Summer Newsletter
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GODFREY PEMBROKE
Financial Advice Specialists


Welcome to the Summer 2019 edition of GPL Outlook, where we look at how you can put a structure around your particular style of philanthropy. If you have any questions or would like to review your financial plan, please feel free to contact me.

Adviser Details
<Adviser Name>
<Details>

PHONE:
<Phone no.>

MOBILE:
<Mobile no.>

EMAIL:
<Email Address>

ADDITIONAL INFO:
<Additional details>

Tomorrow's Philanthropist

We are on the verge of the largest intergenerational wealth transfer in Australian history. Over the next 20 years, an estimated $3.5 trillion is expected to transfer to the next generation as the Baby Boomers pass on their wealth.[1] This presents enormous opportunities for philanthropy in the modern era and for those donors to make a lasting impact.

Throughout history, private charitable giving has undergone cycles of boom and bust. In each, the stimulus has most always been wealth creation and business innovation by private individuals, both of which were then turned towards solving the social problems of the day.

Charitable giving is now being rediscovered by a new generation of philanthropists. Over the last decade there has been considerable growth in giving from the wealthiest Australians[2], and as a high-income earner, you might be one of the growing force who feel a sense of responsibility to redistribute your wealth. While you might give directly to charities throughout the year, you may not realise there are efficient and tax-effective ways to give which can provide long term funding to the causes you choose to support.

There are three main options, all of which provide a structure that allows funds to be invested and managed, with income generated available for distribution to charitable entities. These structures include: private ancillary funds; public ancillary funds; and testamentary trusts. Each has different requirements and benefits, but all provide a structure that facilities a long-term philanthropic legacy.

Private Ancillary Funds

A Private Ancillary Fund (PAF) is a type of charitable trust that allows an individual, family or organisation to put aside a portion of money for charitable purposes in perpetuity. An individual donates capital into the PAF (generally starting with upwards of $500,000) and receives a tax deduction for the donation.

The capital is then invested long-term, and a minimum of 5% of the value of the PAF assets must be distributed as grants to charities each year. To be eligible, a charity must have Deductible Gift Recipient (DGR) Item 1 status, and plenty do – there are well over 20,000 charities to choose from. The PAF is controlled by a trustee who determines its philanthropic objectives and oversees investment and grant making strategies.

PAFs offer a number of benefits not available with other philanthropic options, including a high degree of control over the investment strategy and the ability to decide which charities will benefit. Generous tax deductions are also available for donations made to the fund - any income earned in the fund is usually tax exempt. A foundation also provides a focal point to keep succeeding generations aware of, and in touch with, the values you wish to impart.

However, the Australian Taxation Office (ATO) is responsible for regulating PAFs and has the power to impose penalties on trustees who don't comply with guidelines. Certain investment restrictions also apply to PAFs and the fund's assets must be valued at least annually (or at least every three years in the case of land).

Sub-fund in a Public Ancillary Fund

A Public Ancillary Fund (PuAF) has the same tax advantages as a PAF but is a communal structure. Unlike a PAF, there is no requirement to establish a new trust or trustee company, so a named sub-fund can be established immediately, and initial amounts are usually smaller with entry points from $20,000. A minimum of 4% of the PuAF assets much be given away each year, slightly lower than with a PAF, and the same range of charities can be supported. The investment strategy is usually a single strategy selected and managed by the provider (ie. unlike non-philanthropic publicly available managed investments such as super and unit trusts, there is not a choice of investment strategies).

New research released by Swinburne University shows that more than $123 million of donations flowed into these structures last financial year, with assets held in sub-funds totalling over $1 billion.[3] In fact, there are now more PuAFs than PAFs in Australia, demonstrating that while PAFs and big philanthropy may be more publicised, the accessible and convenient sub-fund is becoming more popular.

While the sub-fund market in Australia is yet to realise the boom experienced in the US with their equivalent, the Donor Advised Fund (assets held in Donor Advised Funds surpassed US$100 billion in 2017)[4], the flexibly of sub-funds are making it easier for people to give. For those of you who have a reasonable amount of capital to donate, but not hundreds of thousands of dollars, and who wish to be involved in granting during your lifetime, a PuAF could be the best approach.

Attraction of immediate tax-deductibility

Structured giving in this way is an especially attractive strategy for donors who need a tax deduction now, and the flexibility to distribute the funds to charity over time. For example, pre-retirees in a higher tax bracket than might be expected in the future can bring forward multiple years of charitable giving and make a lump sum contribution to a fund. It gives the donor the tax deduction needed while they are still earning assessable income but allows them to continue a regular flow of charitable giving throughout retirement.

Testamentary trust

There is also the option of a testamentary trust. These trusts are the oldest form of foundations in Australia with some, including the Wyatt Benevolent Institution and the Felton Bequest, now in their second century. These are established by the will of the benefactor and do not come into operation until after their death. The structures can attain income tax exempt status as a tax concession charity from the Australian Charities and Not-for-profits Commission (ACNC) but donations to them are not tax deductible.

They also must fund the charitable purposes specified in the will. However, the beneficiaries of the testamentary charitable trust do not necessarily need to be registered as Deductible Gift Recipients with the ATO. This gives the trustees greater flexibility in carrying out the benefactors wishes in the administration of the trust.

Which option is best?

If you want the confidence and peace of mind that comes from establishing a structured philanthropic program that you can contribute to during your lifetime, you may want to consider a PAF or a PuAF.

The ultimate choice will, however, depend on a range of factors, including your goals, the degree of control you want and the amount you'd like to donate.

To find out the best approach (and ensure the chosen arrangement is properly implemented) you should speak to your financial adviser who can provide you with specialist support and advice from philanthropic experts. Regardless of which structure you choose, all provide the benefit of allowing family members across multiple generations to become involved in the causes that are most important to you.

[1]McCrindle, 2016, Wealth Transfer Report, A Report for No More Practice, September.

[2]JBWere, 2018, The Support Report: The changing shape of giving and the significant implications for recipients, June.

[3]Swinburne University, 2019, Snapshot of sub-funds in Australia.

[4]National Philanthropic Trust, 2018, The 2018 DAF Report.

Setting up a Private Ancillary Fund: Rewards and Benefits

Developing philanthropic goals together can have a positive impact on any family. A Private Ancillary Fund (PAF) can help bring different generations together and embed family values, while having a positive impact on the community.

A PAF is a great way to engage family members in your giving and can bring a different type of conversation to the dinner table. The engagement around grant making decisions can often change family dynamics - encouraging children to develop their own priorities for supporting charities can promote family cohesion, inspire future generations, and help to build a family legacy that everyone can share.

There are some fundamental rules that apply to PAFs and these kinds of foundations require management by a corporate trustee. However, with the right support, a PAF can provide a range of benefits to you, your family and, most importantly, the community.

Who can be a trustee of a PAF?

A PAF is a charitable trust controlled by a company as Trustee. Most of the directors of the Trustee company can be family members or business associates provided that at least one of the directors is an independent person who is a 'responsible person' who is not the founder or a donor who has contributed more than $10,000 to the fund.

"The directors of the Trustee have the ultimate responsibility for the governance of the PAF," says David Ward, Technical Director of the Australian Philanthropic Services.

"This is usually family members (parents and grown up kids) with the obligatory independent responsible person (often the family lawyer or accountant). It is also worth considering appointing a specialist administrator, who can ensure compliance with the technical aspects of running a PAF," explains Ward.

The Australian Philanthropic Services is a not-for-profit organisation that inspires effective philanthropy, and provides education and practical support for individuals and advisers. The organisation often helps set up private ancillary funds for individuals, families and businesses across Australia.

"A PAF is a tax-effective, family controlled giving structure which can bring a family together in their support of the community and help those less fortunate than themselves," continues Ward. "It is a trust that can be established in perpetuity, but the directors are also human so establishing a succession plan for children (or grandchildren, or nieces and nephews) to take over as directors and run the PAF is an important consideration."

"If there is not anyone to assume the reins to ensure the long-term running of the PAF however, a PAF can be rolled over (or ported) into a public ancillary fund, and a letter of donor intentions lodged with the trustee to guide perpetual giving," says Ward.

Designing an investment strategy

Philanthropy can be hugely personal, and making decisions about long-term grantmaking can be difficult. Andrew Carnegie, widely regarded as the father of modern US philanthropy, reportedly said it was "easier to make money than it was to give it away." Having a PAF enables a family to make those decisions together.

You will need to design an investment strategy that will provide long-term capital growth and a regular flow of income to meet your foundation's objectives in perpetuity.

State trust law requires that the trustees of all foundations, including PAFs, have regard to several matters, including the benefits of diversification and the need to consider mission, risks, costs and tax when investing trust funds. The PAF Guidelines (2009) also set further specific restrictions. All of these need to be incorporated in the investment strategy and considered as part of the annual investment review.

There are a number of favourable tax advantages relating to a PAF that generally allow them to generate better long-term returns than an equivalent investment outside a PAF.

For example, subject to the terms of your will, a donation to an existing Deductible Gift Recipient (DGR) status approved PAF through your will removes capital gains tax on the assets donated. This increases the value of your foundation, allowing it to provide more support for your chosen charities.

"PAFs can register as a charity," says Ward, "and thereby attain income tax exemption, and the ability to reclaim from the ATO in cash any franking credits attached to dividends received form Australian companies."

"One of the key benefits of putting a structure, like a PAF, around your giving includes the ability to give money away whilst also growing your philanthropic capital in a tax-free environment," explains Ward. "Good returns can see the amount you have to give away grow over time."

It is important that you speak to your financial adviser who can assist you with an investment strategy for your PAF that maximises these benefits. You should also consider obtaining legal and tax advice before establishing your foundation, as every donation you make to your PAF is irreversible.

Make a lasting impact

At the very largest end of giving, the nation's biggest donors are the Paul Ramsay Foundation at $85.8 million, followed by the Minderoo Foundation ($60.4 million), established by Andrew and Nicola Forrest[1] - Andrew Forest is the chairman and major shareholder of iron ore company Fortescue Metals Group.

Andrew and Nicola Forrest, along with fellow Australian Len Ainsworth, are also members of the Giving Pledge which asks for a commitment by the world's wealthiest individuals and families to dedicate a majority of their wealth to giving back (www.givingpledge.org). After commencing in August 2010 with 40 members, led by Bill and Melinda Gates, there are now 204 pledgers from 23 countries.

While giving at this level is not an option for most individuals, through a structured approach to philanthropy you too can become an important 'change maker', transferring the same attitudes, skills and networks that helped build your wealth to bring about real social change.

With the right advice, PAFs are simple to establish and administer, provide a tax-effective strategic solution to grantmaking decisions, and offer many rewards for individuals and families, that can last a lifetime – and beyond.

[1]Australian Financial Review Philanthropy 50 List 2019, May 2019.

Philanthropic giving via a Public Ancillary Fund

Sub-funds are one option available to structure your philanthropy. They can be thought of as a form of 'giving account' which sits within a larger public foundation, and are generally fast to establish. They are particularly attractive to those who want to focus first and foremost on giving.

A Public Ancillary Fund (PuAF) is a communal tax exempt philanthropic trust that enables a number of donors to establish and name a 'sub-fund' under the broader PuAF structure. With a sub-fund, you do not need to worry about the trustee obligations and responsibilities associated with a Private Ancillary Fund (PAF) and can instead put your energy into choosing the charities you would like to support.

There are a range of providers with whom you can establish a sub-fund. These include community foundations, wealth managers and trustee companies. Your financial adviser can help you in selecting a PuAF which aligns with the values you wish to impart in your charitable giving.

Anyone can donate to a donor sub-fund and its purpose is to collect donations from the public. Once you donate, the funds are credited against your sub-fund and are then invested together with the assets of all the other sub-funds managed by the provider, to generate a return.

Making grants

The minimum grant is 4% of the opening 30 June value of the sub-fund each tax year. The Trustee will advise the amount, but any amount above this minimum is also possible.

Like a PAF, grants must be to an eligible Deductible Gift Recipient (DGR) endorsed as DGR Item 1 by the ATO. The grant recipient must also be a registered charity with the Australian Charities and Not-for-profits Commission (ACNC).

It is important to note that the Trustee of the PuAF has the final decision on grants. Therefore, if you establish a sub-fund you are not entitled to direct, but only to recommend, the disbursement of your funds. Unlike a PAF, you will not have complete control over where your grants are directed.

"A PuAF must have a single investment strategy covering all giving, or sub-funds", says David Ward, Technical Director of the Australian Philanthropic Services. "The nature of that investment strategy is one of the factors to be considered in choosing a giving fund provider, with other key facets being investment performance, the approach to portability, fees, frequency of reporting, and availability of granting windows."

How much control do you have?

The Board of Trustees of the PuAF has complete control over all aspects of the investments held. However, you are free to choose the DGR recipients within the guidelines and also to name your sub-fund. There are also minimums imposed by Trustees for grant amounts (such as $1,000) and donations (for example $5,000). The Trustee may also undertake its own due diligence on the recommended charity before approving a grant recommendation.

"The Trustee of the PuAF is responsible for all the investments of that fund and they are obliged to review the investments each year and make changes they deem as most prudent," explains Ward. "However, any such changes would normally be communicated to giving fund holders."

"There are PuAFs that apply ethical screens to their investments to different degrees, and you can certainly ask trustees about the investment strategy of the fund," says Ward.

Other considerations

There are also fees involved. Generally, the fee charged for a PuAF is 1%-1.5% p.a. of the value of the sub-fund. This covers all aspects of running expenses such as administration, compliance and investment costs. You should speak to your financial adviser who can help you understand the fee structure of PuAFs and how this might impact your investment position.

Giving in Australia

Total giving to Australian charities in 2016 was $10.5 billion, according to data from the Australian Charities and Not-for-profits Commission . About $1.5 billion of that was 'structured philanthropy' – that is, philanthropy through legal structures such as a PAF, PuAF or testamentary trust.

"Philanthropy is open to every member of society," says Ward. "However, using a long-term structure makes most sense for those with more resources starting from $50,000 for a giving or sub-fund (some providers allow lower amounts) through to over $1m for those wanting a standalone independent foundation."

"Ancillary funds, whether a PAF or a giving fund in a PuAF, have the advantage of donations being income tax deductible," explains Ward. "Utilising other structures such as testamentary charitable trusts established under a will are not as tax effective. While philanthropists are driven by the desire to give back or contribute to the community, doing it in a tax-effective way maximises the benefits that flow to the community organisations being supported."

You may decide to establish a separate legal giving structure for a variety of reasons. You may wish to build a solid governance structure around your giving to enhance its effectiveness; you may want to involve your family; or, you might just simply want to build a legacy that can continue to contribute to the community. Whatever your motivation, there are efficient and tax-effective ways to put a structure around your particular style of philanthropy and ensure your legacy continues for many years to come.

[1]ACNC, Australian Charities Report 2017.