Neithercut
Philanthropy Advisors, LLC

PHILANTHROPY BRIEFINGS

Why Family Foundations Lose Their Way

A Founders' Guide to Long-Term Philanthropic Success

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Family foundations are a large and diverse group. The Foundation Center reports that there were more than 38,000 family foundations in the U.S. in 2009, and these foundations made grants totaling more than $20 billion.[1] The very largest foundations in America today are family foundations, and some of the very smallest are family foundations, as well. Some family foundations focus on local issues, while others concentrate on broad international issues. Some support the arts; others support only religious organizations.

Despite their many differences, all family foundations are legally considered to be private foundations and must abide by certain state and federal regulations; however, as a practical matter, the world of foundations may be one of the least regulated sectors of our society. There are no national standards and there is no certification or accreditation body. Although Congress has expressed an increasing interest in monitoring foundations in recent years, federal and state governments do not have the staff or funding to conduct any real oversight of the foundation world.

Over the past 20 years, the management of foundations has become more professionalized and a set of best management practices has slowly emerged, but despite the good work of the Council on Foundations, the Association of Small Foundations, and the National Center for Family Philanthropy, these best practices for the management of foundations are not well-known. For the most part, attorneys who help organize family foundations lack experience in the ongoing operation of foundations and the craft of grantmaking. Once the foundation is established, the family is often on its own.

1 The Foundation Center, *Key Facts on Family Foundations*, January 2011.

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From a legal point of view, family foundations are usually organized properly, but they often struggle with management issues that could have been — and should have been — resolved early on. These issues frequently lead to problems and dysfunction. In many cases, subsequent trustees spend a lot of time arguing about important issues that should have been clarified at the time of the foundation's organization, or during the first few meetings of the board of directors. The trustees of a poorly planned foundation end up spending time and energy debating (or arguing over) the purpose and direction of the foundation, especially after the passing of the founder. As a result, these trustees frequently feel demoralized and may even avoid board meetings. Serving as a board member of a charitable foundation should be a wonderfully rewarding and fulfilling responsibility, yet poor planning can turn this experience upside-down.

Poor planning most often results in problems for larger foundations rather than smaller foundations. Because of their limited funds, a lack of planning is typically not a problem for very small foundations — but poor planning can be a serious problem for foundations with more assets, because they tend to have a longer life span and they generally focus on more complex social issues. Good planning becomes especially important for larger foundations because, with more resources at stake, there tends to be greater interest and increased emotion from family members and successor trustees. We believe that philanthropy has a great capacity to bring families closer, but a poorly planned foundation can have the opposite effect.

In advising our clients, we have had the privilege to work with some of the best-managed family foundations in America. In addition, we have had the opportunity to assist foundations that were less well-managed. We have found that many of the problems faced by older foundations could have been solved easily and simply at the time of their launch.

Neithercut Philanthropy Advisors has created this consumer guide as a public service to family foundations, their trustees, and professional advisors. You can use this guide to help get your new foundation launched on the right course, or to get it back on track if you think your foundation has migrated off-course a bit. Professional advisors will find this guide useful in working with their clients who wish to start a foundation.

Seven Misconceptions about Family Foundations

It seems that everyone wants a foundation these days — at least many people do. Yet some individuals who contemplate starting a foundation have a poor understanding of the challenges of running a philanthropic enterprise. Further, many officers and trustees of existing family foundations are unaware of these challenges. So, what are the common misconceptions about family foundations?

- **It is easy to give money away.** As Warren Buffet once quipped, "It is a lot harder to give money away than it is to make it." It can be relatively easy to give money away if you do not care what impact you will have. However, if you care about how the money is used and what impact it has, then it can be a very challenging endeavor.

- **My unemployed nephew can handle this, no problem.** Foundations may be "nonprofits," but they are a business enterprise nonetheless. If you would not entrust the family business to your unemployed nephew, it is unlikely that he will be able to manage the foundation, either.

- **My kids can work out the foundation's mission and objectives on their own.** If your children have trouble sharing the family cottage, or if they are still upset about who got the best bicycle at Christmas 25 years ago, then it is not likely that they will be able to resolve the much bigger issues relating to your foundation, such as its mission and goals.

- **My kids always get along.** Maybe so, but how often are they required to work together on a serious business issue? The foundation boardroom is often the only place siblings or cousins must work together, and thus it can be the battleground where a lifetime of resentments comes forth.

- **My children will learn how to do it.** Yes, they may. However, it will likely take them a long time and they would benefit enormously from some guidance from you, the founder.

- **My professional advisors will be on hand to make sure things do not go astray.** Advisors can be extremely helpful. However, they are your advisors, and many times the next generation does not wish to keep them involved. Further, in extreme cases, advisors have treated the foundations they advise as resources for their own interests. Moreover, even if the advisors are trustees of the foundation, most will resign if it becomes clear that this is the wish of the family.

- **You cannot get into trouble running a foundation.** The IRS imposes a set of restrictive rules on the management of private foundations. If you violate these, you can be fined and/or jailed. In recent years, both Congress and the media have shown increasing interest in the abuse of IRS regulations by foundations.

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Five Dangers of a Poorly Planned Foundation

There have been a number of scandals in recent years involving foundations going wildly astray or doing things that were clearly uncharitable, and thus illegal. When launching a foundation, a founder might have some concern that his/her organization could also go astray. What are a founder's greatest fears?

- **The funds will be used for a purpose I don't want.** Founders often fear that subsequent trustees will re-direct the foundation's grants to projects outside their original interests.
- **The funds will be used in a place that I do not want.** Today, the second and third generations of a family are often quite dispersed. Thus, the children and grandchildren of the founders often live in distant places relative to the location of the foundation and the community where the original wealth was created. Subsequent generations feel less connection with the community of the founders, and there is a natural interest in funding projects in their home communities.
- **The family will not care and will not want to get involved.** Despite the deep charitable inclinations of most founders, not all children have the same interests. Some children are eager to get involved in philanthropy, while others decline to serve as trustees — or, if they do serve, they serve passively, without the diligence and keen interest of the founders.
- **The funds will be used for a project or issue that I would find embarrassing or contrary to my personal values.** Foundations can evolve over time, and eventually they may end up supporting projects or organizations that are antithetical to the values of the founders.
- **The foundation will end up being controlled by people who did not personally know me and who know little about me.** After a generation or two, many family foundations end up being run by the law firm or financial planning firm that originally helped set it up. At first, members of this firm may have known the founders and their interests, but as years go by, new trustees come on board and there is a growing distance between the founders and the successor trustees. Most family foundations are established as perpetual institutions, even though perpetuity is a really long time — and 100 years from now, the trustees may have little to no knowledge of the founders and their interests.

The 10 Most Common Mistakes in Foundation Planning

A common mistake: The founders or trustees appointed the least-qualified member of the family to manage the foundation.

A foundation is a business enterprise and, like any good business enterprise, a little bit of planning goes a long way. What can go wrong, you might ask? Well, plenty. Poorly planned foundations typically make many of these common mistakes:

- The founders did not consider the appropriate life span for the foundation.
- The foundation's bylaws do not specify how the officers are to be elected.
- The bylaws do not specify how important decisions are to be made.
- The articles of incorporation and bylaws are vague and boilerplate, and they provide no guidance for future trustees.
- The articles of incorporation and bylaws are so detailed and specific that future trustees have minor roles and little incentive to serve.
- The founders did not discuss whether future trustees could suggest grants for their personal interests.
- The founders did not set forth the mission and goals of the foundation.
- The founders did not record their personal values and charitable interests.
- The founders or trustees appointed the least-qualified member of the family to manage the foundation.
- The board has not involved the next generation in the operations of the foundation and, when the time comes, the new trustees have not been prepared to serve.

Why You Want a Well-Planned Launch for Your Foundation

With thoughtful planning, a foundation can stay out of trouble, honor the founders' interests, contribute to the common good, and bring a wonderful sense of fulfillment and joy to the foundation's trustees and the founders' family.

A well-planned foundation can avoid many of the dangers of poorly managed foundations, and good planning can result in significant benefits, as well. With thoughtful planning, a foundation can stay out of trouble, honor the founders' interests, contribute to the common good, and bring a wonderful sense of fulfillment and joy to the foundation's trustees and the founders' family. Thus, a well-planned foundation will result in the following:

- The founders will be confident that their charitable assets will be used properly and according to their wishes.
- Future trustees will have a clear roadmap to help them focus on managing the organization for maximum benefit, rather than wasting time and money debating what they might or might not do.
- The foundation will be more effective and will be more likely to achieve its goals; as a result, the founders and their family will derive a greater sense of joy and fulfillment from their good work.
- The foundation will serve as a unifying element for the family, integrating subsequent generations together in a common cause for doing good and honoring the founders.

Families engaged in philanthropy are increasingly taking advantage of expert philanthropy counsel.

Five Steps to a Well-Planned Foundation

Are you ready to start planning your foundation? Here are five important steps to help you get started:

- **Consult with your attorney and financial planner.** If you are thinking about getting started in philanthropy, a good first step is to consult with your estate-planning attorney and financial advisor. The legal form of the foundation, the timing of its launch, and how it will be funded are important issues to discuss with your professional advisors.

- **Document your goals, values, and interests.** You may be certain of your goals, values, and interests, but your advisors and children may not understand them quite as well as you think. Documenting these important elements of your philanthropy, either in writing or on video, will be a valuable resource for your family and for the foundation's future trustees.

- **Talk to your children about your interests and your goals for the foundation.** Once you are no longer involved, your children will likely say something like "Daddy would never have wanted us to fund this grant," or "Mother would have wanted us to support this organization." We hear this time after time at board meetings. If you do not discuss your philanthropy with your children, each child may have a very different impression of what you wanted them to support.

- **Involve your children in your philanthropy as soon as possible.** Philanthropy can be a challenging endeavor and, like any activity worth pursuing, you will learn from your mistakes. Getting your children involved early on and giving them an opportunity to learn at a young age will result in more seasoned and experienced trustees when the time comes for them to serve.

- **Get your philanthropy advisor involved early in the process.** Families engaged in philanthropy are increasingly taking advantage of expert philanthropy counsel. A good philanthropy advisor will have extensive experience in translating charitable interests into successful philanthropic endeavors. You will want to get your philanthropy advisor involved as early as possible, so that the issues addressed in this guide are incorporated into the founding documents of the foundation.

Foundation Launch Checklist

Many foundations allow trustees to recommend grants for a personal charitable interest, or the foundation might match a personal gift from a trustee.

Whether you are just getting started or you are well on your way, this checklist can be useful in setting your foundation, or other philanthropic vehicle, on the proper course.

- Are you certain that a foundation is the right vehicle for you? Have you considered the benefits of a donor advised fund, a support organization, a charitable lead trust, or simply using your checkbook? **Y or N**
- Have you considered the benefits of the trust form versus the corporate form for a foundation? **Y or N**
- Have you considered the appropriate life span for your foundation? (Most foundations are launched with the assumption that they will be perpetual, yet it turns out that perpetuity is a rather long time.) **Y or N**
- Have you written a mission statement for your foundation? (Mission statements can be hard to write and they are often too broad or too narrow, but the exercise can be very valuable for a founder. What do you want the mission of your foundation to be?) **Y or N**
- Have you documented your personal values? (Values can mean different things to different people. When you are no longer involved, what principles, issues, or standards would you like your successor trustees to keep in mind as they manage the foundation?) **Y or N**
- Have you decided how successor trustees will be elected or appointed? (Does each child and his/her family get one representative, or can all the grandchildren serve?) **Y or N**
- Have you consulted with your children about their personal interests in being involved in your foundation? (If your children do not have an interest — and some will not — you may want to manage trustee succession in a different manner.) **Y or N**
- Have you already begun to involve your children in your charitable giving? (They will be better trustees in the years to come if you get them involved now.) **Y or N**
- Have you established a geographic focus for the foundation? (If your children no longer live nearby, they may wish to make grants in their home communities.) **Y or N**
- Should your children be able to split the foundation into pieces? (When children cannot agree, they will often consider breaking the foundation into pieces, with each child getting his/her own piece for personal philanthropy.) **Y or N**
- Have you decided if future trustees can make discretionary grants for their personal interests? (Many foundations allow trustees to recommend grants for a personal charitable interest, or the foundation might match a personal gift from a trustee.) **Y or N**
- Do you have any advice for future trustees if they decide to terminate the foundation? (How should the final funds be distributed if future trustees decide to terminate the foundation?) **Y or N**

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ABOUT NEITHERCUT PHILANTHROPY ADVISORS

Neithercut Philanthropy Advisors creates innovative strategies for effective, rewarding philanthropy. Based in the Great Lakes region, where the Kellogg, MacArthur, Kresge, Lilly, Mott, Knight, and Ford families started many of America's greatest foundations, we are dedicated to the traditions of these early philanthropists and to their Midwest values of humility and community responsibility. The staff of Neithercut Philanthropy Advisors brings significant experience, a unique perspective, and exemplary integrity to their work in philanthropy.

Neithercut Philanthropy Advisors works with the following types of clients:

- **Foundations that wish to sharpen their focus.** Many founders do not clearly communicate their wishes or goals for their foundation. As a result, these foundations often struggle to be effective once the founders are gone. Strife and acrimony are common among the remaining family members serving on the board as they struggle to find a shared focus. We work with founders to help give their foundation a clear and well-documented strategic direction. Further, we help existing family foundations review their founder's legacy — as well as their trustees' interests — as a way to clarify and sharpen the foundation's mission and strategy. One of the tools we use in this process is the National Center for Family Philanthropy's Pursuit of Excellence process. Our firm is one of only 20 in the country to have completed the necessary training to use this innovative strategic planning tool.

- **Individuals serving in a new philanthropic role.** Many foundation trustees or executive directors find themselves in new roles with no experience or training in grantmaking. These trustees and directors, as well as individual donors, frequently have a difficult time finding their way in their new position. In response to that concern, Neithercut Philanthropy Advisors has launched a new coaching program, called Philanthropy Fitness™ (www.philanthropyfitness.com), which helps emerging leaders build confidence and expertise in the rapidly evolving world of philanthropy and charitable giving.

  The Philanthropy Fitness™ program functions as a confidential support system for new board members and executives of foundations who may have significant management and leadership experience, but who are less familiar with the unique challenges faced when running a foundation. The goal of the program is to prepare our clients for successful foundation leadership through a five-step coaching process and ongoing support.

- **Foundations that wish to "tune up" their administrative operations.** Many foundations are unaware of the best practices of modern foundation management. These are often small family foundations that have developed administrative procedures on an ad hoc basis over the years, and hired staff who had never worked at a foundation before. We work with existing foundations to develop new administrative operations that ensure they are well-managed, accountable, and efficient.

- **Successful entrepreneurs who are new to the nonprofit world.** Many successful entrepreneurs have a vision of what they would like to achieve as philanthropists, but they know very little about the nonprofit world and how to tackle social problems. We work with these entrepreneurs to help translate their philanthropic vision into practical programs with a high probability of success. In designing new grantmaking programs or initiatives, we emphasize the development of an outcomes-based strategy that includes clear metrics to monitor progress. We have considerable experience designing grantmaking programs, ranging from very small community initiatives to large, multi-foundation consortiums.

- **National foundations looking for local partners.** National or regional foundations often consider using local community foundations as partners because of their local knowledge and credibility. However, these partnerships often are unsuccessful because the national foundations do not understand community foundations, and they place restrictions on their grants that are inappropriate for some locales or that handcuff the local community foundations from adapting the program to suit the needs of their specific areas. We have 20 years of experience working with community foundations and developing successful programs that serve them.

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