

SINCE 1887



Moving from a Private Foundation to the MHBG Donor Advised Fund

Mercy Home for Boys & Girls Donor Advised Fund (MHBG Donor Advised Fund) is a qualified section 501(c)(3) organization and is classified as a public charity. A contribution to MHBG Donor Advised Fund is eligible for a charitable deduction from your federal income tax. A charitable deduction also is available in many states that have their own income taxes.

The board of directors of a private foundation may want to consider alternatives to continuing the foundation for the long term in its existing form. In our experience, we have seen boards opt to discontinue private foundations and establish different entities for charitable contributions. Often, boards decide that a donor advised fund (“DAF”) offers a better opportunity for achieving their goals.

THERE ARE SEVERAL REASONS WHY A BOARD MAY WANT TO TERMINATE A PRIVATE FOUNDATION IN FAVOR OF A DAF.

The pros and cons of both private foundations and DAFs are compared in another article. The following are some of the reasons why the board

of directors of an existing private foundation may choose to transfer its assets to a DAF.

- A private foundation may have outlived the purposes for which it was originally created. Perhaps the needs a foundation was intended to address no longer exist or are otherwise being met.
- A private foundation may turn out to be more cumbersome to manage than was originally anticipated by its founders. The special tax rules dealing with private foundation investments, distributions and financial dealings may prove difficult to navigate without knowledgeable advisors. Without this advice and support, a private foundation’s board of directors risks making missteps that could subject the board and its organization to private foundation excise taxes. By distributing a private foundation’s assets to a DAF, responsibility for those assets is transferred from the foundation’s board to the charity that serves as the DAF’s sponsoring organization.
- The costs of private foundation compliance — including accounting, legal and investment fees — may consume a significant portion of a private foundation’s annual revenue, especially if the foundation is shrinking due to grant-making or investment setbacks. Because of the economies of scale typically associated with a DAF, the administrative costs associated with the assets are often reduced.
- A private foundation’s board may want to free up more time to focus purely on recommending grants or pursuing other interests. Sometimes board members of a foundation wish to go their separate ways. By transferring



assets to a DAF, the board may select a model investment strategy and simply focus on recommending grants. By transferring assets to multiple DAFs, different private foundation board members may each recommend grants independently of each other.

The mechanics of terminating a private foundation by transferring its assets to a DAF are simple:

First, a private foundation in good standing need only distribute all of its net assets to a DAF account. The private foundation's termination for tax purposes is automatic as long as the public charity that is the sponsoring organization of the DAF account is in good standing and has been in continuous existence for at least five years. The MHBG Donor Advised Fund is a public charity that meets these requirements.

Second, the private foundation then must file a final year's informational tax return with the IRS for the year of termination. A private foundation that terminates by transferring its assets to the MHBG Donor Advised Fund owes no termination tax on the transfer and does not need to give advance notice to the IRS of its intent to terminate.

Finally, the private foundation should notify the states in which it is registered and take any steps necessary to terminate its legal existence. For example, a private foundation organized as a charitable corporation, as opposed to a trust, will need to comply with local state law governing the dissolution of a charitable corporation.

Once a certificate of dissolution is issued by its state of incorporation, the foundation will typically need to file notice of the dissolution with the other states, if any, in which it operates. A private foundation considering termination should seek the advice of local counsel to ensure compliance with state requirements.

Although there are some administrative steps to terminating a private foundation in favor of a DAF, those steps are relatively simple with a transfer to a DAF with Mercy Home. A private foundation's board may find the long-term simplicity and low cost of a DAF well worth considering and an extremely appealing alternative to business as usual.



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