



Estate Planning and Philanthropy

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Philanthropy means different things to different people. A person does not have to be rich to be a philanthropist.

For some Philanthropy can be defined as gifting money, assets, encouragement and expertise to create social or environmental impact. It is different from charity, though both are important. By charity, people are referring to something that is purely altruistic, compassionate, and person-to-person, such as providing disaster relief or emergency aid. By Philanthropy, we mean something more strategic and engaging, less intuitive, more thought out, involving an individual giving to an organization that is trying to address the root causes of a problem.

Philanthropy is 'giving' by individuals, families or businesses with no expectation or desire to receive anything in return. It can include gifts of property, gifts in kind such as merchandise or the use of equipment or facilities, expertise for example pro bono services as well as gifts of money. As such Philanthropy can be best described as the practice of applying assets of knowledge, passion and wealth to bring about constructive change.

Philanthropy in Australia is not as well developed in comparison to United States of America and Europe however, it is changing gradually. Australia is now in 'catch up mode', fuelled primarily by the

'biggest' handover of inter-generational wealth in its history.

The growth of Philanthropy in Australia is by way of Testamentary charitable foundations which are established by Will; Public funds which are established by way of Trust Deed and/or a company limited by guarantee as well as Gifts during lifetime.

Funds allocated for charitable purpose are a different category of asset capital which can be leveraged for both Donor and community advantage. One must therefore not underestimate other intangible benefits to Donors who engage in active Philanthropy during their lifetimes. They can often develop a 'new lease of life', discover and enjoy new experiences and make new friends all set in a context of 'doing good'.

What follows is an overview of Philanthropy in the context of Estate Planning

The Practice of Philanthropy

Philanthropy is practised in three ways:

1. By personal involvement, that is, by giving either time, labour, and expertise;
2. By giving money or property directly to charitable organizations thereby enabling them to spend the funds as they choose on their current projects or operations; or
3. By giving money or property to philanthropic foundations



or trusts which support Donor selected causes. In this situation the donation is added to the capital base of the foundation and the income derived from its investment provides an income stream for distribution to charitable purposes usually in perpetuity.

The Prime Ministers Community Business Partnership (PMCBP) was a major driver in the growth of Philanthropy in Australia. It introduced a number of initiatives and tax concessions that generated more than anticipated activity such as:

- a) The introduction of Prescribed Private Funds (PPFs)
- b) The introduction of the Workplace Giving Initiative; a scheme that allows employees to make tax deductible donations from their pay;
- c) As of 1 July 2002, tax deductions for property valued at \$5000 and over donated to deductible gift recipients (DGRs) can be spread over a period of up to five years (with the CGT impost on gifts of property removed); and
- d) As of 1 July 2003, deductions for cash donations of \$5000 or more to DGRs can be spread over a period up to five years.

DGR is defined as the tax deductibility status of a donation which relies on a charity, foundation or Trust being approved as a deductible gift recipient (DGR) by the ATO. The guidelines on what organisations are entitled to DGR status are set out in a free publication issued by the ATO. It is called 'GiftPack for Deductible Gift Recipients & Donors'. In addition to the

commonly known public and ancillary funds, in this new philanthropically disposed environment, Advisors now have two additional vehicles which are:

- a) Donor advised Sub-Funds (DAFs);
- b) Prescribed Private Funds (PPFs); and
- c) Charitable Remainder Trusts (CRTs)

Each of these enable individuals and corporations to establish their own private foundations at an affordable entry cost on the basis that all donations of income as well as capital are made only to ATO approved DGRs. Trustees who are responsible for their administration and compliance must manage them.

Advisers determine whether their client's philanthropic agenda is best managed by making direct donations to the operating charities of their choice or to the clients own donor advised sub-fund or prescribed private fund. As such Practitioners need to be fully versed in the range of structures and 'charities only' tax concessions that are available to support their client's personal and philanthropic agendas.

Advisers therefore have a responsibility to establish whether their clients, both private and corporate, have philanthropic aims because donations to approved charities attract special taxation concessions that can be used to the client's financial advantage.

Philanthropic objectives need to be determined by establishing from the client:

- a) How much time and money does the client have to dedicate



management of the foundation and grant making programs?

- b) How much extra capital can the client reasonably expect to add over the next few years to build the capital base and consequent income streams needed to fund the mission of the foundation?
- c) How important is it that the client will be able to control the investment decisions of the foundation?
- d) How important is it that the client will have control over the grant making decisions made by the foundation?
- e) Is a level of privacy with regard to the client's gifting programs important?
- f) Is the memorial value of having the client's own named private foundation important?
- g) Is the capacity of the foundation to operate and support the client's philanthropic mission in perpetuity important?
- h) Would the client like to see their family and future generations, or business, involved in, carrying the foundation's philanthropic agenda forward?

Philanthropic Structures

At the outset, it is important to bear in mind that while DASFs and PPFs achieve a number of the same objectives, most notably the tax benefits; there are however significant differences with regard to the point of entry such as establishment and ongoing administration costs, and the control permitted by law over the investment and grant making decisions.

The primary advantages that accrue to Donors who make gifts during their lifetimes to a gift fund or foundation are

linked to taxation benefits, being:

- a) The ability to claim a tax deduction to the maximum amount of the donor's taxable income in the relevant tax year; and
- b) The ability for testators to avoid the impost of CGT on the transfer of gifts made by Will to their DASF or PPF, thereby increasing the capital and consequent income available for distribution to the community sector for charitable purposes.

Outright Gifts to Charities

The simplest form of charitable giving is an outright gift to charity. In the typical situation, a gift will be for the charity's benefit only, and the charity will take possession of the gift immediately. This type of gift is called an outright gift. This arrangement satisfies the general rule that a gift to charity must be paid to the charity in the form of money or property before the end of the tax year to be deductible for income tax purposes.

There are two ways in which an individual can make an outright gift to charities. Prior to making a donation, the individual needs to select organisations to which he or she wishes to donate and;

1. Either transfer the property during life (Inter Vivos) and receive and income tax and gift deduction or;
2. Make a specific gift in a Will or Revocable Trust and the Estate will a tax deduction in respect of the Gift.

Outright Inter Vivos Gifts

The simplest of the non-probate transfer techniques is the outright Inter Vivos gift. If



a client completes a gratuitous transfer of property to another person whilst obviously do not own that property when you die. Thus, the property is unaffected by Intestacy or the Will.

A transfer must meet three main requirements in order to qualify as an Outright Inter Vivos gift.

1. **Present Donative Intent:** the donor must have the present intent to make a gratuitous transfer.
2. **Delivery:** the property must be delivered to the Donee.
3. **Acceptance:** the Donee must accept the property.

One major advantage of giving property away before a client dies is that they get to see the recipient enjoy their generosity.

Nevertheless a client must make sure that they do not impoverish themselves.

Donor advised Sub Funds (DASF)

Donor Advised Sub Fund is a vehicle for charitable giving. In the USA this is a vehicle offered by Community Foundations and other commercial and nonprofit organisations. In Australia the equivalent is a Sub-Fund operating under the auspices of a community foundation or other Ancillary Fund. It is not legally possible for an Ancillary Fund to guarantee or promise that they will follow the Donor's direction for Sub-Funds. However, the Donor may make requests, and the Ancillary Fund Trustees will choose whether to follow those requests.

The primary features of a DASF

- a) It sits within a public foundation, such as a community foundation or a

company run public foundation.

- b) The entry and establishment costs are relatively small and affordable. The start-up costs and expenses involved in its ongoing administration are less than those incurred with Prescribed Private Funds.
- c) The Donor can formally request the trustee of the foundation to invest the donations made in one of the managed fund investment options offered by the foundation and the Donor can indicate the charities to receive the distributions of income derived from the investment of the donations. The Donor needs to be aware that while it is most likely the Trustee will follow the Donor's recommendations, the Trustee retains the ultimate decision-making power on how the donations and the investment of the funds are to be managed.

Establishing a DASF Account

A Donor must, complete and lodge a Donor nomination form in which they select:

- a) A name for the gift fund account, usually their family or corporate name, or a cause;
- b) An investment option which meets the criteria established by 'prudent person legislation' (requiring the investment of foundation capital in diversified asset classes); and:
- c) The charities must be registered with approved charities DGRs to receive the periodic distributions of income.

The Donor must also attach a cheque for the initial donation



(which is irrevocable) usually \$10,000 or \$20,000 depending upon the minimum entry limits set by the public foundation of the donor's choice. Once DASF has been established, the following steps are taken:

- a) The Trustee invests the capital donation.
- b) The Trustee distributes the income earned by the DASF each year to the chosen charities for as long as they remain DGRs.

The Donor can:

- a) Claim a tax deduction for the full amount of the initial and all subsequent donations made to the DASF; and
- b) Make recommendations at any time to the trustee to alter the beneficiaries and/or the share of income they are to receive, bearing in mind that all changes are at the trustee's discretion.

Prescribed Private Funds (PPFs)

A Prescribed Private Fund (PPF) is a stand alone private charitable foundation.

Donations made to it are tax deductible. While it can be established with as little as \$1.00, the costs of its formation, ongoing administration and compliance warrant seeding capital of not less than \$200,000 (ideally more) to be donated at its inception. The founder can specify the Trustees, including themselves (but most usually a proprietary limited company or a company limited by guarantee), responsible for the immediate and ongoing management of the PPF. However, they must appoint at least one 'Responsible Person' to the controlling body of the Trustee. A 'Responsible Person' is defined as a person who has a general responsibility to the community. Additionally, the

Responsible Person must not be associated with the Donor/Settlor in anything other than a professional capacity.

A prescribed private fund will be the best option for the client if the client wants to:

- a) Take an active role in philanthropy;
- b) Maintain control over investment and grant making decisions;
- c) Support charities or charitable causes of choice according to the client's own timetable;
- d) Build an endowment fund and continuing income stream for the client's preferred charities using their own named foundation;
- e) Share the philanthropic process with family members and future generations, and business successors

Features of PPF

- a) A PPF is established by Will or Trust Deed (most usually by Deed).
- b) The persons controlling the Trustee of a PPF must include a 'Responsible Person' who is not obliged to control the Trustee. Under new guidelines issued in May 2004, employees of either the fund or a Major Donor are not eligible to be a 'Responsible Person'. 'Major Donor' is defined as a Donor who has made gifts totalling more than \$10,000 to the Trust since the date of the deed.
- c) A PPF is itself a DGR and has Income Tax Exempt Charity (ITEC) status.
- d) It must have its own ABN.
- e) A PPF is permitted to solicit and receive donations from the public provided this is



- not its primary source of income or capital raising.
- f) A PPF is required to maintain a gift fund and have its own bank account.
- g) Funds donated to a PPF must be invested by its trustee in accordance with the Trustee Act of its State of origin and in accordance with the principles of 'prudent person' legislation.
- h) All beneficiaries of a PPF must be DGRs however, being a private foundation; it is not permitted to make a gift to another private foundation or ancillary fund. A PPF can be established with a nominal settlement sum usually \$100, even though \$1.00 will do which is not tax deductible. A PPF's founder and major donor can be a member of the trustee and is entitled to take an active part in the investment and grant making decisions.
- i) A PPF is not permitted to provide an uncommercial financial or other benefit to its founder, trustee, or any donor or associate of any of them. The only exception applies to a member of the Trustee appointed in a professional capacity provided the deed allows for payment of his or her professional fees.
- j) A PPF cannot carry on a business nor can it control or manage a program it has funded.
- k) Generally, the income derived by a PPF each year must be distributed by the trustee to the eligible charities defined in the deed. However, it can, at the trustee's discretion, be accumulated to the extent necessary to maintain the real value of the capital of the PPF at the end of the previous year (after adjustments have been made for movements in the CPI).
- l) If at the time of prescription (or later) a larger capital base is needed to support the future funding objectives of the PPF, its trustee can lodge a Capital Accumulation Plan for approval by the ATO. All future donations can be added to capital, but the ATO usually requires a one-off distribution of not less than 5% of each gift to DGRs in the year following the gift.
- m) At the end of each financial year the accounts of the PPF must be audited and an Annual Information Return lodged with the ATO.

Primary benefits available to the founder/major Donor of a Prescribed Private Fund

Some of the major benefits enjoyed by a Donor who establishes and contributes to a PPF during his or her lifetime are:

- a) He or she will have the pleasure of seeing his or her benefaction at work.
- b) He or she can share this experience with members of his or her family by appointing them members of the trustee responsible for the ongoing management of the foundation.
- c) A PPF operates as a lasting memorial to the founder and is an endowment fund which will potentially benefit the causes of his or her choice forever.
- d) He or she will benefit from the tax deductibility of gifts made to his or her PPF. He or she can choose to spread the benefit of deductions for gifts made to the value of \$5,000 or more over five consecutive years.



e) The PPF he or she establishes during his or her lifetime can also receive his or her testamentary gift of property exempt from capital gains tax.

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