Designing Your Family's Philanthropy:
DAFs, Private Foundations, and Supporting Organizations

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A "school of virtue" – that's how entrepreneur and philanthropist Frank Hanna[1] describes the role that philanthropy can play in a family that collaborates in charitable giving. If you'll permit us to stick with the school metaphor, this white paper focuses on designs for building the campus on which your family's teaching and learning can take place.

Specifically, we will start by briefly describing three different "school campus" designs:

1. Donor advised funds,
2. Private foundations, and
3. Supporting organizations.

Then, we will compare these designs on the basis of three criteria:

a. Deductibility,
b. Complexity, and
c. Control.

Finally, we will consider a few of the many reasons why a family might choose one design over another.

<u>Potential Designs for your "School Campus"</u>

1. Donor Advised Funds

What is a Donor Advised Fund ("DAF")?

A DAF is a charitable giving account established at a DAF sponsor (which has to be a public charity). The DAF itself is <u>not</u> a standalone charitable organization; the DAF sponsor (described below) is the standalone charitable organization that is exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code ("Code") and responsible for ongoing administration and compliance.

What type of entity sponsors DAFs?

Any public charity can sponsor a DAF, but the largest are public charities that are affiliated with financial services firms, such as Fidelity Charitable and Schwab Charitable. Other common DAF sponsors are national charities (such as National Philanthropic Trust and American Endowment Foundation), community foundations that tend to be regionally focused (such as Silicon Valley Community Foundation, Tulsa Community Foundation, and Greater Kansas

[1] Frank J. Hanna III, *What Your Money Means and How to Use It Well* (The Crossroad Publishing Company, 2008), pp. 153 – 173.

Community Foundation), and religiously affiliated charities (such as Jewish Communal Fund, National Christian Foundation, and Knights of Columbus Charitable Fund).

When assets are contributed to a DAF, the DAF sponsor becomes the owner of the assets, and the donor generally is entitled to a charitable deduction.

What makes a DAF "donor advised"?

A DAF is called "donor advised" because, even though the DAF sponsor is the owner of the assets, the DAF sponsor allows the donor or someone designated by the donor (the "advisor") to make *non-binding recommendations* regarding how the assets held in the DAF will be invested and/or granted.

How can you use the DAF as a "school of virtue" for your family?

Although the DAF does not have a board and officers, you can approximate the experience of governing your own charity by creating a family grant committee to discuss giving priorities and specific grant recommendations. Additionally, many DAF sponsors allow you to designate multiple users for portal access so that your family members can recommend grants that you have a chance to review before submitting them to the DAF sponsor.

2. Private Foundations

What is a Private Foundation ("PF")?

A PF is a standalone charitable organization (typically, a corporation or charitable trust; depending on your state, perhaps a limited liability company) whose exemption from federal income tax under Section 501(c)(3) of the Code must be recognized by the IRS. There are different types of PFs; for our purposes, the discussion that follows will focus exclusively on what are known as *private non-operating* (*i.e.*, grant-making) foundations.

What makes a PF <u>private</u>?

Typically, a PF is funded by a single individual, family, or company. Those that are funded by a single individual or family are also sometimes called *family foundations*.

Additionally, a PF can remain permanently under the control of the founders and their designated successors.

What makes a PF <u>non-operating</u>?

A *private non-operating foundation* is one that does not have direct charitable activities (such as operating a school or hospital or providing direct services to the poor), but instead provides funding (typically in the form of grants, but sometimes in the form of loans or investments) in support of organizations or activities (or, in some cases, even individuals) that further the PF's charitable purposes.

How can you use the PF as a "school of virtue" for your family?

PFs are standalone corporations, trusts, or limited liability companies (depending on the applicable state laws). Thus, you and your family members can serve as board members and officers who actually run the PF. The PF can hire advisors to assist with administration and compliance to relieve you and your family of many of those burdens. Subject to compliance with applicable law, you may make the grant and investment decisions for the PF independent of any third-party oversight. Additionally, subject to compliance with applicable law, in some circumstances the PF can actually employ family members for reasonable compensation, provided that their work directly furthers the PF's charitable purposes.

3. Supporting Organizations

What is a Supporting Organization ("SO")?

A SO is a separate charitable organization (typically, a corporation or charitable trust; depending on your state, perhaps a limited liability company) whose exemption from federal income tax under Section 501(c)(3) of the Code must be recognized by the IRS. There are three different types of SOs; for our purposes, the discussion that follows will focus exclusively on what are called *type I SOs*, which are "operated, supervised, or controlled"[2] by one or more public charities.

What makes a SO <u>supporting</u>?

A SO must support one or more public charities by being organized and operated "exclusively for the benefit of, to perform the functions of, or to carry out the purposes of"[3] one or more public charities (*i.e.*, the support<u>ed</u> organization(s)). For SOs that are formed by donors, this supporting relationship usually takes the form of making grants to the supported organization or to other organizations that further the support<u>ed</u> organization's charitable purposes. If you would like your SO to grant to a broad range of organizations, the same kind of charity that sponsors DAFs often makes a good support<u>ed</u> organization.

What makes a type I SO "operated, supervised, or controlled" by its support<u>ed</u> organization?

For donor-created type I SOs, this control is often exercised by the support<u>ed</u> organization appointing a majority of the governing board of the supporting organization. For example, if the SO has a 5-person board, the support<u>ed</u> organization may appoint 2 of its staff to serve on the board and be willing to consider a donor-nominated person (such as a friend or business associate – but not a donor family member due to applicable IRS rules) as a third board member. Then, the donor can appoint the other 2 board members (one of which could be the donor). Further, those appointed by the donor can serve in senior leadership roles in the SO, such as serving as board chair and president.

How can you use the type I SO as a "school of virtue" for your family?

Like the PF, the type I SO is a separate corporation, trust, or limited liability company, so the family can be involved in running it. However, unlike the PF, the type I SO also has oversight from its support<u>ed</u> organization, which can provide help with administration and compliance. Also, like the PF, family members can serve in board member and officer positions (subject to the typical requirement that a majority of the board is appointed by the support<u>ed</u> organization). However, due to specific tax rules that apply to SOs, the type I SO <u>cannot</u> employ your family

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[2] Code § 509(a)(3)(B)(i).
[3] Code § 509(a)(3)(A).

members for compensation, though the SO can employ non-family members for compensation and family members can volunteer their time.

Comparison of Different Design Approaches

While there are many criteria on which these three "school campus" designs can be evaluated and compared, we have selected three common areas of concern for preliminary consideration.

Criterion	**DAF**	**PF**	**SO**
Deductibility	Maximum available deduction	Lower available deduction	Maximum available deduction
- *Cash*	Up to 60% of adjusted gross income ("AGI")[4]	Up to 30% of AGI	Up to 60% of AGI[4]
- *Publicly-traded securities*	Up to 30% of AGI Deductible amount = FMV at time of contribution	Up to 20% of AGI Deductible amount = FMV at time of contribution	Up to 30% of AGI Deductible amount = FMV at time of contribution
- *Privately-held securities (such as LLC or partnership interests) & real estate*	Up to 30% of AGI Deductible amount = FMV at time of contribution[5]	Up to 20% of AGI Deductible amount = Limited to basis	Up to 20% of AGI Deductible amount = FMV at time of contribution[5]
Complexity	Least complex since the assets in the DAF are owned and administered by the DAF sponsor, without need of any ongoing compliance by the donor, advisor, or successors. Although some complicated tax rules apply, these are overseen by the DAF sponsor since it owns the assets.	Generally more complex administration and compliance than a DAF or SO because the PF is a standalone charity that is unaffiliated with another charity, so donor must handle ongoing administration and compliance (or must hire someone to do it). Somewhat complicated tax rules apply that require careful administration.	Generally less complex than a PF from an administrative and compliance standpoint because the supported organization often provides administrative services (for a fee), but more complex than a DAF because it is a separate charitable organization. Although some complicated tax rules apply, these are often overseen by staff from the supported organization.
Control	Least amount of control since the advisor is limited to making recommendations about grants and investments.	Most control because PF can remain permanently under the control of the founders and their designated successors	More control than DAF but less control than PF because the supported organization technically controls through appointment of board majority. Donor still can exercise significant control through senior leadership positions such as board chair and president.

[4] Through 12/31/25. The increased deduction was enacted under the Tax Cuts and Jobs Act of 2017 ("TCJA"). As of January 1, 2026, the maximum deduction for cash contributions will be reduced to 50% of AGI in the year of contribution with up to 5 years to use any amount not used in the year of contribution (*i.e.*, a carryforward). Note that some states, such as California, did not conform to the deduction limit increases under the TCJA; thus, there is still only a 50% of AGI California income deduction for cash contributions.
[5] As determined by a "qualified appraiser" as defined in Section 170(f)(11)(E)(ii) of the Code.

Final Thoughts

Which campus design is best to house your "school of virtue"? For many, the DAF can be a great way to start because of its ease, but that won't necessarily be the right answer for your family. Each situation must be evaluated separately.

For example, if you wish to contribute some of your operating business to be held by your charity for ongoing cash flow, neither a DAF nor a PF will work due to certain applicable tax rules, so you may want to form a type I SO.

If you want to contribute highly-appreciated real estate that has zero basis after years of depreciation before a sale, a PF may not make sense since you won't get a deduction. But if you don't want others overseeing your philanthropy in any way and only plan to contribute cash and publicly-traded stock, a PF may be the way to go.

If you want to make periodic contributions of cash and publicly-traded securities and don't want to complicate your life with additional board meetings and administration, the DAF may be the right fit.

At most schools, campuses change over time, and the same can be true for your philanthropic design. A structure may perfectly fit your needs during one season of your family's life; then, over time, your needs or desires may change, and another structure (or multiple structures used concurrently, such as a DAF along with a PF or type I SO) may better serve your family's philanthropic goals.