanthropy can be to unify the family, particularly across generations.
- Planning philanthropic efforts can be an opportunity to first identify and articulate family values, and then use them to make fundamental decisions for both the family business (management decisions) and the family legacy (what to change/uplift in the world).
- Effective philanthropy requires strong engagement and deep commitment as well as careful planning and sound guidance.

Structures for Family Giving

- Once the family has decided on the right philanthropic commitment, the family must choose the right organizational framework.
  - Private Foundation: A private foundation is a type of charitable organization that is typically established by a family to support charitable activities.
  - Donor-Advised Fund: A donor-advised fund is a dedicated account for charitable giving that is established by a family through a public charity that administers and owns the fund.
  - Impact Investing: Investments made into companies, organizations, and funds with the intention to generate a measurable, beneficial social or environmental impact alongside a financial return.

Advantages and Disadvantages of a Private Foundation

- Advantage: Family members can be employed or serve as members of the board.
- Advantage: Full control over grantmaking.
- Advantage: Ability to support organizations other than 501(c)(3) public charities. By following IRS procedures, donors can make grants to charitable programs undertaken by individuals, scholarship programs, and other entities.
- Disadvantage: Charitable deductions for contributions are limited to 30% of adjusted gross income for cash and 20% of adjusted gross income for long-term publicly traded appreciated securities.
- Disadvantage: Non-publicly traded contributions, such as privately held stock or real estate, may be deductible only at cost basis rather than at fair market value.
- Disadvantage: Information regarding grants is generally not confidential, as filings are public.
- Disadvantage: Investment income is subject to an excise tax of 1% or 2%.

Advantages and Disadvantages of a Donor-Advised Fund

- Advantage: Charitable deductions for contributions are 60% of adjusted gross income for cash and 30% of adjusted gross income for long-term publicly traded appreciated securities.
- Advantage: For contributions of non-publicly traded assets, the deduction can be at fair market value.
- Advantage: A donor can be totally anonymous when making grants from a donor-advised fund.
- Advantage: Donor-advised funds offer streamlined recordkeeping, because the sponsoring organization handles administrative reporting and other functions.
- Disadvantage: Donors do not have control or ownership of the fund.
- Disadvantage: Grantees are generally limited to public charities.

Impact Investing

- A family can also engage in impact investing to further a philanthropic legacy. Impact investing has four core characteristics.
  - Intentionality: Intention to have a positive social or environmental impact through investments.
  - Investment with return expectations: Impact investments are expected to generate a financial return on capital or, at minimum, a return of capital.
  - Range of return expectations and asset classes: Impact investments target financial returns that range from below market to risk-adjusted market rate, and can be made across asset classes, including but not limited to cash equivalents, fixed income, venture capital, and private equity.
  - Impact measurement: A hallmark of impact investing is the commitment of the investor to measure and report the social and environmental performance and progress of underlying investments, ensuring transparency and accountability.

Junior Advisory Boards

- To create an effective junior advisory board, a family should plan for a sustainable structure.
  - Membership Criteria: The family should choose a minimum age for involvement and decide whether to include step-children or other relatives.
  - Powers and Activities: The family should decide how much authority to give the junior advisory board, e.g., whether the board will be advisory only or will direct any grantmaking.
  - Education: The family should set an education plan for junior advisory board members. The plan should include financial literacy, site visits, and information regarding fiduciary obligations.
  - Reporting: The family should decide how the junior advisory board will report its activities to the family.
  - Final Step: The family should determine the steps to full board membership.

Other Ways to Engage Family Members in Giving

- Even without formal structure, a family can engage in philanthropy.
  - Volunteering as a family: Engage as a family with a specific charity's activities.
  - Family conversations and contributions: Meet as a family to select an annual charitable recipient.
  - Service projects: Many charities will craft a specific project for a donor family to complete over a short time frame.
  - Site Visits: Tour a charity as a family and decide as a family whether to fund it.

Pitfalls in Family Philanthropy

- Assuming that giving is easy. Effective giving requires strong engagement and deep commitment, as well as careful planning and sound guidance when warranted. The family must pay as much attention to its philanthropic initiatives as it does to its business or investment activities.
- Assuming that all family members want to be involved. Older generations may assume incorrectly that the younger generations want to become involved in family charitable endeavors. Younger generations may be overwhelmed by the requirements for participation and develop resistance or resentment toward the charitable activities. Over time, the resistance and resentment can cause significant or even irreparable damage to the family dynamics.
- Assuming everyone will always get along. All family charitable endeavors, whether connected to a family business or not, are affected by family dynamics and changing relationships. A family organization may operate by smooth consensus for a period and then may find that external stressors — such as business succession or divorce — impact the governance.
- Assuming that getting it wrong has no real consequences. In most jurisdictions, misapplication of funds and other breaches of duty can lead to real consequences for a private foundation, including in some circumstances individual board members. Where the association of the foundation with the business has been prominent, or where the family name is shared between the business and the foundation, the business can also suffer reputational damage.

Involving Outside Advisors

- Outside advisors can provide assistance in a number of different ways. They can:
  - Develop a process to engage children or grandchildren in giving.
  - Identify or develop opportunities to make a difference.
  - Explore areas of giving where the family has less expertise.
  - Get to know a nonprofit's work well before introducing the family as a potential major donor.
  - Work through the family dynamics to energize the family's giving or take it in a new direction.
  - Help to stretch dollars further through highly strategic gifts or collaborations.
  - Take care of the research, due diligence and vetting to make sure a gift will be used well and the family's name will be protected.
  - Analyzing how loans, philanthropic equity, social impact bonds, or impact investments as well as grants, might contribute to a giving strategy.