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Zuckerberg's Choice

Last year Facebook Chairman and CEO Mark Zuckerberg and his wife, Dr. Priscilla Chan, dedicated 99% of their Facebook shares to charity. The estimated value of the commitment was then $45 billion. The couple chose not to follow the example set by Bill and Melinda Gates, in that they did not set up a private foundation to manage their charitable endeavors. Instead, they created a limited liability company, or LLC. Regardless of the LLC's activities, there is no charitable deduction for transfers to it. What's more, the income of an LLC is fully taxable and must be reported on the personal tax returns of the owners.

Why would they take this approach? Why sacrifice the important tax benefits afforded to private foundations?

Because, in this special case, it was not much of a sacrifice at all.

In the first place, the charitable deduction for the transfer would be limited to 20% of adjusted gross income. Unused deductible amounts may be carried forward, but only for five years. The couple's annual income, even if very high, could not possibly use up all of a $45 billion deduction in just five years. Most of this "tax benefit" would be wasted.

Secondly, Facebook does not pay dividends, and it is not likely to pay them in the near future. If there is no income, there is no need for the income tax exemption that a private foundation would get.

Opting for the LLC approach allows the couple to escape some very tough regulatory requirements that apply to private foundations. Chief among these is the requirement to spend 5% of the foundation assets on charitable endeavors every year. Here, that would come to over $2.25 billion annually. The Chan Zuckerberg Initiative likely is not ready to spend so much so soon. Other bullets dodged include:

- the requirement to file Form 990-PF, which discloses to the public all the expenditures and activities of the private foundation;
- the "excess business holdings rule," which would have mandated selling a portion of the Facebook shares;
- the "jeopardy investment rule";
- the "self dealing rules" that limit transactions with founders; and
- the "taxable expenditure rules" prohibiting political and lobbying spending.

What's more, assets placed in the LLC are not permanently set aside for charity. Such a transfer is really a charitable pledge, rather than a charitable gift. The LLC could be dissolved and its assets returned to the owners without tax penalty.

Although using an LLC for philanthropy may be novel, it is not new. Reportedly, Steve Jobs' widow, Laurene Powell Jobs, channels her charitable gifts through an LLC she created, so as to keep the gifts anonymous.

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