When do I consider setting up a separate foundation for my giving?

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In setting up charitable trusts or advising on structuring a donor's giving from a tax perspective, investment advisors are often asked when it becomes worth setting up a separate foundation. It is often assumed that this might be the domain of millionaires alone.

The answer to this is that there is no magic amount as there are often non-financial reasons for doing so, for example, to set up a foundation in the name of a loved one who has passed away or merely to commit in a more formal way to longer-term giving.

However, whilst a large lump sum amount is not a pre-requisite, a donor does need to look at the financial viability of setting up a foundation, as there would be no point to the foundation if, for example, the annual audit costs exceeded the amount available for distribution each year.

If a donor is committed to longer-term giving, establishing a foundation can often be the most beneficial mechanism for a number of reasons, including:

1. putting processes and governance procedures in place that can endure after your death;
2. setting out a vision for your giving that can endure beyond your lifetime;
3. financial planning to ensure that the foundation generates the funds to be distributed now and for the future;
4. the further tax advantages available.

What is a foundation?

The term "foundation", though widely used, actually has no technical meaning in South African law. It is a term that we have borrowed from places like the United States to refer to an entity through which philanthropic grants are made, for example, a charitable trust.

Vision and governance

If a donor sets up a charitable trust in terms of their Will they unfortunately won't get to experience the ongoing rewards of being personally involved in giving. If the donor instead sets up a foundation during their lifetime not only do they get to enjoy first-hand their philanthropic activities but they can also ensure that their co-trustees (which can include family) fully understand their vision and can ensure that they are comfortable that the procedures and finances put in place are effective and will ensure that their vision can continue to be implemented after they have passed away.

Financial planning

If a donor is committed to long-term giving, they will usually fund the foundation in a way that ensures that it can become self-sufficient. For example, if a donor establishes a foundation and makes a R3million donation to the foundation (even perhaps through lump sums over time), the trustees of the foundation would usually seek to distribute the income, or part of the income, generated on the capital amount each year. If the R3million is appropriately invested, then as the capital grows the income should also grow - enabling the donor at the least to keep his or her giving in line with inflation each year. The foundation can then continue indefinitely in a self-sustaining manner even after the original donor has passed away and perhaps no further funds are added.

Tax advantages of a separate foundation

The tax advantages of giving directly to an organisation (with the requisite approvals) apply equally to giving to a foundation provided that it in turn has the requisite approvals.

It is therefore essential that the foundation be properly structured so that it can and does obtain approval from SARS as a Public Benefit Organisation and also possibly in terms of Section 18A (of the Income Tax Act). As a reminder, Section 18A approval allows the donor a level of tax deductibility in respect of his or her donations.

If giving directly to an organisation or to a foundation with the necessary approvals is straightforward, and brings with it the required tax benefits, one might question (from a tax perspective) the benefits of setting up a foundation rather than simply giving directly.

The answer to this is that there are indeed further tax advantages to giving through a foundation. If the foundation obtains approval as a Public Benefit Organisation then any income or gains earned on the investment within the foundation should be tax exempt1. As a result, any tax saving means more funds available for distribution. If the donor continued to give directly to organisations, it would usually be from funds in respect of which he or she has paid tax.

Clearly there are some significant advantages available to giving through establishing your own separate foundation but you don't have to be a millionaire to do so. It's certainly an option worth exploring for any donor committed to giving well into his or her future and beyond.

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