How to Give Abroad: The Mechanisms of International Grantmaking

As we have written before, Americans are increasingly looking internationally to put their philanthropic dollars at work. Once strategies were set, corporations, financial firms, community foundations, wealth advisors, and individual donors alike have found themselves searching for tax-effective solutions to give abroad. As you may guess, identifying the best options for international charitable giving is rarely straightforward. Below are some of the most common methods of tax-effective international giving that are accessible to both individuals and organizations.

Giving to U.S. Based 501(c)(3) Nonprofit Organizations Operating Abroad

The most straightforward method of international giving is through IRS-recognized 501(c)(3) nonprofit corporations that have programs abroad. Individuals and corporations who make a contribution to a U.S. charitable organization are entitled to an income tax deduction under Internal Revenue Code Section 170. The contribution is deductible if made to, or for the use of, an exempt organization or generally for the benefit of the public. When giving to a U.S. 501(c)(3) in this manner, the donor is essentially funding a program or project of the nonprofit that they run abroad. Most U.S. citizens are familiar with this in the context of disaster relief campaigns, when a U.S.-based nonprofit will fundraise for relief efforts that are ongoing in other countries. The benefit of giving in such a way is that the donor has the right to earmark their donation for the foreign program, as long as the domestic charity has full control over its operations. However, if the donor is looking to tax-effectively support grassroots organizations located in a foreign country, this avenue does not permit such activity.

Donor Advised Funds:

As a growing number of individuals and corporations are already doing, donors may choose to establish a Donor Advised Fund (DAF). The Pension Protection Act defines a donor advised fund as a fund or account owned and controlled by a sponsoring organization, over which the donor or an appointed advisor “reasonably expects to have, advisory privileges with respect to the distribution or investment of the funds”. In short, a DAF allows a donor to make a tax deductible contribution of cash or non-cash assets (such as stocks or real estate) to an account, which is held at the sponsoring organization and receive a tax benefit in the same year as the donation. The sponsoring organization manages the fund (which can be invested), while affording the donor the ability to recommend grants from the fund to operating charities on their own timetable.

The sponsoring organization may be a community foundation, an independent public charity, or a religious organization, but funds managed by financial services companies such as Fidelity Charitable, Vanguard Charitable, and Schwab Charitable are currently the largest.

Contrary to what one may assume, these larger DAFs and most DAFs held at community foundations are often not in the business of international giving. Some U.S. public charities, among them CAF America, have been filling this gap and provide DAFs as a solution for philanthropists interested in giving internationally. It should be noted that, prior to granting to any foreign recipient, these organizations (1) conduct their own extensive due diligence to ensure that the foreign charity recommended by a donor advisor is a U.S. 501(c)(3) equivalent or that the funds will be used for exclusively charitable purposes (2) impose reporting obligations with respect to grants made to a foreign charity and (3) often comply with strict anti-money laundering and terrorist-financing prohibitions and regulations. Such practices have the clear benefit of mitigating risks and protecting the donor's reputation. By law, contributions to these DAFs become the property of the public charity. While the donors can suggest for grants to be made from the fund to foreign charities, the charity maintains full discretion and control over these funds.

DAFs allow for individuals, families, and corporations to fund nearly any charitable organization or project across the world, so long as the sponsoring organization is able to successfully vet the recipient and determine that it complies with the IRS protocols of expenditure responsibility or equivalency determination, as well as the applicable anti-money laundering (AML), anti-terrorist financing and other relevant requirements.

"Friends of" Organizations

U.S. "Friends of" organizations are established for the purpose of raising funds in the U.S. that will ultimately be distributed to a foreign charity with which they are connected. Although the funds they receive are distributed internationally, "Friends of" organizations are typically organized to meet the legal requirements for contributions to be deductible for U.S. tax purposes, i.e. they are public charities. Most of these organizations will be called "The (American) Friends of …" and rely on alumni networks or connected donors in the U.S. for funding. Some common types of "Friends of" organizations include museums, operas, religious institutions, and universities.

These organizations must maintain control and discretion over the donations they receive so as not to become merely a channel for foreign funding. Commonly referred to as the "conduit issue", this is a universal concern among "Friends of" organizations, and addressed through various safeguards as they must not be under the control of the foreign beneficiary organization or the donors. As such, to avoid being regarded as a conduit entity, these organizations should have a board that maintains full discretion and control over the use of the donations, should have a majority of board members who are not also board members of the foreign organization, should carry-out their own charitable purposes other than simply

supporting the foreign organization, and their fundraising materials must inform the potential donors that their donations are under the independent control of the U.S. organization.

“Friends of” organizations are ideal for donors who are only inclined to give to a single organization (e.g. their alma mater). However, operating such an organization is often expensive and tends to only be worth the expense for foreign organizations that are well established or have a substantial donor base in the U.S. For more information about “Friends of” organizations, read CAF America CEO, Ted Hart’s blog here.

Direct International Grants

In addition to the avenues described above, philanthropists, whether individuals or corporations, have the option to make direct international donations to foreign organizations. Private foundations can make direct international grants, however, they face penalty taxes if these grants are not made with expenditure responsibility or equivalency determination — the protocols established by the IRS. However, direct contributions by individuals or corporations to a nonprofit (or equivalent foreign term) created or organized under foreign law are not deductible for U.S. tax purposes. Therefore, individuals and corporations may wish to pursue any of the above avenues for tax-effective giving.

Beyond lacking an option for tax deductions, other concerns linger with making direct gifts, namely that without undertaking any type of due diligence procedure (as done by sponsoring organizations of DAFs and by private foundations), the donor can be exposed to significant risk. It may be the case that the donor ends up potentially financing something other than intended, such as a different project at the recipient organization or even funding bribery or terrorism. Furthermore, with direct gifts, the recipient organization is not legally required to report back to the donor on how their funds were spent and the donor will be able to maintain very little, if any oversight over the funded project. This not only exacerbates concerns about risk but also means that the recipient organization does not have to produce any type of impact report for the donor.

While the above list of giving options is not exhaustive, for most philanthropists looking to give internationally, these options (not counting direct gifts) will be the most appealing as they offer tax-deductibility and other assurances. To varying extents, donors will find that the philanthropic sector is quickly adapting to meet the demand to tax-effectively give abroad.