By: Elizabeth McGuigan | June 3, 2021

Policy Brief

No Evidence Family Foundations Claim Higher Expenses

In a February 2021 debate hosted by the American Enterprise Institute (AEI), Howard Husock and Ray Madoff discussed donor-advised funds (DAFs) and what—if any—changes should be made to DAF rules.[1]

During the discussion, Madoff questioned whether family foundations should be able to count the salaries and travel expenses of family members as administrative expenses that count toward the five percent payout requirement for private foundations, or if this should be reserved for nonfamily staff expenses.

She said, "People are told that they can hire their children to work in the private foundation and they can spend their … time in Bermuda and deduct those expenses for when they have their family meeting. And we think these are really degrading to the sense of what the purpose of the charitable deduction is and that is why the proposals in the Initiative to Accelerate Charitable Giving would not allow those to count for purposes of the five percent."

While Madoff's comment is targeted at clear instances of abuse, she offered no specific evidence this is widespread through family foundations. Surely one can hypothesize scenarios of misuse of funds and conflicts of interest for any type of organization. However, her underlying skepticism raises a question—do family foundations have higher expenses relative to grantmaking than nonfamily foundations?

One multi-year prior research project concludes the answer is "no." In 2008, the Urban Institute, the Foundation Center, and Philanthropic Research, Inc published a study called, "What Drives Foundation Expenses & Compensation: Results of a Three-Year Study."[2] The authors sought to determine what factors drive administrative and operating expenses by analyzing expense and compensation data from the 10,000 largest foundations in terms of giving.

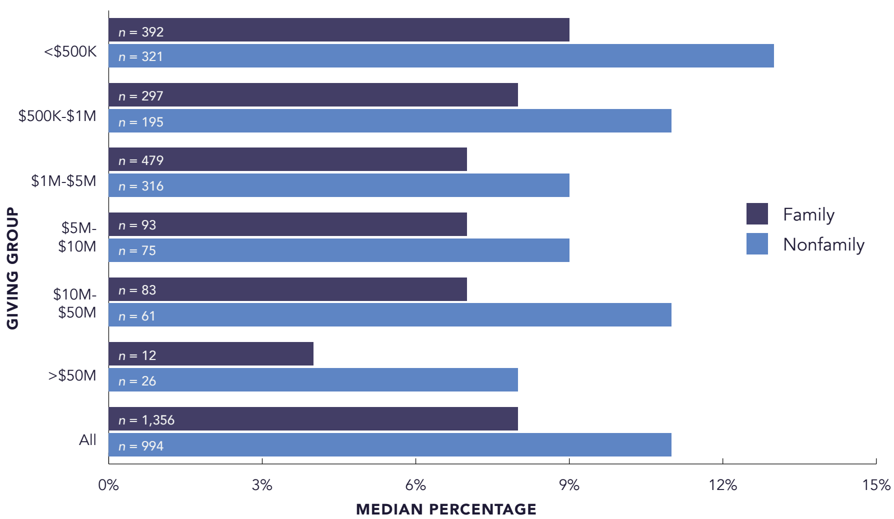
The authors describe charitable operating and administrative expenses as "costs incurred by foundations related to their charitable mission," including expenses for grants administration and non-grant charitable activities, such as accounting or legal services. As these expenses count toward the five percent payout requirement for foundations, much attention is—and should be—devoted to determining whether these expenses are justified in terms of meeting a foundation's charitable mission.

Key to the authors' findings is that family foundations tend to have a smaller percentage of administrative expenses relative to total qualifying distributions than nonfamily foundations. They conclude, "family involvement is one of the few characteristics that notably reduces the charitable administrative expense–to–qualifying distribution ratio for staffed foundations."

This holds even for the largest family foundations. In fact, the 2006 iteration of the Urban Institute study found as larger family foundations achieve economies of scale, the expense ratio consistently declined as giving increased.[4] But the nonfamily foundations

Charitable Administrative Expenses as a Share of Qualifying Distributions, 2001-03: Family versus Nonfamily[3]

(Staffed Independent Foundations)



Source: "What Drives Foundation Expenses & Compensation? Results of a Three-Year Study," Copyright (c) 2008, The Urban Institute, the Foundation Center and Philanthropic Research, Inc.

The Urban Institute et al study found that:

"The lower median expense–to–qualifying distribution ratios for family foundations compared to nonfamily foundations suggests that family members hold staff-related costs down by providing no- or low-cost labor for administering grants and other programs. Some family members also contribute office space and administrative services, such as legal and accounting, thereby lowering expenses."

1 American Enterprise Institute Web Event, "Are we giving fast enough? Donor-advised funds and the state of philanthropy," Feb. 26, 2021. https://www.aei.org/events/are-we-giving-fast-enough-donor-advised-funds-and-the-state-of-philanthropy-2/

2 Elizabeth T. Boris et al, "What Drives Foundation Expenses & Compensation? Results of a Three-Year Study," Copyright (c) 2008, The Urban Institute, the Foundation Center and Philanthropic Research, Inc. https://www.urban.org/sites/default/files/publication/31466/411612-What-Drives-Foundation-Expenses-and-Compensation-.PDF

3 Elizabeth T. Boris et al, "What Drives Foundation Expenses & Compensation? Results of a Three-Year Study," Copyright (c) 2008, The Urban Institute, the Foundation Center and Philanthropic Research, Inc., Page 32, Figure 3.5. Data from NCCS-Foundation Center-Guidestar, Foundation Expenses Data Set, 2001-03, https://www.urban.org/sites/default/files/publication/31466/411612-What-Drives-Foundation-Expenses-and-Compensation-.PDF

did not report the same economies of scale. The authors say, "The difference in charitable expense levels between family and nonfamily independent foundations was greatest for the largest foundations—less than four percent compared to over eight percent."

But what if something has fundamentally changed since this analysis? We dug into the data for a handful of foundations to see if the association still held. On one side of the scale, we looked at the Form 990-PF data for the foundations publicly backing the Initiative to Accelerate Charitable Giving. Among other provisions, these groups support limits on the ability of family foundations to allocate the costs family members accrue toward payout.

For our anecdotal sample, we looked at the foundations listed as members of the Initiative on its website: Arnold Ventures, Ford Foundation, Hewlett Foundation, High Tide Foundation, MGR Foundation, TomKat Foundation, Wallace Global Fund, and W.K. Kellogg.[7] While this is far from a random sample of nonfamily foundations, it is only fair to consider those calling for changes to how their family foundation counterparts are treated.

Laura and John Arnold switched over from their foundation to an LLC, Arnold Ventures, in 2019.[8] So we used 2017 as a sample year to keep this informal analysis apples-to-apples, as John Arnold is a co-developer and vocal proponent of these reforms. Naturally, their LLC will not face the same transparency or requirements as would a foundation.

On the other side, we looked at the data for eight of the largest family foundations in terms of assets.

Unsurprisingly, there is little difference between the family foundation expense ratios and those of nonfamily foundations. The foundations publicly supporting the Initiative had an average expense ratio of about 10%. The large family foundations' average expense ratio came in around 9%. While critics can find the unfortunate and rare examples of "bad apples" in the charitable space, vilifying those who work for family foundations and happen to share the last name of the family may not be supported by data. In this time of increased need, let's keep the focus on the good work that all foundations and other charitable organizations are accomplishing.

Expense Ratios for Foundations Supporting the Initiative to Accelerate Charitable Giving

Foundation	Charitable Administrative Expenses (2017 unless noted)[5]	Qualifying Distributions[6]	Ratio
Laura and John Arnold Foundation	$17,072,352	$176,911,101	10%
Ford Foundation	$129,184,321	$764,973,289	17%
Hewlett Foundation	$41,975,789	$473,430,130	9%
High Tide Foundation (2018)	$87,739	$15,468,645	1%
MGR Foundation	$10,304	$220,304	5%
TomKat Foundation	$363,178	$6,513,178	6%
Wallace Global Fund II	$2,371,008	$16,478,411	14%
W.K. Kellogg	$78,609,340	$426,343,571	18%
Average			10%

Expense Ratios for Large Family Foundations

Foundation	Charitable Administrative Expenses (2017 unless noted)[9]	Qualifying Distributions[10]	Ratio
Bill & Melinda Gates Foundation	$928,089,920	$5,456,962,565	17%
Bloomberg Family Foundation	$13,996,374	$448,768,802	3%
The David and Lucile Packard Foundation	$36,955,031	$403,153,759	9%
Walton Family Foundation	$36,403,953	$562,381,888	6%
John Templeton Foundation	$16,539,907	$145,249,619	11%
Charles Stewart Mott Foundation	$15,743,468	$140,133,683	11%
Susan Thompson Buffett Foundation	$23,749,039	$618,843,949	4%
Conrad N. Hilton Foundation (2018)	$19,961,523	$175,293,657	11%
Average			9%

4 Elizabeth T. Boris et al, "Foundation Expenses & Compensation: How Operating Characteristics Influence Spending," Copyright © 2006. The Urban Institute, the Foundation Center, and Philanthropic Research, Inc., https://www.urban.org/sites/default/files/publication/50481/311281-Foundation-Expenses-and-Compensation.PDF

5 Source: 990-PF forms, Part 1, Line 24, column (d)

6 Source: 990-PF forms, Part XII, Line 4

7 The list of supporting foundations was last accessed on March 30, 2021 here: https://acceleratecharitablegiving.org/about/

8 Kelsey Piper, "Why this billion-dollar foundation is becoming a corporation," Vox.com, Feb. 7, 2019, https://www.vox.com/future-perfect/2019/2/7/18207247/arnold-foundation-corporation-nonprofit-charity

9 Source: 990-PF forms, Part 1, Line 24, column (d)

10 Source: 990-PF forms, Part XII, Line 4