

## Weighing the Options ©

Council on Foundations and Community Foundations of America

*Benjamin Franklin knew the value of money- and time. In 1791, he left \$5,000 to the citizens of Boston to invest for 100 years. In 1891, a portion of the appreciated assets established the Franklin Institute, with the remainder left to grow for another 100 years. In 1991, the balance of the Franklin money-by then \$5 million-was used to benefit the Boston community.*

Not everyone has the vision of Ben Franklin, but many philanthropists know that a wise decision today can make a world of difference tomorrow.

What does it take to start a private foundation today? Experts say commitment, time and money. Commitment and time requirements are high, but just how much money is a matter of debate. In theory, any amount is possible. In practice, many underestimate the amount needed to operate efficiently, both in terms of the charitable asset and ongoing operating costs.

### Money

Gift size. How much is enough? Two hundred years ago, \$5,000 was an ample sum. More recently, \$1 million was considered a sufficient base.

But benchmarks change. For small foundations, operating expenses are often out of sync with the dollars actually reaching charities. Unless much of the work is done by a volunteer founder, some experts say it takes a charitable gift of about \$5 million to establish and operate a private foundation efficiently. Despite this, of the 1,000 new private foundations established each year, about two-thirds have assets of less than \$1 million.

Operating efficiency. In the world of private foundations, bigger is usually more efficient. First, the most basic level of administrative support is essentially a fixed cost. Regardless of the asset size, few private foundations can operate without minimal administrative services. Without a pro bono arrangement, the foundation must pay for staff or professional services to handle administrative, financial, and legal work.

Second, the greater the asset, the greater the opportunity to actively manage a diversified portfolio of individual stocks. Given market performance in recent years, most investment experts stress the value and necessity of diversification across classes.

Consider the potential expenses for a \$1 million foundation that wishes to preserve an endowment and pay out 5% of net assets:	A larger foundation can operate more efficiently. Assuming incrementally higher administrative costs, consider the potential expenses for a \$10 million
---	--

Example One			Example Two		
Total Payout	5%	\$50,000	Total Payout	5%	\$500,00
Operating Expenses		\$15,000	Operating Expenses		\$100,000
Available For Grantmaking (up to 5% payout)		\$35,000	Available for Grantmaking (up to 5% payout)		\$400,000

In these examples, operating expenses for grantmaking consume a significant portion of the total payout. Increasing the payout for grantmaking is an option, but many private foundations are concerned with preserving principal and generating asset growth. A higher payout could jeopardize their permanence.

Recommended asset size of three major philanthropy options

- Private foundation: \$5 million or more
- Supporting organization: \$2 million or more
- Donor advised fund: \$10,000 or more; \$50,000 or more to endow

*The economies of scale and resources that a community foundation can offer may be critical for smaller foundations.*

Rhian Evans

Senior Advancement Officer

Arizona Community Foundation

### **Alternatives**

For those who want to give, but are not comfortable with the demands of a private foundation, two practical alternatives are available: supporting organizations and donor advised funds.

Supporting organizations. A supporting organization is the closest thing to a private foundation, with a fraction of the administrative requirements. Donors establish supporting organizations through community foundations or other public charities. The organization that is created is legally separate but affiliated with the parent charity.

The founding donor of a supporting organization appoints 49 percent of the board members, with the rest appointed by the charity. This arrangement also offers the prestige and involvement that make private foundations attractive to many philanthropists. The community foundation or charitable partner handles startup and other administrative tasks. Ongoing costs are minimized through the community

apply.

Donor advised funds. When a client has less interest in controlling certain aspects of charitable management but still wants a hands-on giving experience a donor advised fund might be the best option. Administration and investment are pooled with those of other funds at the public charity, and the donor can recommend grants to the organizations board of trustees. Grants are issued in the name the donor chooses for his fund (or anonymously if the donor wishes).

Today's high net worth individuals share a lot in common with their predecessors. They want to give. They want to start a legacy. And they want a good value. Private foundations, supporting organizations, and donor advised funds are attractive giving options but no one of these options is right for every donor.

As Benjamin Franklin famously advised, A penny saved is a penny earned. With his own legacy, Franklin demonstrated that by planning deliberately and investing wisely, he was able to create the giving solution best for him.

Copyright 2005, Council on Foundations and Community Foundations of America  
Used with permission