

# Painting Your Canvas: Where to Begin?

~ Doug J. Elmore

Your charitable endeavors are helping to paint your legacy, a legacy embodying honored values and an enduring vision. You have decided to create a private foundation to cement this legacy and to perpetuate your values and vision beyond your lifetime.

In many ways, you have a blank canvas on which to structure your private foundation. Given this degree of flexibility, how do you get started? Without question, a broad spectrum of considerations is in play. By addressing some of the essential design issues outlined below, however, you should have the blueprint for a private foundation that expresses your charitable intent, furthers your philanthropic goals, and sustains your values well into the future.

## Designing the Charitable Purpose

The heart of your private foundation is its charitable purpose. The charitable purpose is a narrative describing the foundation's ideals, objectives, and activities. A key component of the narrative is the foundation's mission statement. The narrative may also pinpoint core values, initiatives, and methods of collaborating with other charitable organizations. In addition, the narrative may identify specific organizations or causes that you intend the foundation to benefit. Your foundation's charitable purpose may even include a statement of your family's giving philosophy.

Your foundation's charitable purpose is critically important to its day-to-day operations and the perpetuation of its existence. Not only does the charitable purpose help shape your foundation's distribution policies and activities, but it becomes the cornerstone of your foundation's identity and its role in the community. Long after you have passed away, the charitable purpose will be a lasting reflection of your intent. It becomes a guidepost for the future stewards of the foundation, providing a set of values and parameters that help steer the evolution of your foundation over time.

Designing a charitable purpose is not necessarily an easy task. You have a great degree of flexibility, with the only real restriction being that you observe the tax rules. This degree of flexibility can be beneficial, but it can also make it difficult to know where to begin.

Ultimately, you are the lead architect of your private foundation's charitable purpose. By working closely with your advisors, you should be able to craft a charitable purpose that provides a framework for grantmaking and operations. Among the questions you should answer in constructing your foundation's charitable purpose are the following: (i) What are the foundation's overarching goals? (ii) Which aspects of your own ideology and which personal or family values would you like to see reflected in the foundation's activities? (iii) Which charitable needs would you like the foundation to support? (iv) Should the foundation benefit or support the work of any existing exempt organizations or perform direct charitable work? (v) Should the foundation specifically forgo any charitable purposes?

Private foundations are typically structured to be perpetual. But that doesn't mean that your foundation has to remain in existence forever—it depends on what you seek to accomplish. If you envision your legacy as the thoughtful stewardship of family resources for charitable purposes long into the future, then a traditional foundation with perpetual existence is likely to appeal to you. If you prefer to make a big splash that will have a lasting impact that your children and grandchildren can witness, you could consider different approaches. One approach may be to require the distribution of the foundation's assets within a particular time frame (such as 20 years after the death of the founder or within a certain number of years of the death of the last surviving family member in a particular generation). Allowing the board the discretion to make large grants for signature charitable accomplishments, even to the point of exhausting the foundation's assets, may be appropriate in certain circumstances.

In designing the charitable purpose, be forward-looking. Consider the possibility that one of your objectives may become impracticable or impossible to achieve. Also consider that one of your preferred grantee organizations may no longer exist or may cease to exist in the form to which you are accustomed. In addition, you should articulate your charitable purpose with an eye toward how it may be interpreted by future generations, based upon changing societal perceptions, values, and needs. So as to facilitate the future interpretation of your charitable purpose, consider documenting in a separate letter or policy statement a detailed statement of your philosophy, highlighting how it differs from current, prevailing views and ways that it might be affected by changing societal perspectives.

You may also want your foundation's charitable purpose to be adaptable. Toward this end, you could provide for the amendment of the charitable purpose through a vote of the foundation's governing body or institution (herein, the "board"), certain family members, a committee, or an independent third party (or some combination thereof). While this flexibility could possibly dilute your foundation's specific charitable purpose, the power to amend can be counterbalanced by the level of control you wield over the governance succession plan or over the persons having the power to amend. Moreover, you can limit the power to amend by tailoring it to be applicable only in a narrow set of circumstances.

Related to the design of your charitable purpose is whether your foundation will be a private operating foundation or a private non-operating foundation. A private operating foundation is a foundation that directly carries out its own charitable activities or program instead of making grants to other charities. Under the Internal Revenue Code, a private operating foundation must expend substantially all—at least 85 percent—of its net investment income directly for the active conduct of its charitable activities. Some museums and libraries are structured as private operating foundations.

By contrast, the central focus of a private non-operating foundation is grantmaking to other charitable organizations that actively provide services to end users. A private non-operating foundation generally does not directly operate charitable services or activities. These foundations are typically endowed by a single donor or family and, therefore, tend not to be active fundraisers or grant seekers.

In general, the nature of your foundation's charitable purpose will drive the analysis of whether it is a private operating foundation or a private non-operating foundation. In practice, most of the private foundations we structure and represent are private non-operating foundations. This article is geared toward this more popular form of a private foundation.

## Enforcing Your Charitable Purpose

Another important design issue is the enforcement of your charitable purpose. First, you should know that there is no perfect way to ensure that your charitable purpose will be honored by future boards. Moreover, as illustrated by several recent cases involving nationally renowned private foundations, there is also no guarantee that a court of law will strictly enforce your foundation's charitable purpose.

With that said, you may be able to structure your foundation to have an enforcement mechanism to discourage or remove from office a trustee or director who departs from your articulated purpose. For example, if your foundation is structured as a trust, you could provide for a committee advisor with the ability to remove and replace a trustee with or without cause. If your foundation is instead a not-for-profit corporation, you could structure the entity to have founding "members" who have broad powers to control the board and whose approval is required to change the governing documents.

Incorporating an enforcement mechanism is a multifaceted area of foundation design, and you should work closely with your advisors if this is one of your goals. Among the issues you may need to grapple with are the following: (i) Who or what entity will have authority to enforce the foundation's charitable purpose? (ii) What legal basis and legal standing will such person or entity have to enforce the charitable purpose? (iii) In what jurisdiction will such person or entity enforce the charitable purpose? (iv) How will the succession of persons or entities charged with enforcement be structured?

## Governance

Designing effective governance is one of the most important tasks in establishing a private foundation. Effective governance is rooted in a practical board structure and a board composition suitable to your foundation's charitable purpose.

As to the structure of your board, there is no "cookie cutter" approach that works for every foundation. You may structure the board to have as many or as few board members as you believe to be appropriate to serve the foundation's charitable purpose (bearing in mind that a not-for-profit corporation established under Florida law is required to have at least three directors). You also have considerable flexibility in structuring board members' term lengths. Many boards are structured to have staggered term lengths so that, in any given year, the board does not comprise a significant number of new members. In addition, you could consider limiting the number of consecutive terms that a board member may serve so as to maintain accountability and infuse the board with fresh ideas.

Board composition is critical to effective foundation governance. Not only is the composition of the board vitally important to the preservation of your foundation's charitable purpose, but it is also important to a number of the foundation's essential functions, such as investment management, compliance with state and federal tax laws, recordkeeping, and accounting. Thus, it is imperative that you give careful consideration to the short-term and long-term compositions of your foundation's board.

You have considerable flexibility as to the composition of your foundation's board. You may name family members, non-family members, or a combination of both. You may require that the board consist of a maximum or minimum number of family members, and you may apply similar or different requirements as to the number of outside board members. Also, if your private foundation is organized through a trust, then you may arrange for it to be managed by an institutional trustee, with family members and outsiders as advisors.

Although it's impossible to ensure that all board members will share your views and passions, you should consider establishing board member qualifications to consistently identify potential members who are more likely than others to preserve your foundation's charitable purpose.

You may also require that family members meet the same board member qualifications as non-family members. While you may be reluctant to impose membership standards on family members, doing so can be appropriate in many circumstances. Down the road, the unrestricted inclusion of family members on the board is just as likely to undermine your foundation's charitable purpose as the unrestricted inclusion of third parties.

An appropriate succession mechanism for your foundation may involve member nomination by a board committee or by an outside committee. It could also involve one or more persons having a veto right as to potential candidates. In terms of granting board membership, your foundation may approve qualified candidates upon the affirmative vote of a majority of existing board members.

You may also want to incorporate advisory board members into the governance regime. This can involve requiring potential board members to serve in an advisory capacity for a certain period of time prior to being granted full membership. This role could be structured to be similar to an apprenticeship. The advisory members could attend meetings, be aware of board activities, and even receive compensation. However, the advisors would not vote on board matters until they become full members. In addition, the existing board members would not be obligated to grant membership to the advisory members. This may be an effective way to groom the younger generations for board membership.

### Summary

On the whole, creating a private foundation is a rewarding, yet challenging, project. The flexibility you have in structuring your foundation is like working with a blank canvas. By working with your trusted advisors, however, you should be able to tackle many of the core design issues relative to your foundation, such as defining its charitable purpose, structuring its governance, and defining its lifecycle. With these issues resolved, you should have the underpinnings of a private foundation that expresses, preserves, and advances your charitable intent far beyond your lifetime.



#### Doug is a Williams Parker associate.

As a trusts and estates attorney, he focuses on helping families develop personalized, tax-efficient wealth transfer plans using the latest estate planning methodologies. Doug is a member of the 2016 Leadership Sarasota County program. He earned his LLM in Taxation, JD, MAcc, and BAcc from the University of Florida.