

J. A. WEDUM FOUNDATION COMMUNITY FOUNDATIONS PROGRAM ANSWERS TO FREQUENTLY-ASKED QUESTIONS (FAQ'S)

The J. A. Wedum Foundation has established a program to create community foundations in Minnesota cities which do not have a general community foundation, although they may have special-purpose foundations or family foundations. Community leaders who are considering the creation of a community foundation, or have already created one, ask many good questions, and this document is an attempt to answer the most common questions in writing.

For simplicity, the term “community foundation” will often be abbreviated as “CF.” Third-person plural pronouns such as “we,” “us,” and “our” mean the J. A. Wedum Foundation. Second-person plural pronouns such as “you” and “your” mean leaders of communities who are considering a CF or administering a CF. Any use of the first person singular such as “I,” “me,” or “my” will indicate that the opinion expressed is that of the primary author of these answers, Dayton Soby, a trustee of the J. A. Wedum Foundation.

1. WHAT IS A COMMUNITY FOUNDATION AND WHY SHOULD A COMMUNITY HAVE ONE?

Under our program, a community foundation will be a Minnesota nonprofit corporation that qualifies as an IRS 501c3 public charity (tax exempt and tax deductibility). A community foundation can play a significant permanent role in preserving, strengthening, and enhancing a community and community life. A detailed answer to this question can be found in our four-page essay entitled “Why Should a Community Have a Community Foundation?” which you can read on our website, “wedumfoundation.org,” under “community foundations.” This is where you should start. This essay may be attached to this FAQ document if it is being e-mailed to you.

2. WHY DO WE WANT TO CREATE COMMUNITY FOUNDATIONS?

Our mission is to “positively change and improve people’s lives,” and we strive to utilize our charitable resources in ways that will have the greatest possible impact over the longest possible time period. We concluded that creating community foundations is a great way to accomplish our charitable goals and benefit the communities and people of Minnesota now and forever.

3. HOW WILL THE J. A. WEDUM FOUNDATION SUPPORT THE CREATION OF YOUR COMMUNITY FOUNDATION?

We will help you organize the CF and will pay the legal costs of creating the CF and obtaining IRS approval. We will also provide matching gifts at various stages of your fundraising, and we are prepared to expend up to \$40,000 for each CF created. The details of our program for establishing CF’s can be found in a two-page statement entitled “Program to Create Community Foundations,” which you can read on our website, “wedumfoundation.org,” under “community foundations.” This program description may be attached to this FAQ document if it is being e-mailed to you.

4. HOW MANY COMMUNITY FOUNDATIONS HAVE BEEN ESTABLISHED SO FAR UNDER OUR PROGRAM?

Three CF's have been created and are functioning well through September of 2016, and we are in discussions with other communities. These first three Minnesota cities with new CF's are Brooten ("Brooten Community Foundation"), Lake City ("Greater Lake City Community Foundation," website: lakecityfoundation.org), and Nicollet ("Greater Nicollet Area Community Foundation," website: investinnicollet.org).

5. WHAT TYPES OF COMMUNITIES ARE ELIGIBLE FOR THIS PROGRAM?

Our program is for geographic communities, for example, city, city plus surrounding area, or county. Population size is immaterial. Brooten and Nicollet have populations of about 1,000 each and Lake City has about 5,000. We recommend that the community be one that is coherent and has a sense of community loyalty. You may choose your own name which identifies the geographic community.

6. HOW MUCH MONEY MUST YOU RAISE IN ORDER TO RECEIVE OUR FIRST MATCHING GRANTS?

We will establish an initial goal for gifts and pledges from your community by mutual agreement with you, understanding that cities are different from each other in population, economic circumstances, culture, leadership, and other realities. The initial goal should be significant enough so that the foundation will be viable and credible in the community, and we have suggested that the initial goal for a community should be at least \$40,000 so that the new foundation starts out with at least \$50,000 (including our first \$10,000 gift), but we are open to a proposal for a lower initial goal for a smaller community which more fairly reflects its population or financial capacity. Please see paragraph 2 of our policy statement (referred to at #3 of this FAQ document) for a complete statement of our policy.

As the CF's financial assets increase, the CF will have greater credibility when approaching donors and other foundations, the board members are likely to take their duties more seriously, and more and larger grants will have a greater impact in a community.

7. WHAT DOES OUR POLICY STATEMENT MEAN WHEN IT SAYS WE WILL PAY LEGAL AND ORGANIZATIONAL COSTS?

When it is apparent to us that you have organized yourselves with an appropriate plan and leadership group, and you have approved our prototype governing documents (with acceptable modifications by you), we will ask our attorney to create a Minnesota nonprofit corporation at our expense. After the Articles of Incorporation have been filed and this new legal entity (your new community foundation) has come into existence, it may choose to retain that attorney, or any other attorney, to complete organizational matters, and that attorney will be representing and advising you as your attorney, not as our attorney. Your attorney will take the steps described at #8 of this FAQ on your behalf. We note that the attorney must be representing you in order to

apply to the IRS for 501c3 status and otherwise communicate with the IRS, and the IRS requires that a Power of Attorney be filed.

We will pay the legal and related costs of creating the CF and obtaining 501c3 status, which are described in detail at #8 below, provided that the legal fees do not exceed the amount that would be charged if you selected our attorney as your attorney.

Once the organizational matters described in #8 are completed, and you begin to administer your new CF, you may continue to choose any attorney to represent you, in the event that you have any legal needs. You may not need an attorney if your CPA understands the legal compliance matters which will arise. Compliance matters are discussed at #13 of this FAQ document.

8. WHAT ORGANIZATIONAL AND LEGAL STEPS MUST BE TAKEN TO CREATE A COMMUNITY FOUNDATION AND BEGIN FUNCTIONING AS SUCH?

A. You must first assemble some leaders who will see the vision, make a commitment to creating your new community foundation, begin planning, and determine who the initial members of the board of directors should be. These leaders and the initial board members will not necessarily be the same people, since people have different interests, talents and availability. When your leaders make a commitment to create the new CF and to raise funds, and we see that you have an appropriate organizational plan, we will ask our attorney to proceed to create your new CF.

B. At the same time, you must decide who the initial board members (also known as “directors”) will be, since they will be named in the initial filing. This is a very critical step, which is discussed at #9 of this FAQ document.

If you are the visionaries and organizers, remember that you do not need anybody’s permission to create a community foundation. If you and we decide to do this, we can do it, and we will do it together. No local government, government official, community organization, community leader, or self-appointed negative grouch has any authority to stop or control your new CF. The CF will be governed and managed by the new board of directors. However, the new CF must act in a way that generates public respect and support, or it will not be successful.

C. The new CF, a Minnesota nonprofit corporation, will be created by the filing of Articles of Incorporation with the Minnesota Secretary of State. The Articles will state basic governing principles, name the first board, state the purpose of the corporation, and satisfy legal requirements.

D. Bylaws of the corporation will be prepared which will govern its proceedings, to be approved by the board at its initial meeting.

E. The board of directors at its initial board meeting will approve the Bylaws, elect the officers of the corporation, select an attorney, and take any other necessary actions.

Minutes of this meeting shall be recorded. At this point, the new CF has begun its legal functioning.

We believe that we have prepared very good prototype Articles of Incorporation, Bylaws, and first minutes, which have been used by our recently-created CF's. Your leaders should review them. We recommend these documents for your approval, but they may be modified at your request, since this is your foundation. We will pay the costs of carrying out items C, D, and E above, and F, G, H and I below.

F. Your attorney then, in consultation with you, prepares an application for 501c3 status as a public charity with the IRS. With this status, the CF is tax exempt and gifts to the CF are deductible for income tax purposes, and also for estate and inheritance tax purposes. Approval may take several months or more, but deductibility relates back to the time of a gift once approval is obtained. We anticipate approval since the other CF's we have helped to create, using the same documents, have received approval.

G. Your attorney will register your CF with the Attorney General of Minnesota, a legal requirement for an organization which will be seeking contributions.

H. Your attorney will provide you with a bound minute book in which you can keep governing documents and minutes of board meetings.

I. Your attorney will obtain a federal tax identification number for you (Employee ID#, "no employees").

Once these matters are completed, you are in business, as a public charity able to do what public charities do.

9. WHO SHOULD BE SELECTED TO SERVE ON THE BOARD OF DIRECTORS?

Your decisions regarding board members will likely determine the success or failure of your new community foundation. We refer you once again to our essay, "Why should a community have a community foundation?" (referred to at #1 of this FAQ document), which describes why this subject is so important. As stated in that essay, "It is absolutely critical that these directors be responsible and competent persons who are dedicated to their community, who are respected by the community and have a reputation for integrity, and they must exercise leadership and good judgment."

Board members must not only believe in the vision, and be enthusiastic about beginning this important legacy for their community, but they must accept responsibility to do their jobs and to accept responsibility for the success of the foundation. I have observed that on most boards, only a few leaders take that responsibility seriously, while others may sound supportive but just watch others do the work. Beware of people who like to control others without acting positively themselves. Nobody should be on the board who understands that his or her role is to represent, or be liaison to, another organization; responsibility is to this organization, not another.

Do not name anyone to your board whose motivation appears to be: “I find this very interesting.” “I am curious.” “I want to learn.” “I am knowledgeable about pertinent matters.” “I like to make policy.” “I am a good listener.” “I understand the community.” “I am well connected.” “I am willing to come to board meetings to listen and vote.” “I want to help choose grants.” These are all helpful motivations and qualities, but they are not by themselves sufficient. They do not indicate that someone is willing to lead and work. Look for people who say “I want to take action to make this foundation go.” A board member must be a competent person who is willing to lead and accept responsibility and carry it out. A board member must be willing to contribute financially and be willing and able to ask people to give money for this cause. If your board members are not willing to support their own foundation financially, why would a potential donor do so, and why should the J. A. Wedum Foundation do so?

The starting board should probably be 5 or 7, possibly 6, members. Choose them carefully. A larger board will likely collect a few of those referred to above who will slow you down or frustrate you. You can create committees, teams, or task forces to include other people (non-board members) in this enterprise and use them effectively to carry out your mission, including qualified leaders who do not wish to be board members. Varied expertise and talents are useful on the board, but remember that forming a board with people who are not on the same page, even if they are nice people, can stop you from being as successful as you ought to be.

10. WHAT ARE THE DUTIES AND RESPONSIBILITIES OF THE BOARD OF DIRECTORS?

- A. Directors have various legal duties, referred to as “fiduciary duties.” You should obtain from the Office of the Attorney General of Minnesota copies of its publication entitled “Fiduciary Duties of Charitable Organizations” and provide a copy to each board member, who should read this brief booklet.
- B. The Articles of Incorporation and Bylaws (the governing documents) will provide principles and processes for the board to follow, and directors should be familiar with their provisions.
- C. At its initial board meeting, the board approves the Bylaws, elects officers as provided in the governing documents, authorizes the establishment of a bank account and the officers who can sign checks, and takes other necessary and appropriate actions, all of which are recorded by the secretary in the minutes of the meeting. The attorney will provide the form for that purpose, and a representative of our board may be able to attend to provide guidance.
- D. The board of directors has the duty and authority to manage and govern all the affairs of the community foundation, including administration of its assets, business, programs, and projects, subject to the requirements of applicable laws and subject to the provisions of the Articles of Incorporation and Bylaws. Boards of directors of other organizations tend to be policy-making boards because they have employees to conduct business, but since a CF will not likely have employees until it gets much larger, the CF board

becomes an operating board which authorizes officers and board members to carry out certain tasks on behalf of the organization.

E. The board has the responsibility to find and elect new board members when needed, although the initial board is appointed in the Articles of Incorporation. While the constituency of a CF is the community, there is no legal constituency that elects board members, so the board is self-electing, that is, self-perpetuating, subject to rules in the governing documents. The fact that the board elects its own successors, including directors to fill vacated or increased openings, magnifies the importance of having directors with recognized integrity, competence, and commitment.

F. The board needs to deal with board members who fail to perform their duties as board members. If board members fail to show up at board meetings, fail to do the work that other board members are expected to do, or otherwise fail to carry out their duties, they should have the good sense to resign. Resignation is simply recognition that they are too busy or preoccupied, have health problems, are away from the community for much of the time, or are no longer sufficiently motivated to continue. It may be necessary for the board or its leaders to diplomatically suggest that inadequately-performing board members should vacate their memberships to make room for someone who has the time, health, and motivation to carry out the duties of a board member. Ultimately, the matter can be resolved by declining to re-elect when a term expires.

G. The board is responsible to set financial goals and raise money to fund the new community foundation, and the directors are expected to actively lead the fund-raising. You may establish a committee, task force, or team which includes other supportive community members to assist with fundraising. You may decide to give recognition for levels of giving or create special recognition for founders or charter members. All fundraising matters are for you to decide, but we will advise as you may desire. When you have received cash and pledges at the various levels required in our foundation's policy, you will be entitled to receive the promised matching gifts.

H. The board is responsible for providing ongoing education to people who might care about their community, including both community residents and former community residents, such as people who grew up there, with the expectation that not only will some give to the foundation currently, but also that some will give later in life or as part of their estate planning. The major part of funding for your foundation is likely to come from bequests and beneficiary designations in the long run, which long run is well into the future, that is, forever.

I. The board will arrange for investment of foundation assets. Initial receipts should be deposited in a bank checking account, and when cash deposits have increased, the board will determine how the money should be invested. As assets begin to grow, the board should establish a written investment policy. Investment issues will be discussed at #12 of this FAQ document.

J. The board is responsible for establishing and monitoring appropriate financial accounting and reporting.

K. The board defines the mission, vision, goals, and strategies of the CF. The board decides what the CF will do, acting within the principles established in the Articles of Incorporation. The primary purpose of a CF is usually to create an endowment, the income from which is granted for community programs and projects. However, the CF is a public charity which is not limited to making grants to other charitable organizations, and can initiate and carry out its own charitable programs and projects. Please refer to our initial essay (cited at #1 of this FAQ document) for further commentary about this. Your CF can and should collaborate with other charitable organizations, community organizations, and governments in various causes that benefit your community. Leading such collaboration can be a significant goal for you. However, your CF is an independent nonprofit corporation and you do not need the permission of local government, local leaders, or other organizations to do what you decide to do.

L. The board has the responsibility and the right to decide whether to accept gifts that are given with conditions that might be unacceptable, and whether to accept non-cash gifts, for example, real estate, which come with risks that might be unacceptable.

M. The board may decide whether donations should be allocated to the endowment fund or for current programs and projects, but once assets are allocated to endowment, they should maintain that status. However, if donors request that donations be allocated for a certain purpose, they should be allocated accordingly. Generally speaking, it is important that donor intentions should be honored, for legal reasons, for ethical reasons, and because if donor intentions are not honored you can expect reduced donations in the future. As implied in the prior paragraph, the board should not accept donations if it is not willing to comply with donor intentions.

N. The board decides how to utilize funds of the foundation. It makes decisions regarding expenses being incurred with respect to fund-raising, education, and operations. It makes decisions regarding the amounts and allocation of charitable grants to others and the amounts and allocations for your own charitable programs and projects. You may support a broad range of causes that benefit your community, all of which are listed in our proposed Articles of Incorporation, which contain the same list of causes described in our essay entitled “Why Should a Community Have a Community Foundation?” (referred to at #1 of this FAQ document).

O. Directors must avoid conflicts of interest. While this rule is in effect from the beginning, at some point the board should develop a written conflict-of-interest policy.

P. The board is responsible to assure that the foundation annually complies with requirements of state and federal law. These compliance requirements are relatively simple, and are described at #13 of this FAQ document.

11. CAN SEPARATE FUNDS BE CREATED WITHIN YOUR COMMUNITY FOUNDATION?

Separate funds can be created within your CF, either permanent or temporary. There will of course be an endowment fund and funds for current programs or projects. Additional separate funds may be created by the board on its own or created in response to a gift with conditions by a donor that the board is willing to accept, and such separate funds may be created as permanent funds. Donors can be expected to request the creation of separate funds, which might be intended to benefit a specific organization (for example, a local school), or a specific type of cause (for example, education generally or education scholarships), or a general subject matter (youth or historic preservation), and they might specify some detailed requirements. The board will have to decide whether to accept these gifts, establish the separate funds, and carry out donors' intentions. There is potential for creating many such funds, but the desirability of that is subject to debate.

Having such donor-designated funds in your CF will certainly complicate the administration of your CF. However, they may also be consistent with your community mission, and they will increase the size and impact of your foundation. Two of the key questions for you to consider are how much is the gift and how complicated will it be to administer, and you will consider a balancing of these factors. You can accept more complicated conditions if the gift is a very large gift. Consider the amount of income you can generate annually for the intended purpose and whether such amount is worth the extra effort. I would not recommend setting up a separate fund for a gift of less than \$25,000, and you might reasonably set the amount much higher, for example, \$50,000 or \$100,000. You might remind the donor that the purpose of the CF is to provide broadly for community needs, with flexibility for an unknowable and unpredictable future (forever), and try to negotiate fewer and less complex conditions, or even convince the donor to make the gift a general grant without conditions. You might also suggest that the donor make the gift to another foundation which administers donor-designated or donor-advised funds such as one of the "lead foundations" discussed at #14 of this FAQ document, which is better equipped to handle such challenges, where the gift could still benefit your community without being administered by your board. Finally, we note that you will often receive small gifts when you are raising money for a current program or project which are designated for that purpose, or for a fund you have already established, and there is usually no reason not to accept those.

You may not accept any gifts for any purpose that may be unlawful or immoral, or intended to provide tax deductibility for a donor that the donor would not be entitled to take if he paid the money directly to the specified recipient.

12. HOW SHOULD YOUR COMMUNITY FOUNDATION INVEST ITS ASSETS?

You should first set up a bank checking account for your foundation, into which you can deposit donations, and from which you can pay expenses and grants, and in which you can hold your cash pending decisions regarding further investment. You should decide who can sign checks, with the usual stipulation that any checks beyond a small amount need two signatures. You could later establish a money market account with an investment company where you have other assets, with check-writing privileges.

As you decide how to invest your endowment funds, do not make any investment which incurs a “load” (commission), since there are hundreds of no-load mutual funds and investment advisors who are just as good as those who charge a “load.” While board members or community members may have helpful investment knowledge, you should avoid conflicts of interest and hard feelings, and possible distrust by donors, by deciding up front to not invest with local persons. I have sometimes heard directors or local advisors claim that the best investment for an organization happens to be the one they sell.

Any reasonable investment decision will involve consideration of such factors as your investment time horizon, your tolerance for risk, and your need for current income. Remember that your time horizon is the distant future, and you can accept risk if you are trying to grow the principal value of your assets and you are concerned about the long term and not the short term. You do not need income to fund operations of your organization as other charities do (for example, colleges), since you only need to fund minimal expenses and fund your grants and charitable programs and projects; that is, your foundation will not be in financial trouble if your investments are in a down period. This means that you can and should invest primarily in equities (stocks) since history shows that over the long run you will likely achieve greater growth in financial assets than with any other class of financial investments. You can reduce risk by diversifying your investments, and you can do this with mutual funds, whether by investing in a mutual fund which holds stocks of a number of companies or investing in several mutual funds which have different investment styles.

Some foundations will hire an investment advisor to choose investments, and you might decide to do so, but you should carefully consider the fees, which can add up to a lot of money over the years. Consider passive investing, which means investing in index funds such as an S & P 500 Index fund. Studies have shown that the S & P 500 Index outperforms almost all managed funds over a period of years, first of all because it IS the average of all managers, and since it has no costs it MUST outperform the average manager. Managers or managed funds normally charge from 1 to 2% fees per year, which means that only a very few can consistently outperform the index, and we cannot know in advance which ones they will be. I recommend Vanguard Investments (vanguard.com), one of the largest families of funds, with many dozens of funds to choose from, because they have the lowest fees in the business and are considered to be very competent and trustworthy. They have no shareholders, as they are owned by those whose funds they manage. They are the pioneers of index funds. Most importantly, they charge only 5 basis points as their annual fee for their Index 500 Fund (that’s .05 %, or 1/20 of 1%, almost free). Their fees for some good managed funds are about .25 or .30%. Two of the CF’s we have helped to create are moving their funds monthly into Vanguard index funds and managed funds. Vanguard representatives can provide free guidance to an individual CF about an appropriate allocation of funds for your foundation. Finally, note that Warren Buffett, the greatest investor of our time, recently disclosed publicly that he is establishing a trust for his wife with cash when he passes, and he has instructed his trustee to invest 90% of that money in the Vanguard Index 500 Fund and the balance in U. S. Treasuries.

13. WHAT LEGAL COMPLIANCE IS REQUIRED, MEANING WHAT ACTIONS MUST THE COMMUNITY FOUNDATION TAKE EACH YEAR TO COMPLY WITH LEGAL REQUIREMENTS?

Certain actions are required annually, which are set forth in response to the following questions. They are relatively simple steps, and should not discourage you from establishing a CF, but because they are technical, a qualified tax professional should assist you. Our policy provides that we will reimburse you for up to \$2,000 for your CPA costs incurred in your first year, and thereafter you may be able to obtain pro bono services or get this work done at minimal expense.

A. What actions must the community foundation take each year to comply with federal law and to maintain its status with the IRS as a 501(c)(3) charity?

In general, the charity must keep accurate and complete books and records during each year. This includes tracking and recording all financial transactions and keeping updated and complete minutes of board meetings. The board should meet at least once each year and more frequent board meetings are recommended.

In addition, a 501c3 public charity has the obligation to file an annual IRS form 990 with the Internal Revenue Service. This filing should be completed with the assistance of a CPA or attorney knowledgeable about the tax status and operations of nonprofit organizations.

For an organization with gross receipts of less than \$50,000 annually, a postcard form 990-N can be used. For organizations with gross receipts of less than \$200,000 annually and total assets of less than \$500,000, a form 990EZ or a form 990 can be used. For organizations with gross receipts in excess of \$200,000 or assets of more than \$500,000, a form 990 must be used.

Consultation with a qualified tax professional is required to determine which form is to be used and the filing deadlines and extension periods for each form.

B. What actions must the community foundation take each year to comply with state law and to maintain its status as a Minnesota nonprofit corporation and a qualified charity?

(1) An annual renewal of a nonprofit corporate registration must be filed with the Minnesota Secretary of State before December 31 of each calendar year following the year its Articles of Incorporation were filed. Minn.Stat. 317A.823. This is typically done by the tax preparer for the organization in connection with the filing of federal form 990.

(2) Before an organization can solicit contributions, an organization must register with the Minnesota Attorney General's office (Minn.Stat. 309.52, subd. 1). There are exemptions for organizations that do not plan to receive more than \$25,000 in any year (unless it employs a professional fundraiser) (Minn.Stat. 309.515, subd. 1(a)). Since you will hope to raise more than \$25,000 in some years, you should register with the Attorney General.

(3) Once registered with the Attorney General, you must file an annual report with the Attorney General on or before the 15th day of the seventh month following the organization's year end. Minn.Stat. 309.53, subd. 1. Since you will likely use a calendar year, your report will be due by July 15th of each year. You will likely want professional assistance with this report, so you can be in compliance with all the detailed information required.

A booklet published by the Minnesota Attorney General's office, "A Guide to Minnesota's Charities Laws," contains a great deal more specifics and details about the annual reporting requirements for a nonprofit organization in Minnesota. The Attorney General's office invites calls regarding such matters at 651-296-3353.

C. What are the requirements for the community foundation, as a public charity, with respect to the amounts or percentages of annual charitable grants?

No specific grant or gifting requirements are imposed on organizations that are public charities. In contrast, a private foundation must make grants of not less than 5% of its investment assets each year. To continue its status as a public charity, however, the community foundation must itself demonstrate that it is fulfilling its charitable purpose. It can do that by direct participation in programs, projects, events and the like or it can promote that public purpose by making grants to nonprofit organizations that fulfill that public purpose.

We have been and are establishing CF's as public charities and not as private foundations. Because of that status and so long as it is maintained, a public charity has no mandated minimum level of gifts and grants.

14. WHAT IS THE DIFFERENCE BETWEEN AN INDEPENDENT COMMUNITY FOUNDATION AND A COMMUNITY FUND IN A LARGER FOUNDATION?

A community seeking to establish a community foundation needs to decide whether it will be an independent foundation, that is, a nonprofit corporation with its own 501c3 tax status, or a component fund within a larger 501c3 foundation. Such larger foundations which administer component funds include the six regional "initiative foundations" in Minnesota created by the McKnight Foundation, which are West Central Initiative, Southern Minnesota Initiative Foundation, Northwest Minnesota Foundation, Northland Foundation, Initiative Foundation, and Southwest Initiative Foundation. Other such larger foundations include Community Giving (formerly known as the Central Minnesota Community Foundation), the Minnesota Foundation, the St. Paul Foundation, and the Minneapolis Foundation. We will refer to these larger foundations as "lead foundations," a term used in a national study of these matters, for want of a commonly-used term or a better term.

The independent foundation owns and controls its own assets, programs, projects, grants, and everything else. It is a legal entity that can act on its own. Its sole loyalty is to its community and its donors. When a community establishes a fund within a lead foundation, all assets are transferred to the lead foundation to be held in a geographic component fund ("Fund") of that foundation. The assets in that Fund are legally owned by the lead foundation and held

permanently under the control of the lead foundation. The lead foundation must make grants for the benefit of the community which established the Fund, but makes all the decisions. The Fund is not a trust. The community has a local “advisory committee” or advisory “board” that raises money and recommends grants. The lead foundation will normally make grants as recommended, but is not always required to do so (see below). The Fund is referred to technically as the “[Community Name] Fund of the [Foundation Name].

This is similar to the situation where an individual sets up a “donor-advised fund” with a 501c3 foundation and transfers money to that foundation to be added to the individual’s designated fund (“the John Doe Fund of the X Foundation”). The gift is complete, the individual is entitled to a charitable deduction, and thereafter the charitable foundation has complete ownership and control. The donor may request that grants be made to donor’s favorite charities. Those grants will normally be made as requested, but not necessarily. A community’s Fund at a lead foundation is really a community-advised fund. The donor-advised fund has better application for an individual than for a community, because of the need for permanence after the individual’s limited life span, whereas communities are normally expected to continue to exist.

While the lead foundation has ownership and control of the community component Fund, it must satisfy legal requirements. It is required by the law of contracts to act in compliance with the terms of the community Fund agreement; however, it must also fulfill its fiduciary obligations to be sure that the requested grant meets the purpose of the Fund and that the grantee is an eligible organization to carry out the charitable activity and fulfill the grant conditions, which means that the lead foundation has sole discretion to determine the fit of the grant to the purpose of the component fund. Furthermore, the lead foundation has the variance power under federal law to modify, redirect, or decline to make a grant, if the grant, or any restriction or condition “becomes, in effect, unnecessary, incapable of fulfillment, or inconsistent with the charitable needs of the community or area served.” The lead foundation understands that it can be sued if it fails to carry out legal requirements and that its reputation, as well as the reputation of the community Fund, depends upon its proper handling of its duties.

When donations are intended for the local Fund at a lead foundation, they should be made payable to the lead foundation and designated for addition to the community’s Fund. However, donation checks payable to the local community Fund or the so-called local “foundation” are normally forwarded to the lead foundation and deposited there.

The communities with component Funds often refer to their component Funds as “foundations” in their publications and communications. They are not separate legal entities. I do not believe they can correctly be called “foundations.” They are “Funds” within a 501c3 foundation. I believe the incorrect terminology may create misunderstandings and may create issues which are discussed under the following question #15.

15. WHY IS THE J. A. WEDUM FOUNDATION CHOOSING TO SUPPORT INDEPENDENT FOUNDATIONS RATHER THAN FUNDS IN A LEAD FOUNDATION?

Our intention and focus is to create independent foundations. Some communities should have an independent foundation and some should have a community fund in a lead foundation, as many

do. Each community should make its own choice. If a community wants a community fund in a lead foundation, there is no need for us to be involved, since there are a number of lead foundations which are ready, willing, and able to help. If a community wants an independent foundation, we are ready, willing, and able to help.

The initiative foundations and the other lead foundations in Minnesota which establish and manage community funds are admirable institutions. They are developing the philanthropic base throughout Minnesota. They do great things. Communities need foundations and community funds, and they are leading and fostering the creation of community funds that provide significant benefits to many communities that would otherwise have no community foundation or community fund. They provide significant expertise, experience, security, continuity, and simplification of administration for many communities.

We are all involved in the same philanthropic cause. We are not competitors. We have an understanding with one of these lead foundations that we will refer communities that want a community fund to them and they will refer communities that want an independent foundation to us. We are very open to working in that way with other lead foundations.

As you read the following paragraphs, remember that we respect all these lead foundations. We understand that they all may act differently from each other in some respects, and concerns raised may be more applicable to some than others. We do not intend to criticize, but are pointing out differences and expressing opinions with the intention that you will consider the differences, ask the right questions and make the best choice for your communities. You not only need to decide whether to choose the independent foundation or the component fund of a lead foundation, but, if you choose to be a component fund, you must decide which lead foundation is the best affiliation for your community.

If your community is considering working with a lead foundation, you should carefully review the fund agreement so that you clearly understand the terms and you can find the answers to the questions raised in this FAQ document, since these terms and answers can vary greatly from one lead foundation to another.

If you wish, we can refer you to more than one lead foundation so you can compare any differences between their documents and approaches. You should be well informed before making your choice.

I believe that there are a number of reasons why the independent foundation may be a better choice for your community. They are listed as follows, not necessarily in order of importance:

A. The independent foundation will always be completely controlled by the community, not by someone outside the community. Some lead foundations have declared that certain causes have priority, and those priorities often differ, and furthermore, those priorities may change over the years. Leaders will change in either organization, but I believe that the local leaders, being responsible to their own community and its donors, and being exclusively focused on their community, may be more motivated by what is best for their community than the more distant

leaders who have many other concerns and communities for which they are responsible. However, results may depend more on the quality of leadership than the type of legal structure.

B. I believe you can raise more money and raise it more easily if you have local ownership, control, and leadership, but again, the quality of leadership is an important variable. Some potential donors may be less motivated, and may be distrustful, when they find out you are raising money to send to a foundation located in another city, even if the money will be used for the benefit of their community.

C. You may achieve greater community engagement for the same reasons stated in the prior two paragraphs.

D. Donors to a component fund can write checks payable to the local “foundation,” as it may be often referred to, which will be passed on to the lead foundation and thus qualify for the charitable deduction. What happens when someone mistakenly lists the local “foundation,” rather than the lead foundation, on his or her income tax return and then, because there is no such foundation on the IRS list of qualified charities, the deduction gets disallowed and an audit results? Although the deduction will likely be allowed eventually, tax audits are unhappy events for donors.

E. There is some risk that a donor, perhaps a significant donor, will believe that he or she is supporting an independent foundation, especially if the local community fund is being called a “foundation,” as it often is, and the donor might demand return of the gift when the donor learns the true facts. I would expect the lead foundation to return the gift, but that result is not certain. If the gift is not returned, someone may be liable, although foundation insurance may cover that risk.

F. The most significant gifts will likely be from bequests, either specific cash or property gifts or gifts of a percentage, possibly even 100%, of the residuary estate. If the gift is a large amount, the deceased person’s relatives might be very unhappy about that. If the gift is made to the “X Community Foundation,” and there is no such foundation, only a fund at a lead foundation, the gift may be challenged. The gift may then fail because there is no such foundation, or because the testator’s intent was to give to a local foundation, or even because of claimed misrepresentation. It would be easy for the relatives to find an attorney to take that case, and there is a good chance they would win. Even if the challenge fails, it would be costly litigation. Careful drafting would avoid this result, but it is well known that people leaving such bequests, and their attorneys, often have no communication with the charity about the gift before death.

G. The independent charity is a public charity which can seek donations from other foundations and charities. Some of them may not be willing to donate to or through the lead foundation. While lead foundations may be willing to cooperate in seeking the grants, and have often successfully done so, the process is more complicated, and the need to involve the lead foundation might deter the local leaders from seeking such a grant. If the local leaders are seeking small amounts from local charities, perhaps for a small fund drive, the need to involve the lead foundation may be problematic.

H. The independent foundation can carry out programs and projects more simply than if it has to involve the lead foundation. It can simply receive and disburse funds itself. The lead foundation may not want to participate. A simple example would be building or restoring something. Who would enter into contracts with suppliers and contractors? Some lead foundations would, but others might not, and the decision might vary depending on the project. The independent foundation can enter into contracts, but a component fund's advisory committee members might incur personal liability if they try to do so.

I. One of the reasons for creating a community foundation is to provide leadership to a community. Can leadership be provided as effectively if you are an advisory committee that requests grants from a lead foundation? I believe that seriousness of purpose is less likely from an advisory committee. In my experience, generally, advisory committees do not do much. We have learned that in some communities the advisory committee is one person, and in others the committee sometimes ceases to function, although the lead foundation may work to get them restarted.

J. I believe that there is greater likelihood of continuity of local leadership for your foundation if there is a board of directors with fiduciary responsibilities and significant assets than there is if all you have is an advisory committee which owns no assets. That will not, of course, necessarily be the case.

K. There are potential personal liabilities for members of an advisory committee or other local leaders who are not protected by the corporate status of an independent foundation. However, the lead foundation will likely have insurance that will cover most of such liabilities.

L. The lead foundation will charge the community fund for administration services and for the costs of asset managers, likely in the range of 1 to 2% of assets in total. The independent foundation may be able to save some of these costs.

M. If your community foundation is ever not succeeding as a local independent foundation, the foundation can then choose to transfer ownership and control of assets to a lead foundation to be placed in a community fund there. On the other hand, what happens when assets are transferred to the lead foundation and the community later wants such assets to be transferred back to an independent community foundation? Some lead foundations will do so and have done so, but they are not required to do so and they might not. Changing your mind might only go one way.

16. COULD AN INDEPENDENT COMMUNITY FOUNDATION OBTAIN SERVICES FROM A LEAD FOUNDATION?

An independent CF could choose to purchase services from a lead foundation, and many do, and thus obtain assistance without having to transfer ownership of its assets to the lead foundation. Such an arrangement often results in what is called an "agency fund." (Some lead foundations will accept such an arrangement, but some will not; these practices are evolving.) The amount of assets may be a factor. Cost may be a factor. A CF can also purchase needed services from a CPA, attorney, bank, investment company, or other provider of services, and can do so on an as-needed basis and thus avoid continuous fees. It may not be necessary to hire someone to make

deposits, thank donors, hold assets, keep records, write grant checks and do other tasks you can easily do yourself, with local counsel as needed.

17. WHAT CONTINUING RELATIONSHIP WITH THE J. A. WEDUM FOUNDATION IS EXPECTED?

Once your CF is established, there will be no ongoing legal or contractual relationship between us, only a relationship as friends. We are, as part of our mission, acting as midwife at the birth of your new foundation, but it is your baby. You own the new foundation. You owe us nothing. We do hope to receive a progress report from time to time, perhaps annually, because we enjoy hearing good news and because your information and experiences will help us as we continue to start new community foundations. We will continue to be mentors and provide advice to you as you may desire.

18. WHEN CAN YOU EXPECT THAT MATCHING GIFTS WILL BE PAID TO YOUR FOUNDATION?

Our policies are stated in our policy description, referred to at #3 of this FAQ document. As for the \$2,500 per year matching grants for current programs or projects, we will pay those when we receive appropriate assurances that you have made a commitment for specific current purposes of at least an equal amount. Then when you make your grant you will be able to deliver double the money, which should increase the impact of your gift, which is our intention.

19. WHAT ARE COMMON EXCUSES FOR COMMUNITIES FAILING TO PROCEED TO CREATE A COMMUNITY FOUNDATION AND HOW DO WE RESPOND TO THEM?

A. "This is not a good time." It has been said that "perfect is the enemy of good." Anyone can think of a reason why another time might be better, but it is always a good time to start something that will be a permanent benefit to your community. Perhaps a fund drive might better begin months from now, but start getting ready for that. At a meeting considering whether to build a church sanctuary in Minneapolis over the objections of those who said it was not a good time, a wise man declared "If you had to wait for all the lights to turn green, you would never go to St. Paul." The project was approved and successfully built.

B. "We should not be in competition with other community charities." Our proposal is to make the pie bigger, not to slice the pie into smaller pieces. You should provide more opportunities for people to give, so they are more likely to find a cause they will support. The more organizations and people that are teaching about philanthropy, and the importance of leaving a legacy to give back to their community, the more likely it is that people will think about it and leave that legacy, and all charities will benefit. Furthermore, one of the goals of a CF is to financially support other community charities, and these other charities should welcome this new potential supporter.

C. Some leaders hesitate because they are not sure whose approval they need, or they know there is some opposition. First, you do not need anybody's permission. Those who want a CF can start one, with our help. Secondly, the opposition is often from people who do not want

something to happen that they do not understand or cannot control, or from people who are afraid they might be asked to do some work or give a gift. You should simply ignore that negativity.

D. “Our community is too small.” Brooten and Nicollet, where we have helped to start CF’s, each have a population of 1,000, and they both have very strong starts.

20. WHAT IS OUR CONTACT INFORMATION?

The address of the J. A. Wedum Foundation is 2615 University Avenue SE, Minneapolis MN 55414. Our website is wedumfoundation.org. Our phone number is 612-789-3363. Our President is Jay Portz. Our authorized representative for our community foundation program is Dayton Soby, who is a trustee of our board and the primary author of this FAQ document. He is willing to work with your community leaders and looks forward to your call. His cell number is 763-229-9228. In summer his home number is 218-763-3128.