

Creating a Supporting Foundation

A separate nonprofit charitable corporation (or charitable trust) which operates as a supporting foundation to Dade Community Foundation is an alternative to a private foundation and, for that matter, to an advised fund in Dade Community Foundation. Significantly such an entity qualifies as a “public charity” under the federal tax laws. Sometimes called an “affiliated foundation”, “supporting organization” or, by its statutory number, “section 509 (a)(3) organization”, it will be referred to here as a “supporting foundation”.

A supporting foundation may be established under state law in the form of a nonprofit corporation or a trust. Normally, a nonprofit corporation is used because such form of organization is generally more familiar and is usually more flexible.

A supporting foundation first must be structured to qualify as a tax exempt organization for charitable, educational, religious, etc. purposes under IRC Section 501(c)(3). The federal tax laws divide such tax exempt organizations into two categories: “private foundations” and “public charities”. Private foundations are subject to various restrictions which are not applicable to public charities.

Also, donors are generally entitled to larger deductions for contributions to public charities than to private foundations, as provided in IRC Section 170. This disparity became greater under the 1986 Tax Act.

The term “public charities” applies to three kinds of organizations defined in IRC Section 509 (a)(1), (2), and (3). The first two types generally encompass publicly supported organizations, such as a school, church, hospital, or community foundation. The third kind is a supporting foundation which is generally supported or endowed by an individual, a family, a corporation or similar close group, but which is entitled to public charity status under the tax law by reason of its affiliation with one or more other public charities of the first or second kind and by its compliance with other statutory requirements.

The two principal characteristics of a supporting foundation which are generally important to donors and which distinguish it from an advised fund in Dade Community Foundation are:

- (a) It is a separate entity outside the Foundation, having its own identity and usually known by the family name, and
- (b) One or more members of the family (or other persons designated by the founder) can participate officially as officers and directors of the Foundation (although they cannot control it).

Creating a Supporting Foundation

continued

To establish a supporting foundation described in Section 509(a)(3), each of these three separate tests must be satisfied:

A. Organizational and Operational Test:

The organization must be organized and at all times thereafter operated exclusively "for the benefit of, to perform the functions of or to carry out the purposes of" one or more specified publicly supported charitable organizations (hereafter "public charities").

B. Relationship Test:

The organization must be "operated, supervised or controlled by or in connection with" one or more public charities.

C. Control Test:

The organization must not be controlled directly or indirectly by one or more "disqualified persons, other than "foundation managers"" and other than one or more public charities.

A supporting organization is relatively complex. Thus, anyone who wants to create a supporting organization should consult with a tax advisor familiar with this area of the tax law. For example, the three relatively simple tests described above are further defined and discussed in more than 50 pages of tax regulations.

Reasons to Create A Supporting Foundation

A supporting foundation may be used in various situations:

1. A donor wishes to terminate a private foundation but desires to have a continuing role in the operation of a charitable fund. A supporting foundation can serve such a purpose. The private foundation can be "converted" to a public charity and will no longer be subject to the restrictions on private foundations, particularly with respect to limitations on grantmaking activities, as well as the tax on investment gains or income. Additionally, future contributions to this "converted" foundation will qualify for the maximum charitable deduction (unlike the case with contributions to private foundations).

2. The IRC Section 507 imposes a tax on certain conversions. Because the application of this tax is complex and can be large, anyone desiring to convert from private to public status should, before doing anything, consult with a tax advisor familiar with these taxation rules.

3. A donor who wants to create a charitable fund may wish to use stock in a closely-held corporation or other assets which might present management problems, risks or other burdens to which Dade Community Foundation should not be subject. By placing those assets in a supporting foundation organized as a separate corporation or trust, such assets can be independently managed and still provide the benefits stemming from being a "public charity". Such benefits include more flexible tax treatment for charitable gifts.

Creating a Supporting Foundation

continued

4. For example, consider a husband and wife who desire to have their family play a direct and continuing role in the program of a charitable fund to carry on the family tradition of community responsibility and participation. They also wish to maintain the identification of the family name with a separate charitable foundation. A supporting foundation, separately incorporated, bearing the family name and having members of the family on the Board, accomplishes these objectives.

5. If a donor wants to enjoy the status of a separate entity but does not wish to perform various administrative tasks (e.g. screening grant requests, managing assets, conducting an audit, etc.), a supporting foundation allows the donor to contract with Dade Community Foundation to perform some or all of these tasks.

A relatively simple way of qualifying a supporting foundation under IRC requirement Section 509(a)(3) is to establish a not-for-profit corporation that has as its purpose the support of Dade Community Foundation and which requires in its articles or bylaws that Dade Community Foundation elect a majority of the trustees or directors of the corporation. A disqualified person or members of his or her family may serve on the governing body but must be in a minority position and cannot have a veto over the actions of the majority.

The IRS will look at the actual operations of a supporting foundation and not only the formal documents. Therefore, it is essential that the supporting foundation's trustees or directors understand that such an organization must operate within the spirit as well as the letter of the IRC Section 509(a)(3) requirements.

Because Dade Community Foundation has broader charitable, educational and civic purposes than just about any other public charity, most donors contemplating the creation of a supporting foundation will find Dade Community Foundation a broad enough, flexible enough parent to link up with (i.e. "support"). So long as the supporting foundation's distributions are determined to be in furtherance of the community foundation's broad purposes, the supporting foundation can enjoy wide latitude in what it does and who it supports. Such conformance (as determined by those directors representing Dade Community Foundation) can be readily documented in minutes of the supporting foundation's board meetings.



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