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# Establish a Family Foundation



A Proven Plan to Save Taxes,  
Establish a Family Legacy,  
and Serve Your Community




The Stewardship Institute

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## Introduction

 Everyone is looking for ways to increase their estate. Setting up a Family Foundation is one way of achieving that as well as “doing well” by “doing good.” You can substantially reduce your income tax burden this year. That means you may be able to reduce lost opportunity costs and significantly increase your estate.

Most estate planners acknowledge that there are two tax systems, one for the informed and another for the uninformed. The same is true with charitable organizations. With effective planning and direction you can reduce income taxes, help your community and build a permanent family legacy. You can do this by applying proven wealth building principles and creating your own Private Family Foundation.

Act now and benefit your family and community for generations to come. With your own Private Family Foundation, you’ll get more than tax savings.

With a Family Foundation you will:

- Have greater control over how your wealth is put to work.
- Have greater focus, structure, and continuity through the usage of a well thought-out plan.
- Gain tax benefits immediately, and give to your favorite charities later.
- Have full control over the assets in your foundation.
- Invest and grow assets tax-free, giving to charity over the course of many years. You will want your money to keep doing good for a long time.
- Establish a legacy. Families that plan and do charitable work together stay together. A Family Foundation is a great way for a family to make a profound statement for future generations.
- Identify and establish values with your family.
- Further your family’s mission by actively involving children, grandchildren, siblings and even parents in your charitable enterprise.

## What is a Family Foundation?

A Family Foundation is simply a private foundation funded primarily by a single donor. This is usually a family patriarch or matriarch, family members, or a small number of related donors who control and help manage the foundation. The donor may make tax-deductible gifts to the foundation. There is no income tax on the income (passive) earned by the foundation. To qualify for these tax benefits, the foundation must distribute a certain amount each year to public charities. Most foundations function as general-purpose endowment funds that the families use to make charitable contributions. Given the nature of the Family Foundation, it’s easy to involve relatives. Simply appoint them as voting members to the board, which decides what causes to support and hires whatever support personnel are required for asset management and administration. For example, younger family members might start off with little or no power to affect grant-making choices but assume greater responsibilities as they mature.

Family Foundations have long been the vehicle of choice for wealth preservation and direction. Although there are many easily recognized large foundations, there are also tens of thousands of smaller, less well known foundations that quietly and privately control, in the aggregate, billions of dollars. These dollars have created many of the great gifts that we experience in society today.

These include medical research, scholarships, providing for the homeless, teaching our youth, prevention of cruelty to life, religious activities or the





promotion of the arts. These are just a few of the areas in which society and the world at large have been positively affected by Family Foundations.

The basic activity of the Family Foundation is simple. It consists of four elements:

1. Receiving contributions from the donor.
2. Managing its assets. You may manage the assets yourself, or use one of many available professional fund managers (recommended).
3. Complying with the required forms and governmental reporting.
4. Making contributions (grants) to charities in at least the required minimum.

## Benefits of Your Foundation

There are several substantial financial and personal benefits of creating a Private Family Foundation.

- Establish a legacy bringing you closer to your children and grandchildren.
- Create fiscal responsibility by directing tax dollars to the charity of your choice.
- Improve and even save lives through charitable work funded by your family funds.

Specifically, when you create your Family Foundation:

- You benefit from an immediate tax deduction by contributing to the foundation. You can reduce your personal income taxes by up to 30% of the value of the donation.

- Your Family Foundation's assets grow exempt from income tax, so you have more income to fund your most passionate causes. Neither you, your family, nor your foundation ever pays any gift or estate taxes on assets donated to the foundation during your life or upon your death.
- You get the satisfaction of declaring your family name as "doing good" with a personal stamp on an entity that may live forever.
- You maintain control and flexibility to donate to those qualified organizations that further your charitable goals.
- Your charitable goals and desires can change at your discretion. Nobody tells you where to donate your money.
- You maintain control over the assets in the foundation throughout your life and beyond.
- You determine how the assets are invested, when to distribute funds to charity, which charities to give to, and how much.
- You can keep perpetual control of the foundation in your family, or choose successors to carry on the name and purpose of your foundation.
- Your family is involved. Charitable activities bring families together. The younger members express their values through the grant-making process.
- Your children learn how to responsibly manage money. They develop skills including understanding financial statements, agendas, conflict resolution and consensus building.
- Your children experience leadership through trusteeship.
- You experience leadership with a heart serving the common good of the community.



## Is a Family Foundation Right for You?

There's been an immense surge in giving in recent years, due partly to the immense increase in the creation of wealth. As the Babyboomers enter retirement; they do so as the wealthiest and healthiest generation of Americans in history. They have a great desire to preserve and direct the wealth they have created, and they have the good health and mobility to make it happen. The only thing missing has been the vehicle to do it with and the source of education to put that vehicle in motion. A Private Family Foundation will allow you to get a full tax deduction today, and to build wealth for both charity and your family to manage well into the future.

## Goals

If you have any of the following charitable goals, you should create a Family Foundation:

- A desire to create a permanent legacy.
- A desire to share values and vision with your children and grandchildren.
- A desire to have control of your charitable endeavors and to further your selected charitable concerns.
- A desire to maintain legal control over assets you have worked hard to create.
- A desire to freely give and yet remain anonymous.



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## How to Determine Whether You Are Financially Qualified

While a Family Foundation is a very powerful instrument, it is not for everyone. When a foundation is funded you are taking money or assets and irrevocably gifting them for charitable purposes. If you can answer YES to the following two questions, you are financially capable of creating a Family Foundation:

1. Do you have money or assets that you don't require for yourself or your family's benefit, now or in the future?
2. After determining your family's needs, wants, and obligations, are you willing to donate to a qualified charity?

## Charitable Possibilities: Situations Where a Family Foundation May Be Especially Appropriate

As much as we would all like to participate in charity ... the Family Foundation does require some economic reflection. If you experience any of these economic situations, you are an ideal candidate for your own Family Foundation:

- Do you currently give to charity?
- Do you plan to continue to give to charity?
- Do you have the income to set aside for charitable giving?
- Do you have income with a tax burden?
- Do you need a secure and prosperous retirement plan?
- Do you need a secure and prosperous estate plan?
- Do you have steady, or growing, income well above your personal needs?
- Do you own appreciated stock?
- Do you own appreciated property with capital gains?

## Immediate Income Tax Savings

Generally, you will be able to reduce your personal income tax liability by up to 30%. You would do this by transferring 30% of your pre-tax income to your foundation as a donation. Of course, you may transfer a smaller percentage, and get the corresponding smaller tax benefit. The 30% limit was established by Congress as the limit to how much you personally can reduce your taxes by donating to a qualified foundation. In other words, you can give more than 30% of your income to the foundation, but you can only deduct up to 30% of your income in a given year. If you donate more than 30% to your foundation you can use the excess portion of the deduction in future years. You have five years to carry over the deduction until it is exhausted.

## 4 The Advantage of Giving Appreciated Stock

You can donate cash to your foundation. You can also donate appreciated stock of a publicly traded company and get a deduction. If you own appreciated publicly traded stock, you will owe capital gains tax when you sell it. However, if you donate the stock to your foundation, you do not owe capital gains tax, but you do get an income tax deduction for the fair market value of the stock. Donating appreciated stock to your foundation can boost your tax savings considerably, because the foundation has no capital gains tax and never will.

## Your Family Foundation Allows Time

There is an increasing desire among individuals and families to play a vital role in our society. Besides the benefit of an immediate tax deduction, you have years to determine where these moneys can best be directed for charitable use. Family Foundations and private philanthropy fill that role. The Family Foundation buys you time.

Large gifts to charity are serious business. No matter what the charity is, it deserves your thoughtful attention and demands your utmost scrutiny.

Consider the possibility of your own Family

Foundation. Once money and or assets have been legally gifted to your foundation, you are required to expend 5% of the net investment value to charity each year. In effect, you maintain control of the fund as long as you want. Forever, if you desire. And all the while the financial rating of the foundation increases free of income taxes.

As you have more time in the future, and as you refine the grant making process to meet your goals, you can, of course, increase your giving. Statistics among our clients show an average annual contribution of 17% of the earnings of the foundations they manage. Why? The answer should be obvious. Your Family Foundation provides the flexibility you need now to borrow time from the future.

## How a Family Foundation Can Be Used Most Effectively

Remember:

1. You receive an immediate tax deduction for contributions of cash or appreciated stock to your foundation.
2. The assets (financial rating) of the foundation increase without income tax (may be an excise tax on certain investment income).



3. The assets donated to the foundation are not subject to gift or estate tax. Any time you have charitable interests, high current income, liquid assets or appreciated stock, a Family Foundation should be considered.

The value of making such contributions is illustrated by the following examples:

### *Example 1: Income Tax Benefit in a Single Year*

In any given situation, creating a Family Foundation will usually result in both an immediate and a longer-term increase in net assets for you and your foundation. The immediate increase results from the immediate income tax deduction you receive. For example, suppose a person in the 45 % income tax bracket has \$1,000,000 of income, and is considering whether or not to make a \$300,000 contribution to his foundation (30% limit).

If he does not make the donation, he will be taxed on the full \$1,000,000. He will pay \$450,000 in taxes, leaving \$550,000 of assets.

If he does make the contribution to his family foundation, he pays tax on the adjusted \$700,000 of income. His income tax now drops to \$315,000, a decrease of \$135,000, and his total assets, both personal and foundation, increase by that same \$135,000. By making the contribution he controls total assets of \$685,000, instead of just \$550,000. The significance of this scenario is the recovery of lost opportunity costs (135,000). This represents not just \$135,000 but  $(\$135,000) \times (\text{a return}) \times (\text{years})$ .

### *Example 2: Income Tax Benefit Is Greater When Appreciated Stock is Gifted*

In example 1, the person was assumed to have given cash. The income tax benefit would be even greater if he instead donated appreciated stock. For the sake of example, assume that the person gives \$200,000 of stock (appreciated property is limited to 20% of contribution base, which equals AGI in most cases) and has a basis of \$50,000, and \$100,000 of cash. His income deduction is still \$300,000 and saves him \$135,000 of income taxes. But he also avoids a capital gains tax on the \$150,000 of unrealized appreciation. At a 20% capital gains rate, he saves another \$30,000 of income taxes.

### *Example 3: Income Tax Advantages Over Time*

Over time, the advantage of the foundation increases because Family Foundations are not subject to income tax. Properly managed, foundations pay only a minimal excise tax of 2 % on investment income. Let us illustrate the effect of these tax savings by expanding the previous example.

Suppose the person is 55 years old, and has assets of \$12,500,000, which return 8% a year net pre-tax, giving him \$1,000,000 of income. Also assume that each year he contributes 30% of his income to his Family Foundation. The foundation earns 8%, makes the required minimum annual distribution, and pays excise taxes of 2 % of investment income, and foundation management fees of 1 % (optional but typical fee) of assets. After 27 years (his life expectancy) his net worth will be \$27.7 million, and his foundation will be worth \$20.8 million, for a total of \$48.5 million.

Contrast that situation to one in which the person has no foundation. During the twenty years he makes the same charitable contributions as his foundation would have made. He will have \$35.2 million after 27 years. Thus, during his life, he can increase the assets under his control by over \$13.3 million just by funding his Family Foundation annually.



### *Example 4: The Estate Tax Advantage*

The fact that the foundation is not subject to estate tax can also be important in building and sustaining assets over time. In the example above, assume the person dies at the end of year 27, and leaves no additional assets to charity. Estate taxes would take 55% of the amounts not in the foundation. The amount in

the foundation would not be affected by estate taxes. In the case where the person had not funded his foundation during his life, he would leave 25% of \$35.2 million, or \$8.8 million to his foundation. That would leave a taxable estate of \$26.4 million, of which the estate tax would take \$14.5 million or 55%. This leaves just \$11.9 million to his heirs.

In contrast, in the case where the person has funded the foundation annually, the foundation already has \$20.8 million, or more than twice what it would have if he waited. At his death, he leaves his entire estate of \$27.7 million, less taxes, to his heirs. After paying estate taxes of \$15.2 million, the heirs receive \$12.5 million, more than they would have received without annual funding of the Family Foundation.

## 6 Philanthropic Considerations

Family Foundations have proven over time that they are vehicles for some of the most humanitarian and progressive acts known to society. A Family Foundation is an opportunity to go beyond providing for charitable areas into which governmental institutions cannot or should not advance. Family Foundations are uniquely qualified to initiate thought and action, experiment with new and untried ventures and act quickly and flexibly. As in any business or personal endeavor where goals exist, the more time and effort you put into it, the more effective you will be in achieving your charitable goals.

Creating a Family Foundation will expand your charitable vision. Your family's mission will be clear and easily understood. Your family will have profound purpose and be supported in a giving culture. The influence that your family can have on society is limitless.

A Family Foundation fortified with vision and a sense of mission that is clear and so inspiring is the embodiment of stewardship. Living principles of stewardship is the universal trend for the future. Stewards are always a part of the solution. Families living in stewardship, exercising their decision making power through charity, will preserve Significant Living.

## The Stewardship Institute's Vision, Values and Educational Program

In today's business world consisting of dot coms, mega-mergers, right-sizing and phone menus, the primary concern of most organizations is directed toward financials, sales, profit margins and the like. The family is often no different.

At The Stewardship Institute the interest in families and their education is our foremost activity. *Moving beyond success to significance* is more than a company's motto or credo. It is the movement beyond success and output to significance and measurable outcomes. This directive reflects the personal philosophy of the dedicated people who embody The Stewardship Institute.

Conceptually the Family Foundation is simple. The principles of stewardship are self-evident. The education required to be a successful and productive foundation is vital. The Family Foundation is a dynamic tool that allows the family to plan, develop and implement ambitious philanthropic projects. The Stewardship Institute provides a hands-on approach to teach principles of stewardship and philanthropy. Family traditions are honored and expanded. The educational programs provided encompass values that are essential to charitable living. The understanding and implementation of these values are found in the acronym; ART: Accountability, Responsibility and Trust. Your family will discover the empowerment and joy that comes by serving others. When families are in the service of their fellow beings ... they are true stewards.





## Investing Your Family Foundation's Assets

Creating a Family Foundation is easier than creating wealth. The concept is also simpler to understand. Creating a Family Foundation is like moving money from your left pocket to your right pocket. You maintain full control over the assets.

- You can keep your foundation's bank or brokerage accounts with the same bank or broker you use now, so there's no need to actually send your money anywhere.
- You can continue to enjoy the help of the same trusted investment advisors you currently use, or you can manage the assets yourself.
- You maintain full control over how the foundation's assets are invested.

## Key Rules That Every Trustee Should Know

Although the benefits of a Family Foundation are many, and the activity of a Family Foundation is conceptually simple, the compliance and accounting aspects need to be understood and implemented. The Stewardship Institute provides the necessary training for you.

Foundations were not defined by the Internal Revenue Code or any Federal Statute until 1969. The resulting definition is as follows: "A non-governmental, nonprofit organization, with funds and programs managed by its trustees or directors, and established to maintain or aid social, educational, charitable, religious, or other activities serving the common welfare."

Therefore, it is Congress that, by statute, has defined the categories of organizations that are eligible for tax exemption and it is Congress that, by statute, has determined whether a tax exemption should be continued.

To minimize potential abuse Congress has placed a number of restrictions and requirements on Foundations. The rules are fairly straightforward. Although all private charities must follow the rules, in practice the real impact of the rules is to simply create the appropriate paper work and disciplines to be successful. The following is a list and brief description of the most important of these requirements:

1. No "self-dealing."
2. No "excess business holdings."
3. No "jeopardizing investments."
4. Must make annual distributions.

The necessity for these requirements is obvious: To ensure the success of your charitable endeavors, follow the rules.

### *Rule Against Self-Dealing*

Generally speaking, the prohibition on self-dealing means that disqualified persons, generally the founder, parents and children, and people under their employ may not engage in any transactions with the foundation, except to make donations to it or, under limited circumstances, to receive fair market value for services. These rules are detailed in IRC Sec. 4941.

In general, a donor is never allowed to receive an improper benefit from a charity he or she supports. A disqualified person may not:

- Use the foundation's assets or its income for his or her personal use.
- Borrow money from the foundation.
- Buy things from the foundation or sell things to it.
- Keep foundation assets (e.g. paintings) on his or her premises.



A disqualified person is allowed to have certain “arm’s length” dealings with the foundation. The founder and his/her family may receive reasonable trustee/director fees (provided they do not receive preferential treatment), and the donor and/or family members may be employed provided that their compensation is reasonable for work actually performed.

### *Excess Business Holdings and Jeopardy Investments*

A set of rules concerning “excess business holdings” is designed to keep a Family Foundation from owning a significant stake in a family business. In general, founders should not allow their foundation to own any part of the family (or other closely held) business. Technically, very small stakes in such companies are allowed (20%). See IRC Sec. 4943.

### *Prohibition on Jeopardy Investments*

The prohibition on jeopardy investments will rarely come into play. It is very unlikely that this prohibition would ever be a factor as long as the assets of a foundation were being managed prudently. See IRC Sec. 4944.

### *Requirement to Distribute Income*

Family Foundations are required to distribute a certain amount of assets to qualified public charities each year. Generally, the amount is 5 % of average net investment assets, less certain foundation costs and expenses.

Generally, the distributions must be made in the year following the year upon which they are based. This assures that there is time to calculate the required amounts, and to make effective decisions about the required distributions. These rules are detailed in IRC Sec. 4942.

### *Tax Reporting*

Even though the Family Foundation is tax exempt it is still required to file a tax form with the IRS. A Private Family Foundation files Form 990PF annually. The requirement to file a tax form means that records and accounting must be maintained as would any enterprise.

## The Stewardship Institute Makes It Possible for Families to Have Their Own Foundation

Creating and running your family foundation is easy once you understand and have the right help. All you need to do to acquire this knowledge and help is to make three decisions:

1. Decide whom you want to serve on the board. All you need is one person. We recommend at least two. This board should consist of you, your spouse, and family members if you desire.
2. Decide when you want to get started. Contact TSI and register for the Stewardship Workshop. The funding of your foundation remains private and is only known by those whom you designate. Creating your Family Foundation in one year does not require you to contribute to it in future years. You never have to give to your foundation again if you don’t want to. Of course, you can contribute as often and as much as you like in any one year or subsequent year.
3. Decide what you want to name your Family Foundation. Typically this is the family name but you can be creative in this area.

At TSI, our goal is to educate you and your family in such a way that the benefits of a Family Foundation are realized immediately. When you leave the Stewardship Workshop your Family Foundation is up and running.

Establish  
a  
Family  
Foundation

## Conclusion

There are tremendous benefits available to you and your family when you decide to create a Private Family Foundation. These benefits are actually too numerous to review here. Nevertheless, you will experience immediate tax advantages, and the fulfillment of knowing that you are contributing to a better world. A Family Foundation is a virtual learning center. It provides structure and purpose for your charitable endeavors. Your family will be empowered by exercising thoughtful grant-making. The Family Foundation maintains control over your assets. Through education, hands-on experience, and personal involvement, your family will experience the benefits that can only come from charitable work. That's why there is a surge in the number of Family Foundations being established.

## How TSI Can Help You

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**T**he Stewardship Institute is in business to provide learning opportunities that contribute to the betterment of the family. TSI invites you to participate in an Educational Program that will teach you to reorganize and manage your charitable interests in trust, thereby giving you greater control over your assets and your family's future and financial destiny. This Educational Program acknowledges that Family Foundations have been used for generations to preserve assets and benefit mankind. TSI's Stewardship Workshop, however, is unique because every strategy and procedure has been verified in current laws, regulations and codes. We teach that "honoring and sustaining the law" means understanding and knowing the law. It is the only way to effectively build a generational plan that will accomplish your family's charitable goals.

There are a select number of families who have always used trusts and foundations and have chosen to keep information about their charitable activities private. TSI gives you an opportunity to learn and implement the same financial strategies at a cost that is within the reach of small businesses and mainstream families.

Through a series of hands-on workshop programs, TSI provides you with the on-going education you need to create and administer a Family Foundation. This educational program is recognized by tax and legal professionals as the best way to create a legacy receive immediate tax benefits and build a generational plan that empowers the family while benefiting society.

There is simply no better way to describe TSI than to say we are committed to helping others by strengthening the family unit through the usage of the Family Foundation. That which lifts anyone out of the oppression of ignorance is education. TSI has assisted hundreds of families in the process of creating the required paperwork to establish a Family Foundation. TSI provides the organizational and administrative tools so that family members become responsible stewards, capable of managing, giving and moving beyond success to lives of significance.



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