

# Informed Philanthropist

May 2000

## Message from the CEO

### Our Goal Is to Give You the Knowledge You Need to Be In Control of Your Charitable Giving

**W**e decided to create this newsletter in response to feedback we've received from clients and high-end donors—people like you—who are concerned about charitable giving. We listened, and we understand that there is a lack of useful information designed from the donor's point of view.



Roger Silk, CEO

Many of you felt that there is a need for information about the charitable world—and different estate planning techniques

—that is not designed to raise money for a specific charity. This newsletter is not trying to raise funds for any specific charity. In fact, although we encourage charitable giving, we believe donors should have as much

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**We believe donors should have as much control over their funds—and as much input into the charities they support—as they can.**

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control over their funds—and as much input into the charities they support—as they can.

Of course, with control comes responsibility. And the best way to make responsible decisions is to be informed. That's why we've inaugurated the *Informed Philanthropist*—to help you get the information you need to be an effective and responsible donor over both the short and the long term.

This newsletter is for you—today's philanthropist. I invite you to give us suggestions, comments, criticisms, or any other feedback that you think will be useful. I look forward to hearing from you.

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## News from the World of Philanthropy

### Virginia Software Entrepreneur Creates \$100 Million Private Foundation; Promises Free College Education

**M**ichael Saylor, 35, the founder and CEO of MicroStrategy, has contributed \$100 million to create a private foundation. He intends the \$100 million as a “down payment” in his effort to make available a free college education to all comers.

Saylor, who made his fortune by helping companies make sense out of huge amounts of data by using cleverly designed software, believes that

*See \$100 million foundation, page 3*

### Two Cases Illustrate Control Benefits of Private Foundations

**M**arylou Whitney, a descendant of the founder of the Whitney Museum, and prominent member of the Whitney Museum's national fundraising committee, has decided to cancel a planned \$1 million gift to the museum. She has also removed the museum as a beneficiary of her will. She objects to the museum's decision to exhibit a piece which she believes trivializes the events of the Holocaust.

Separately, John Sykes has discontinued all future gifts to the South-

*See Control benefits illustrated, page 3*

## Readers' Ideas for Effective Giving

This marks the first installment of this column, whose purpose is to help our community of philanthropists share ideas, so all can benefit from each others' insights.

In the future, we will feature your ideas regarding the techniques, tools, or approaches which make your charitable giving as effective as possible.

Please send us your ideas. When considering effectiveness, you may wish to consider the following: how you select grant recipients; how you determine the amount of support; how you choose between multiple good causes; how you measure results; how you find new grant recipients; what are the key reasons you stop giving to particular charities. Of course, any ideas on any philanthropic subject are welcome. We will publish those submissions which we believe will be of the greatest interest and value to our readers.



Please submit your ideas to: Effective Giving, Sterling Foundation Management, 14622 Ventura Blvd., Suite 745, Sherman Oaks, CA 91403, or by fax 801-459-5935; or by email: [Ideas@Sterlingfoundations.com](mailto:Ideas@Sterlingfoundations.com).

Please specify if you would like to remain anonymous.

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Editor: Erica Mannard  
[www.sterlingfoundations.com](http://www.sterlingfoundations.com)  
468 Camden Drive, Suite 300, Beverly Hills, CA 90210  
Phone 310-285-5322, Fax 801-459-5935

Sterling Foundation Management is the nation's leading manager of private charitable foundations. Our mission is to assure that our clients achieve the maximum possible results from their charitable giving. We do this by providing turn-key foundation management, and advice to make sure clients enjoy the greatest available tax benefits, optimal control, desired family involvement, and long term continuity of purpose.

Sterling Foundation Management does not practice law, and nothing in this text is to be construed as legal or tax advice.

## Private Foundation Permitted to Make Grant to Foreign Charity Not Recognized by IRS

If you, as an individual, wish to give money to a foreign charity that is not recognized by the IRS, you may do so, but you cannot claim a tax deduction.

However, that very same gift to a foreign charity, if made by a private foundation, may be permitted. A private foundation may allow you to get an income tax deduction that you could not otherwise have received. You simply make a tax deductible contribution to your foundation, and then have your foundation make a contribution to the foreign charity.



There are certain rules that the foreign charity must satisfy, and your foundation must make a good faith and satisfactory effort to determine, in effect, that the foreign charity would qualify under IRS rules as a tax exempt charity if it were to seek such a status.

IRS has recently reaffirmed this principal in a recent private letter ruling (Ltr. Rul. 200010056), making a private foundation the vehicle of choice for international charitable giving.

## IRS Affirms that Private Foundation May Pay Board Members Compensation

Under current tax law, the IRS has generally permitted private foundation disqualified persons (e.g. the founder and family, employees, etc.) to receive compensation for services, provided that the services are reasonable and necessary, and the payment is not excessive. However, because of the nature of these requirements, there are few black and white rules. As a result, to be absolutely certain that your foundation is in compliance, it is often necessary to obtain a private letter ruling.

In Ltr. Rul. 200007039, the IRS again upheld the general rule that a private foundation's payment of compensation to its individual board members will not be self-dealing if (1) the services the board members provide are reasonable and necessary for carrying out the exempt purposes of the private foundation and (2) the compensation is not excessive.

*Have a legal or tax issue you'd like to hear about? Email us at [ericamannard@sterlingfoundations.com](mailto:ericamannard@sterlingfoundations.com)*

## Consultation Corner by Roger Silk

John is a retired businessman. During his very successful career, he built a net worth of \$10 million. He enjoys income from his investments and residual business activity of about \$1 million a year. He is very active in a number of charitable causes, with a particular emphasis on education.

In recent years, he has been giving about \$100,000 a year to support his favored causes. John plans to leave at least 25% of his estate to charity when he and his wife are gone. Like most of us, John doesn't much care for paying taxes.

John and I spent a couple of hours discussing how he might best achieve his charitable goals, while at the same time minimizing his taxes. The analysis that follows applies to anyone in a situation similar to John's.

### Economic Analysis

The key facts in John's situation are that he is currently giving \$100,000 annually to charity, and that he intends to leave 25% of his estate to charity. Given these two facts, he can save over a million dollars in taxes

over ten years, just by creating a private foundation and funding it with \$2 million now.

Here's how to calculate this savings: Assume that the \$2 million in the foundation earns 8% a year, and that the income tax rate on this income would have been 45%. Since

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**NOT creating a foundation would cost John over a million dollars over the next ten years. He concluded that setting up a foundation would be a "no brainer."**

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the income in the foundation is not subject to income tax (but is subject to a 2% excise tax), John saves the \$68,800 (i.e. 43% of \$160,000) that he would pay if the \$160,000 (i.e. 8% of \$2 million) of income were on that return. Over ten years, that adds up to \$688,000 (more, if he lets it compound).

Then add the value of the additional annual tax deductions which

John gets from the \$2 million gift. With his income of \$1 million a year, John will be able to deduct \$300,000 each year for five years. This generates an extra \$200,000 in deductions each year (i.e. \$300,000 less the \$100,000 that he would get anyway because he gives \$100,000 to charity). The extra \$200,000 deduction, at a 45% tax rate, is worth \$90,000 a year. For five years, that adds up to \$450,000.

These two sources of savings together exceed \$1.1 million over ten years. And since John is going to ultimately give at least \$2 million to charity anyway, it's pure savings.

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*If you have a private foundation, or are considering creating one, Sterling will be happy to consult with you at no cost and no obligation. Our professionals can help determine how to get the maximum possible tax savings, and how to use your foundation to most effectively achieve your charitable goals. Please call 310-285-5322 and ask to speak to Erica to schedule a free consultation.*

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### \$100 million foundation, from page 1

the internet provides an ideal, low cost, and highly efficient venue for offering the content of a college education.

Part of the concept—according to MicroStrategy vice president Mark Bisnow—is to gather together, in electronic form, courses and lectures featuring the greatest minds in a wide variety of fields. If successful, the concept represents an interesting challenge to the education establishment.

According to Bisnow, for the internet to reach its full potential as a teaching and learning tool, technology will have to develop further. For example, he says, "people will want really cool pictures" and the ability to stop, search, and even randomly access data. He estimates that the necessary technology will be widespread within perhaps five years, and hopes to facilitate this process with his foundation.

### Control benefits illustrated, from page 1

ern Evangelical Seminary, to which he has given over \$3 million dollars. Sykes made his decision after a dispute arose among the board members regarding the naming of a building. Sykes is also trying to recover past gifts.

These two cases illustrate the perils of making large endowment gifts to public charities. A better strategy for donors concerned with how their money is used, is to hold onto the funds, often in a private foundation, and contribute on a periodic basis.

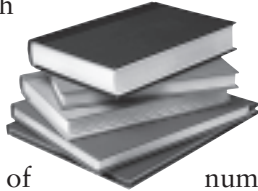
This approach, as illustrated by Whitney and Sykes, allows donors to cut off funding if they no longer agree with the course chosen by their beneficiaries.

Both Whitney and Sykes are dedicated and involved philanthropists. Whitney immediately committed the \$1 million to another art museum. Sykes has recently completed a \$10.1 million gift to Queens College in New York.

## Book Briefs

**F**ounders of private foundations are often so enthusiastic and involved with the causes they support that they want to raise additional money from the public for the cause. Certain highly publicized celebrity foundations have greatly heightened awareness of the possibility. For example, baseball home-run king Mark McGwire committed a million dollars to launch his foundation. The Mark McGwire Foundation has since been running a series of national commercials featuring the exploits of the great slugger, and inviting the audience to join him in the fight against child abuse by contributing money.

But most philanthropists are not as famous as McGwire. For the rest of us, raising public money is much more difficult than it is for major celebrities. But, depending on the cause, the goals, and the strategy, it can be done. There are several recent books which address the issue. Among these are Peter Dalton's *Key to Fundraising Success*, and Mal Warwick's *Five Strategies for Fundraising Success*.



Dalton's approach is to emphasize his view that people give to people more than they give to causes. While certainly not the whole story, his view does explain, for example, why celebrity appeals can work so well. Dalton boils his philosophy down to a clever acronym: ASK. Argue your case; Show and tell the prospect why they should give; Key in to what really drives them.

Mal Warwick, a very successful fundraising consultant who has been around for years and has written a number of "how-to" books, turns his hand to high level strategic thinking in *Five Strategies*. Warwick also presents the reader an easy to remember acronym: GIVES. In this case, the letters stand for: Growth, Involvement, Visibility, Efficiency, and Stability. Each letter is an alternative strategic vision which an organization may choose to adopt.

Warwick's philosophy stresses trying to understand why. Why does something work or not work? Why do people give? It remains to be seen whether his ambitious attempt to develop a "method of analysis that

takes into account the full spectrum of fundraising possibilities and techniques" produces the same nice results in the real world as it does in theory.

Both of these books, as well as dozens or even hundreds of others, remind us of the obvious problem: raising money can be a difficult and challenging task, even for the most worthy of causes. And perhaps the most important lesson for founders of private foundations is that it can be done—with the proper strategy, knowledge, and skills.

### Know Anyone Who Would Like Their Own Free Subscription?

If you know someone who is a high-end donor, or a potential high-end donor (generally, someone who is capable of giving at least \$25,000 a year, or creating a foundation with at least \$250,000 of assets), please send us their name, address, and telephone number, and we will be happy to send them a free subscription, with your complements. Just contact us by phone, fax or email (see contact information in the box on page 2).

## Questions and Answers

**Q:** What is the minimum that I can put in my foundation?

**A:** While there is no legal minimum, keep in mind that there are certain fixed costs which every foundation faces. These costs, for administration, compliance, bookkeeping, accounting, reporting, tax return preparation and filing, and the like should be at least offset by the tax or other benefits of your private foundation.

The minimum that makes it worthwhile, therefore, varies quite a bit. For example, if you use your private foundation to make gifts to foreign charities which would not be deductible if you made the gifts directly (see news item on page 2 of this issue), then

you will probably find it worthwhile to have a private foundation even if you give as little as \$10,000 a year.

On the other hand, if your main reason for having a foundation is to have your charitable assets earn on an income-tax-free basis, the minimum amount would probably be higher.

**Q:** Do I have to add to my foundation every year?

**A:** No. You have total flexibility to add whenever you want to.

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*If you would like to submit a question, please email Q&A@sterlingfoundations.com.*