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Considerations in Choosing a Grantmaking Vehicle

Two popular grantmaking vehicles are private foundations and donor-advised funds (“DAF”). While both allow donors to make tax-deductible contributions and make grants to nonprofits over time, there are meaningful distinctions:

1. How much control do you want?

A private foundation is an independent entity with its own board and governing documents, while a DAF is affiliated with a sponsoring nonprofit. As such, private foundations allow donors considerably more control, making it easier to institutionalize philanthropy within the family—and involve multiple generations. DAF donors, alternatively retain advisory privileges for distribution of the assets. While the IRS requires that foundations grant out at least 5% of net assets annually, DAF distribution requirements are set by the sponsoring organization.

2. Not all charitable contributions are created equal.

The IRS treats DAFs as “public charities,” allowing DAF donors the most favorable tax treatment. For example, contributions of special assets like real estate, restricted stock, and private business interests to a DAF may be deducted at fair market value, whereas a private foundation would limit the deduction to the donor’s cost basis in the assets they are contributing.

3. Private foundations’ activities are public record.

Private foundations are required to file annual tax returns. Anyone can research the grants a foundation has made, its total assets, donors and contribution amounts, board members, and any compensation received from the foundation. Conversely, DAFs are not required to identify donors, and grants can be made anonymously.

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4. What does it cost to get started and to maintain?

Establishing a private foundation entails forming a new legal entity and obtaining tax-exempt status. Once established, a foundation must file annual tax returns, pay excise tax on net investment income, and ensure it is compliant with all other ongoing legal obligations. These requirements come at a cost in the form of accounting, legal, and filing fees. DAFs generally do not have up-front costs, but the nonprofits administering them do collect annual administration fees and investment fees. For these reasons, private foundations are generally recommended at higher contribution levels.

5. DAFs and private foundations are not mutually exclusive.

It is increasingly common for private foundations and foundation trustees to establish DAF accounts as a complement. Some foundations use DAFs to achieve a higher degree of privacy with respect to grantmaking. Others use DAFs to give trustees the flexibility to support nonprofits that do not necessarily align with the foundation's funding priorities, or to expose the next generation of leaders to philanthropy before they join the board. Smaller foundations may benefit from winding down and converting to one or more DAF accounts. Although private foundations can transfer assets to DAFs, DAFs generally may not transfer assets to private foundations.

If you have further questions, don't hesitate to contact your Relationship Team or email us at Top5@glenmede.com.