

## READER'S GUIDE TO THE FORM 990-PF

The annual Form 990-PF is a public document that provides useful information about a private foundation's financial and charitable activities. The IRS uses it to assess excise taxes owed by the foundation and to monitor certain activities. The underlying tax rules for private foundations are complicated, so it's not surprising that some of the information provided on the Form 990-PF is often misunderstood. We hope this Reader's Guide will demystify the key information contained in the Form 990-PF.

We have organized the information into charts that show some of the information that people most often seek, as well as answers to some of the questions we're asked most frequently. We provide specific references to the location in the tax return where the information can be found.

First, it will help to explain an important organizational structure change. In October 2006, our trustees created a two-entity structure. One entity, the Bill & Melinda Gates Foundation Trust (which we refer to as "the trust"), manages the investment assets. The other, the Bill & Melinda Gates Foundation ("the foundation"), distributes money to grantees. The trust and foundation are separate legal entities, and each is required to file a separate Form 990-PF. Those returns can be found at <http://www.gatesfoundation.org/about/Pages/financials.aspx>. Under this structure, the trust makes grants to the foundation, and the foundation distributes those funds directly to grantees. For more information about the two-entity structure, please refer to <http://www.gatesfoundation.org/about/Pages/gates-foundation-asset-trust.aspx>.

Following are key data points and answers to frequently asked questions for the foundation and the trust.

## Key Data Points from the 2008 990-PF for the Bill &amp; Melinda Gates Foundation

Topic	2008	Form 990-PF Reference	Comments
<b>Grants Paid</b>	\$2.805 billion	Page 1, Part I, line 25 (d); detail listing attached to the return	The foundation distributed just over \$2.8 billion in 2008 from contributions received from the trust.
<b>Total Charitable Distributions</b> (including grants)	\$3.308 billion	Page 7, Part XII, line 4	Total distributions of \$3.308 billion comprised three categories: grants of \$2.805 billion, operating expenses of \$385.8 million, and capital investments of \$117.4 million, primarily in IRIS Holdings, LLC, the separate company that is developing the foundation's new headquarters in downtown Seattle. Of the total distributions, the foundation treated \$1.456 billion as qualifying distributions and \$1.852 billion as distributions of corpus.
<b>Excise Taxes</b>	\$14,932	Page 4, Part VI, line 5	The foundation receives its funding from the trust and therefore does not maintain a separate endowment. Having no endowment results in a relatively low excise tax.
<b>Distribution Ratio</b> (sometimes called the "payout ratio")	4,133.39%	Not calculated on the return	Although the return does not display this ratio for the current year, it can be calculated by dividing total adjusted qualifying distributions of \$3.308 billion by \$80 million in non-charitable use assets (page 7, Part X, line 5). This ratio is very high due to the significant distributions required under the terms of the gift from Warren Buffett.
<b>Compensation of Officers, Directors, and Trustees</b>	\$4.079 million	Page 1, Part I, line 13(a); see detail on Page 6, Part VIII, line 1, column (c)	The schedule provides a listing of 2008 compensation and benefits paid to the foundation's officers. The trustees receive no compensation. The increase in compensation of officers, directors, and trustees from 2007 is primarily due to three additional people included on the 2008 list.
<b>Compensation of Five Highest Paid Employees</b> (other than officers, directors, and trustees)	\$2.538 million	Page 6, Part VIII, line 2, column (c)	The schedule provides a listing of 2008 compensation and benefits paid by person.
<b>Contributions</b>	\$3.316 billion	Page 1, Part I, line 1 (a); see detail of gifts of \$5,000 or greater on Schedule B of the Form 990-PF	Contributions were received from the trust as explained in the introduction to the Reader's Guide. The foundation also received unsolicited contributions from other people; any that were for \$5,000 or more are disclosed on Schedule B.

## FREQUENTLY ASKED QUESTIONS

### Payout

#### 1. How much was the foundation required to distribute in 2008?

The foundation was required to distribute \$6.9 million in 2008 as shown on page 7, Part XI, line 7. The technical IRS term for the minimum payout is "distributable amount." The distributable amount for the foundation is quite small compared to the trust; this is because the foundation retains only a modest amount of money on hand. As explained previously, the endowment assets are maintained by the trust, rather than by the foundation.

The trust, by contrast, was required to pay out \$1.710 billion. It actually paid out \$3.307 billion, all to the foundation. This excess amount of distributions is required by the terms of the gift from Warren Buffett. The foundation in turn distributed \$3.308 billion in grants and other charitable expenses.

#### 2. How is the required payout calculated?

Although the calculation is a bit complicated, the concept is simple. IRS rules require the foundation to pay out 5 percent of its average "non-charitable use assets," which means the investment assets and any other assets that are not used directly in the charitable work of the foundation. The actual calculations involve several steps as summarized on page 7, in Parts X, XI, and XII of the tax return.

### 3. What types of disbursements count toward the foundation's annual payout requirement?

All reasonable operating expenses count toward the payout requirement, provided they further the charitable goals of the foundation. This includes grants as well as the foundation's operating costs. Program-related investments (PRIs) also count toward payout. (PRIs include low interest loans made for charitable purposes and certain types of charitable-purpose equity investments.) Finally, capital costs for charitable use—such as furniture, computer equipment, and the construction of our new campus —also count toward payout.

## Administrative and Other Costs

### 4. How much did the foundation spend in administrative overhead in 2008?

People use the term “administrative overhead” in different ways, and the format of the return is not very clear on this question, so let's start by explaining the cost components. If we take the total 2008 expenses on a book basis—i.e., accrual, not cash—and subtract grant expenses, we're left with \$405.4 million in operating costs (line 24). The operating costs include three major components: (1) direct grant-making expenses to pay salaries and operating costs of the program staff who make and manage grants, (2) “direct charitable expenses” such as technical assistance paid to support the work of our grantees, and (3) administrative costs to operate the foundation, including salaries and benefits for support functions such as finance and human resources, legal services, rent, office supplies, etc. The format of the tax return does not allow a foundation to display these operating costs, so we have provided this information below:

\$195.3 million	direct grant-making expenses
54.1 million	direct charitable expenses (page 6, Part IX-A)
<u>156.0 million</u>	administrative costs to operate the foundation (referred to by some as “administrative overhead”)
\$405.4 million	total operating costs (page 1, line 24, column “a”)

### 5. What were the foundation's administrative overhead expenses in 2008 as a percentage of total expenses?

The answer to this depends on how you define administrative overhead, as discussed in the answer to question 4. If you mean total operating costs as a percentage of total expenses including grants, then it is 10.01 percent (calculated as \$405.4 million divided by \$4.049 billion). The problem with this approach is that it includes costs to make and manage grants as well as costs of activities that directly benefit grantees and are therefore not just administrative overhead costs.

We believe a better definition of “administrative overhead expenses” would exclude direct grant-making costs and direct charitable activities. Under this approach, the percentage for 2008 is 3.85 percent (calculated as \$156 million divided by \$4.049 billion).

Under either method, the foundation's high level of grantmaking, which makes up most of the denominator in the percentage calculation, results in a fairly modest overhead percentage relative to what is normal for most organizations.

## Taxes and Other

### 6. I thought foundations were exempt from taxes. What kind of taxes do you pay?

Under IRS rules, foundations are exempt from income taxes, but they are required to pay a 2 percent excise tax on net investment income. (Foundations can reduce their excise tax rates to 1 percent if they meet certain conditions. See question 7 below.) Net investment income includes rent, interest, dividends, royalties, net realized capital gains, and other similar types of income, minus expenses for managing investments. The income and expenses that figure into this calculation are shown on page 1, column “b” of the Form 990-PF. The foundation's net taxable revenue in 2008 was \$746,585 (page 1, Part I, line 27b), resulting in an excise tax of \$14,932.

### 7. Why do some foundations pay 1 percent in taxes, and others pay 2 percent?

A foundation may reduce its excise tax rate from 2 percent to 1 percent if it disburses a sufficient amount above its required 5 percent minimum distribution. The calculation to determine whether a foundation qualifies for the reduced tax rate is shown on page 3, Part V of the tax return. In 2008, the foundation needed to distribute \$3.42 billion to achieve the lower tax rate (page 3, Part V, line 7). It distributed less than that amount, so it did not qualify for the lower rate.

## Key Data Points from the 2008 990-PF for the Bill & Melinda Gates Foundation Trust

Topic	2008	Form 990-PF Reference	Comments
<b>Grants Paid</b>	\$1.852 billion	Page 1, Part I, line 25 (d)	The trust distributed \$1.852 billion in qualifying distribution grants, plus \$1.455 billion in additional grants that were not applied toward the annual payout, as explained in question 1 below. All grants were made to the foundation.
<b>Total Charitable Distributions</b> (including grants)	\$1.852 billion	Page 8, Part XII, line 4 and Attachment A	Charitable distributions were made up nearly entirely of grants, since the trust incurred only \$1,481 in operating costs in 2008.
<b>Excise Taxes</b>	\$20.9 million	Page 4, Part VI, line 5	The trust's excise taxes are calculated as 1 percent of its net investment income of \$2.090 billion, as shown on Page 1, Part I, line 27b, column (b).
<b>Distribution Ratio</b> (sometimes called the "payout ratio")	5.29 percent	Not calculated on the return	Although the return does not display this ratio for the current year, it can be calculated by dividing total adjusted qualifying distributions of \$1.831 billion (Page 8, Part XII, line 6) by the net value of non-charitable use assets of \$34.623 billion (Page 8, Part X, line 5).
<b>Compensation of Officers, Directors, and Trustees</b>	None	Page 6, Part VIII, line 1, column (c) (see detail at Statement 28)	No compensation was paid in 2008 to the trust's officers and trustees.
<b>Compensation of Five Highest Paid Employees</b> (other than officers, directors, and trustees)	None	Page 6, Part VIII, line 2, column (c)	No compensation was paid because the trust does not have any employees. Administrative matters for the trust are handled by employees of the foundation.
<b>Cumulative Excess Distributions</b>	\$657 million	Page 9, Part XIII, line 9	This is the amount by which the trust exceeded the required minimum distribution for the five-year period from 2004 through 2008. These excess distributions will continue over time, primarily due to the terms of the gift from Warren Buffett.
<b>Contributions by Bill Gates</b>	\$57.24 million	Schedule B, page 1 of 1, of Part I	This contribution is comprised of \$57.24 million in investment management fees paid by Bill Gates on behalf of the trust.
<b>Contributions by Warren Buffett</b>	\$1.799 billion	Schedule B, page 1 of 1, of Part I and Part II	This contribution is comprised of 451,250 Class B Shares of Berkshire Hathaway, Inc. stock.

## Payout and Other

### **1. Did the trust qualify for the 1 percent tax rate in 2008?**

Yes. The trust needed to distribute at least \$1.831 billion to achieve the lower tax rate (page 3, part V, line 7), and it actually disbursed \$1.852 billion in qualifying distributions (page 3, part V, line 8).

### **2. Statement 23 shows that the trust made grants to the foundation totaling \$3.307 billion, but only counted \$1.852 billion of the grants toward its payout. Why is that?**

The answer to this is due in part to some complicated tax rules, and in part to impacts of the gift from Warren Buffett. The trust has a goal each year of making sure it achieves the 1 percent tax rate by distributing sufficient grant funds to the foundation (see question 7 above); however, the terms of the gift from Warren Buffett require the trust to distribute a good deal more than the minimum necessary to achieve the 1 percent tax rate. So the trust makes “qualifying distribution” grants to the foundation at the level necessary to achieve the 1 percent tax rate (in 2008 this amount was \$1.852 billion), and then treats the additional distributions required under the terms of the Buffett gift as a “distribution of corpus.” These distributions are permitted under the IRS regulations for private foundations. For its part, the foundation must meet its own required minimum distribution (i.e., the 5 percent payout) and then must distribute out of corpus at least an amount equal to the “qualifying distributions” received from the trust.

### **3. Why do the trust's total assets of \$29.7 billion, as listed on the tax return, differ from total assets of \$32.1 billion listed in the trust's audited financial statements?**

We arrive at the \$29.7 billion figure by eliminating certain investment-related transactions. This avoids counting those transactions twice, which we think provides a clearer picture of the amount of money that's actually available for the charitable activities. These investment balances are disclosed in the tax return in Statements 13 & 14. A more complete explanation of the elimination entry is provided in footnotes 3 and 4 to the Combined Statements of Financial Position for the Trust and Foundation, found on our web site at <http://www.gatesfoundation.org/annualreport/2008/Pages/combined-statements-financial-position.aspx>