Please note: This is a transcription so there may be slight grammatical errors.

Kara:

Hello, everyone and welcome to today's webinar, Starting and Growing Your Endowment. I would now like to introduce Heather Shanahan, director of Endowments and Foundations at CAPTRUST. Heather?

Heather Shanahan:

Thank you, Kara. Thank you so much for joining us this afternoon and thank you to our panelists as well. We are all super excited to cover all things endowments with you today. Everything from starting an endowment to growing an endowment. I think this is a hot topic. We get a lot of questions and have had an increasing number of questions from our existing clients about how best to navigate some of these issues here. So we're excited to take a deep dive. I will ask each of our panelists to introduce themselves, say a little bit about them who they are and their background. And I'll begin with Christina Ayar, vice chancellor for External Affairs with Oakland Community College. Christina, welcome.

Christina Ayar:

Thank you, Heather. And thank you so much for having me today. As Heather mentioned, I'm Christina Ayar, the vice chancellor for External Affairs at Oakland Community College in Michigan. With that role, I'm also the executive director of the Oakland Community College Foundation and also a limited licensed professional counselor which I think everybody in philanthropy has a little bit of that counseling background in them, so thank you.

Heather Shanahan:

Welcome. Our next panelist is Ed Chaney, counsel to philanthropy in the nonprofit sector and an attorney with Schell Bray.

Ed Chaney:

Thank you, Heather. And also thanks for inviting me and including me on this panel. My name is Ed and my clients are almost all nonprofits and they come in all shapes and sizes, but I do a lot of work with both institutional clients that are creating and maintaining and managing endowments, whether that's on the private foundation or public entity side and also working with donors in their gift planning around whether to create endowments, et cetera, things like that.

Heather Shanahan:

Excellent. Welcome. Next up, Dan Simon, principal and financial advisor with CAPTRUST.

Dan Simon:

Thank you, Heather. It's also great to be here this afternoon. Dan Simon. I'm a principal with CAPTRUST out of our Chicago office. I've been working with endowments and foundations, helping them structure investment programs for over 25 years. I'm also fortunate enough to have worked with the Saint Louis Zoo where Lori Sullivan who will shortly introduce herself is at and worked with the Saint Louis Zoo as they've created the endowment and really watched it grow significantly as Lori's just done such a fantastic fundraising over the last several years. So look forward to participating in the panel.

Heather Shanahan:

Excellent, thank you. And finally, Lori, that was a nice tee up to tell us a little bit about you. If you share a little bit about your background.

Lori Sullivan:

Yeah. Thanks. I appreciate it. Yeah, Lori Sullivan. I'm the director of Planned Gifts for the Saint Louis Zoo. I've been in this position for 10 years. Prior to that, I was in higher ed, nature conservancy conservation organization. So I've always raised Planned Gifts and endowment gifts, but now I'm in the chair to actually run the program and do all the extra things that tee all that up. So it's been a great ride like Dan said. The zoo is on a great trajectory, thanks in part to CAPTRUST expertise and guidance. We're kind of a team. Dan and his colleagues manage those investments and make sure that they grow and my team and I, we do our best to get new gifts in. So between the two, it's been a nice success story.

Heather Shanahan:

Wonderful. Well, welcome to everyone. We're going to cover a lot of topics today, but certainly we encourage all participants. If you've got questions, please drop those into the questions section and if we don't cover what you're interested in, then we'll hopefully have some time at the end to address some questions and concerns. So let's go ahead and start with the foundation pieces and talk about endowments 101. What are the different types of endowments? How do they work? What are some things to be mindful of from an administrative standpoint? Pros and cons, how we get started. So I'll call on Ed to kick us off on that conversation on our next slide.

Ed Chaney:

Those are awfully big questions, but we'll try to tackle them one at a time. I think the most important thing to do when we start out is to get on the same page about what is and what is not an endowment, because that word is used pretty frequently, but it is also a legal term of art. And so it's important to understand when you're using that word, whether you're trying to indicate the legal term or not.

I've had lots of conversations with nonprofits who say they want to create an endowment and they sit down and say, "Well, we've got this reserve fund and we want to have it invested." I'm like, "That's not the same thing as an endowment. An endowment is something that is meant to create sustaining support, enduring support over time, whereas a reserve or a rainy day fund is exactly that."

Funds that need to tap into in case of a crisis or emergency or something special, things like that. But even if you were creating a fund that is meant to be enduring in nature, that doesn't necessarily make it a legal endowment. A legal endowment is a restricted fund that only a donor can create that prohibits an organization from spending down the principle of a gift. It can only spend the income of a gift. So the gift gets invested wisely, managed by Dan and his team, and then the board determines on an annual basis how much they want to pull down to spend based on a prudent analysis. And we'll get into a little bit more details about all of that later in the session, but I often hear nonprofits sort of refer to an enduring fund as a reserve fund. I mean, excuse me, as an endowment or a fund that the board has kind of set aside as an endowment.

And it's not the same thing. And the reason why that's important is because if you're a board and you set aside funds and you say, "We're going to treat this like an endowment." Again, as I said before, a donor is the only one who can create the legally binding restriction that prohibits you from tapping into that fund. So if you are a board and you set aside that there's nothing that prohibits a future board from releasing that restriction and pulling those funds down.

Also, we'll talk about this a little bit more when we get to [inaudible 00:06:57]. If you are out and you're talking to donors and you say, "Please contribute to my endowment," and you've created a quasi endowment and that donor gives you a million dollars to put in your endowment, that donor is not thinking a quasi endowment. That donor is thinking a true endowment. And so now you have sort of money that's side by side. You've got a true endowment and a quasi endowment even though you're using the same words.

So it's important for you as organizations to really understand what it is you're creating so that you can communicate that appropriately to your advisors and also to your donors as well. The type of endowment that a board creates is a quasi endowment, and it's typically managed just like an endowment. It's invested, pulled down in a spending policy on an annual basis, and it's even reported on your both 990 and your financial statements as quasi endowments, but not as donor restricted funds. So oftentimes the management of a true endowment in a quasi endowment looks practically the same.

Heather Shanahan:

What would you share about best practices from a documentation standpoint? Because I know we bump into that with clients and we have certainly experience where somebody set this up 20 years ago, we're managing it one way. We're not sure that's actually right. How important is the documentation on all of this?

Ed Chaney:

The documentation is very, very important because an endowment is a legal term and it bears a restriction that can only be modified according to law. So you want to have a gift agreement that is clear, and that also gives you some flexibility. If the purpose is very narrow, you want to have some flexibility. If things change a little bit, if the sloth exhibit at the zoo no longer exists, then you want to be able to deploy those assets to support a similar without having to go to court to get that endowment agreement modified.

If you are charging a fee or contemplating charging a fee or may ever charge a fee, you'll want to put in there that an sort of administrative fee may be assessed from time to time is determined by the board. Similarly, if there's a fundraising assessment or something like that, you typically see those in larger institutions like colleges and universities and healthcare systems who want to charge a fee so that they can do the overhead of managing everything, but also have a fundraising fee that goes to support the development teams as well. All of that ideally should be in a gift agreement or it should cross-reference policies that you have the right to change from time to time.

Heather Shanahan:

Is there a tipping point? Do we have organizations that don't have an endowment and they decided, "Okay, it's time to start an endowment"? What are the things that an organization should be mindful of when they get to that point? Why to start or why not to start an endowment?

Ed Chaney:

I think you'd typically get into a conversation with an organization when it has some cash that it just doesn't need to deploy right now. And so it's pondering whether it should create an endowment. And really the question that you need to ask is what are your long-term plans? Are you trying to create a fund that's going to sustain? If so, what do you want that to look like? Do you want it to be permanently restricted by a donor? Do you want the board to have flexibility to spend if it needs to?

If you've got six months of reserve and you're thinking about maybe creating an endowment with three months of that, that's probably not enough to do that. So you might want to sort of think about, okay, we want three to six months in reserve, ideally six, what is the window past that at which we can a point where we feel comfortable enough.

And it's large enough that it makes sense to create a standalone fund that you can pull down 5% a year. $100,000 won't do all that much on an annual basis.

Heather Shanahan:

So that's taking it from the quasi board restricted endowment. What about organization says, "Okay, we want to solicit donors to start an endowment, to build an endowment with us." Then what things do organizations need to be mindful of?

Ed Chaney:

So donors think an endowment is one thing, but an endowment can be a hundred things depending on what the donor said when they gave you the gift. When economic crises hit, you hear colleges and universities sweat over whether they should tap into their endowment. Well, the reality is they generally can't because you've got a scholarship fund here, a chair fund here, and all those things are designated for specific things, but altogether they create an endowment.

Now, why I'm saying this is that when you decide that you want to create an endowment, you need to think about whether you want to set the parameters for that endowment or you are willing to accept endowments targeted for specific purposes or tailored or whatnot. And if it's the latter, then you need to have some good gift acceptance policies and other things in place so that you don't end up with some bad gifts down the road that you really have no idea what to do with or they're problematic or too cumbersome to administer.

Heather Shanahan:

Unintended consequences of generous donors. So that's probably a good segue to our next question to get some feedback from Lori. Christina, how do you engage potential donors and how is that conversation when you're talking about an endowment with a donor different? How to ask different than a major gift? Lori, you want to kick us off?

Lori Sullivan:

Yeah, I think it is a major gift, but you're right in that it has a whole different set of expectations. And to Ed's point some guardrails and dreams really. My favorite phrase to make sure donors really let soak in is forever is a long time. And so kind of piggybacking on what Ed had shared, you have to have a clause in all these agreements to say, if for some unforeseen reason, the funds cannot be allocated as the donor has originally set forth, please trust the institution's leadership at any given time to make the next closest allocation for the harvest.

No one can see for forever. And you try to get the donor to understand, if you want these funds to do the best work for our mission, you're going to have to trust us to redirect this if for some reason plan A change has evolved. There are some organizations in nonprofit space that specifically don't set up endowments because they said, "Our mission is to cure whatever disease. We hope we don't need it forever." It's a funny space. It really is.

Heather Shanahan:

Thank you. Christina, talk a little bit about-

Christina Ayar:

I will add that a lot of times when we're having conversations with donors or potential donors, we're not financial advisors and we don't claim to be, and we're not attorneys and we don't claim to be. However, I think it's our responsibility in our profession to be able to give some really honest and constructive-

Christina:

Responsibility in our profession to be able to give some really honest and constructive criticism when the donor has specific intentions for a gift that maybe isn't needed or doesn't make a lot of sense for the organization. So a lot of times it's just redirecting their giving intentions to a fund that makes the most sense and is the best fit for both their wishes and the organization's wishes. And there's also some real, I guess, benefit of having a conversation of making an outright gift that you can see and you can experience. And if it's a scholarship, for example, in higher education, a lot of times the donors will say to me, "I understand what an endowment is and I love my gift to last in perpetuity, but I also want to make gifts today and I want to be my scholarship recipients today." And so there's a good opportunity to educate the donors on the different types of funds that they can establish both endowment and just unrestricted annual fund that they can create with that organization. So it's just about having real honest and transparent conversations and putting all the options on the table and really selecting one with the donor that is the best fit for them.

Heather Shanahan:

That makes sense. Let's talk about what happens when your gift acceptance policy is orally drafted. Then you set yourself up for, you can have the conversation, but you've got documents that may not match up what you're saying. Ed, do you have any thoughts on that? What are the dangers there?

Ed Chaney:

Oh, do I ever, so the benefit of a gift acceptance policy is the ability to say no. It is so difficult to say no to a donor when they have this passion and they want to do this thing that you know is just not going to be work out. Well, it's hard for you to say that, but it's easy to say, "We've got this gift acceptance policy and this is outside of the policy and we're going to have to figure out another way to do what you want to do."

So a good gift acceptance policy will enable you to do that when there are going to be tax issues that could arise for your own purposes or for the donor's purposes when it's going to be costly in nature for y'all to administer, when the reputation of a donor may change and you've got a naming policy, it's part of your gift acceptance policy, things like that, you'll want to have a policy that's robust enough to get you out when you need to get out, and let you say no when you need to say no.

I was going to say, sometimes development officers, I love them. Sometimes they want to pull in the money, and if there aren't guardrails around them, sometimes you'll end up with, they'll work with a donor until they can get that money in the door. So it's not only, I guess what I'm saying is that it's not just a ability to say no to the donors, it also helps offset some of the incentive that fundraisers naturally feel that they need to pull in as much money as possible.

Heather Shanahan:

Christina and Lori, do you have any examples of gifts that you've been offered that you had to turn down along the way or things that you've accepted that were more complicated to unravel?

Christina:

I can take this one. I've been in higher education my entire career and in a lot of different capacities, and I think Ed's point, I think at times if you're a development officer and you're managing a portfolio and you have specific goals that are set for you, you feel a sense of urgency that you need to secure a gift and you need to just do whatever it takes to sign the MOA. But I also think that there's, again, going back to the conversations of being honest and transparent with donors, we've had donors that have put real specific requirements, for example, in some of their scholarship guidelines, and we simply can't award based on certain things, race, gender, ethnicity, religion, so on as one example. And so we can redirect some giving. Again, we can have that healthy conversation to say, "Here's what I think we could do, or why don't we say preference given to a resident of the city or township."

So there are creative ways to again, redirect some of their intentions. But certainly there has to also be that conversation where you can say, "I'm sorry, but we just can't accept this gift." So it's challenging, especially again, if you're working for an organization that's really all about bringing in certain numbers and hitting your goals. But I think in our profession, we are not physicians, we're not attorneys, so we're not signing any kind of hippocratic oath, but we do honor donor intent and we also honor the organization's missions that we work for. So we have to be able to align them together. And if it's not matching, then we have to be able to say, "I'm so sorry, but we just can't go this direction anymore."

Lori:

Yeah, I find that bravery by being donor focused because if you know, can't fulfill that donor's wishes, it doesn't work for them either. So you just like Christina said, you just bring them into the picture, paint it more fully so they can see where they don't fit, and then try to find a place that they do. That's really being donor focused and that's what we're all about.

Heather Shanahan:

Do you have internal controls set up both of you, so that you receive a gift from an established endowment, or maybe it was set up 20 years ago. What do you do to make sure that you're executing on that donor intent? How do you make sure that on an ongoing basis you're honoring that donor intent?

Christina:

So in our organizations in higher education, most of the time the foundation either seek guidance from general counsel at the organization or seek external general counsel support. So I always turn to others to review the documentation even if it were a legacy gift that was left 20 years ago that we didn't even have on file and weren't aware of. So again, we check everything and make sure that we're circulating it to external people both at the organization and outside. And if there is a need to redirect the gift or make changes to an outdated document, especially if there's no beneficiary listed that we can connect with, we just take that route and document everything that we need to on our end to protect us from an audit as well.

Heather Shanahan:

Makes sense. Let's talk about some structural issues then Dan and Ed, when you take a look at this, should there be a separate entity to house the endowment? Let's talk about UPMIFA and some of the standards that we're held accountable to in the nonprofit space.

Ed Chaney:

Yeah, that's actually, we'll start with UPMIFA and then we can go to that question because there's a relevant tie in. So UPMIMFA is the Uniform Prudent Management of Institutional Funds Act. That is the law that exists in every state but Pennsylvania, and that's because Pennsylvania has its own version of it that governs how you invest and spend endowment funds and also how you can release or modify restrictions that a donor has put on a gift. Now, when it comes to standards for investing and standards for spending, just think of the word prudent, because that is the word that applies to both of these acts. When you're investing your standard is the prudent investor standard. And if you want to delegate the investing to Dan, making a prudent decision to do so and monitoring as you would anybody else, the standards for spending is, and I should back up and say, and UPMIFA also provides some factors that you kind of look at in terms of all of those things in deciding what's prudent and what's not, like how much you're going to put in Bitcoin, what is the nature of the economy? What are the needs of the institution? What's happening with inflation and deflation? Things like that.

On the spending side, you're looking at similar factors, but the prudential consideration is how much can you spend while also honoring the intent that this be a perpetual fund and maintaining the spending power of that original gift over time. So you're going to take a look at an inflation adjusted principal amount to sort of protect over time. So is that 4%, is it 3.5%, is it 5%? And there are ways that you can decide to make a special distribution sometimes if in extraordinary times, but you have to sort of go through the same analysis, things like that.

And then at UPMIFA also provides, okay, so you've got an endowment and it's designated for the sloths. We no longer have the sloths, but we want to give it to the polar bears. What do you do? Well, if your agreement doesn't say anything that you can make the change, you've got to go to court and ask a judge. In most states, some states may have sort of different processes, but in most states it's either the court or the attorney general that has oversight over a change of a gift. And that includes both its purpose and also the endowment restriction. So if you wanted to release the endowment restriction for whatever reason, that would also have to be done by court. And UPMIFA contains the process under which you have to follow to make that happen.

Heather Shanahan:

I'm smiling at your slot and polar bear analogy, and Lori's looking very serious, like yes, "That's a legitimate analogy right there for the zoo." How do organizations familiarize themselves with a UPMIFA laws for their state?

Ed Chaney:

There isn't, thankfully, there is not a whole lot of variance if you're in the space of charitable solicitation. It's maddening how different the charitable solicitation registrations are from state to state. Generally speaking, UPMIFA is pretty consistent from state to state. There are only a few places where it can vary. Some states might stick in an extra criteria to look at. Some states will cap what is a prudential spending rate at 7% or something like that. So if you spend above 7%, that's going to be presumed to be imprudent. And so the best way to do that is just check with your counsel, check with your accountants who might have knowledge, or if you're a crafty, go search UPMIFA for Pennsylvania or actually not Pennsylvania for Illinois.

Heather Shanahan:

Good deal. Dan, you work with a lot of nonprofit boards. What types of conversations do you have around UPMIFA and best practices and guidelines for boards to make sure that they're staying compliant with law?

Dan Simon:

Well, first of all, UPMIFA is in basically every investment policy statement outside of Pennsylvania. So that is, and the language of UPMIFA is pretty consistent across states if there is some state specific language that will go in the investment policy statement. But the important things in terms of UPMIFA and just general prudence are having a diversified portfolio by asset class, and strategy, and manager and then on spending. That is something that's very specific to endowments, even relative to other types of nonprofits. And just because there is some more spending flexibility with an endowment. Endowment gets to choose whether that's spending rate is 3.5% or 4%, whereas, a foundation it's 5%, there's no flexibility there. And so crafting an overall investment strategy aligned with that spending level. And so we work with our clients, all clients, we do an asset allocation review. We have expected return assumptions across different asset classes to make sure that the long-term expected rate of return will exceed what the organization's spending rate plus inflation is to make sure that there's long-term perpetual growth of capital.

Heather Shanahan:

Well, let's talk about growth again, and going back to, excuse me to Lori and Christina. What trends are you seeing with donors now, there was certainly a shift in how donors engaged during the pandemic and post pandemic, but now we're kind of getting farther away from that. What are you seeing in your conversations?

Christina:

I can start. In higher education, I think donors are recognizing more so as a result of the pandemic that students really do need some additional supports above and beyond just tuition and fees, which is more of the traditional forms of giving it in higher education, setting up a scholarship fund for example. So they're really recognizing the need for what we call wraparound services is kind of the phrase of choice. And what does that mean? That means technology needs, we have a Open Community College of Student Success Fund where if a student experiences an unfortunate circumstance in their life that prevents them from having access to a laptop and to be able to actually participate in their coursework, then we do have a fund in place that can provide that emergency needs for technology. But also other things that happen. You get a flat tire on your way to school and you didn't consider that.

And so if you're living paycheck to paycheck, as most of our students do, 75% of our students are part-time and they're working full-time. So an unexpected emergency really throws them off, and we're here to support the whole student, not just get in and enroll. Well, how do we keep them? How do we retain them? And how do we eventually help them to complete their degree? So I think donors are starting to recognize more so than not that we need things beyond tuition and scholarship support. So we've been establishing these more, I would say, unrestricted funds that we can use for other needs besides those traditional means.

Heather Shanahan:

That's excellent. I've got three kids in college. I'm very aware of the fact that expenses extend far beyond just-

Kara:

... which I'm very aware of the fact that expenses extend far beyond just tuition. If that was all it was, we'd be okay.

Christina:

That's right.

Heather Shanahan:

That's great that you're able to pivot. Laurie, how about you? What are you seeing? How have things changed or have things changed?

Lori Sullivan:

Well, I think as awful as it was, the pandemic was a wake up moment for people maybe of a certain age. That mortality is just that. And I think it's a truism in our space that the older one becomes, the more legacy becomes a consideration. Once you've got your basic needs covered, your kids are in college, your house is paid for, you've gone on your vacations, you've got your yacht, whatever it was. What am I going to do with all this stuff?

I think those conversations have become richer in the last three or four years, and so we've seen an uptick in our legacy society as a result. We've had more individual named endowed funds this year than I've ever seen in the 10 years I've been here. It is just a more natural topic now. So once the door is open and we try to coach our major gifts team, our allies, to have those conversations, it's just one more avenue for somebody to support the mission in, you said words, an enduring way. And the concept of forever becomes all the more magical when you realize I might not have that much time.

Heather Shanahan:

Right. There isn't really forever. Yeah, and it is, I mean, this is the more potentially emotional conversation with the donor, not in terms of we're going to sit and cry together, maybe. But how do you frame that? How does that conversation go?

Lori Sullivan:

I take a lot of lessons from Professor Russell James, who's down in Lubbock at University of Texas. He does a lot of research in this and there's magic in the word remember. So on my brochure, I don't say, "Leave a bequest." I say, "Remember the St. Louis Zoo." And then our promise back to them is that they, the donors, will be remembered forever. So on the softer emotional side, to your point, Heather, it's a little different conversation frame.

Heather Shanahan:

Thank you. Christina, how about you?

Christina:

I like that, Laurie. I might take that as well. That that's fantastic.

Lori Sullivan:

Thank you. It works.

Christina:

We share best practices in our field, so there's no competitive nature here. But to Laurie's point, I think again, it goes back to having just those real, honest and transparent conversations with donors. And a lot of times too, I think fundamentally the people that are giving to our organizations, they really mean well, and they want to do more. They just need some direction on how to do that. So it is emotional. And so, Heather, we do have times where we are having conversations with donors and you're bringing out the tissue, and that's kind of the nature of the beast. And so it takes a special person, I think, to work in this field to really cater to the donor's needs to listen to what they're saying and maybe to what they're not saying so that you can meet their needs.

But to kind of go back to the earlier question too, something I thought of is that flat is the new up. That's also a phrase that we use in this industry. So we're seeing that the growth in our endowments, it may not be spiking at exponential numbers, but it is flat. And I think that's success, especially in today's day and age. There are donors that we work with that have some uncertainty, whether it's just because of the state of the economy or the upcoming elections. And so we recognize that if we're meeting giving where it's been in past years pre-pandemic, then that's probably okay, and that's probably a good thing. We are noticing fewer donors, but larger gifts from those donors. So things are sticking, and I think that means that we're doing our work with our major donors and kind of transitioning them to thinking about their future giving and their planned gifts.

Heather Shanahan:

I'm curious through these conversations, both of you, I guess I'm reading between the lines that you're having conversations with older donors, but is there a space to talk to younger donors or to address diverse donors? When you're talking about endowments, what does that look like?

Lori Sullivan:

Well, you're never too young to have a will or a legacy plan. And I think that's where companies like Free Will and Giving Docs have kind of come into the space. Even if you don't have much, you want to put something in place. So I think, yeah, we work at all levels, but I think the majority of my work anyway is with people who are in that sort of sweet spot of in their late 60s, 70s, it is within sight. If they haven't already done something, that's a good time to bring it up. And another powerful motivator to piggyback on what we were talking about before is if they don't want to be looking like they're self-aggrandizing in any way, you do something like this in memory or in honor of a loved one, very powerful, very powerful motivator to memorialize someone forever.

Christina:

Organizations I've worked for, we have financial planning workshops, and we do see that there are people in the younger generations that are starting to attend them, but I think in higher education, we do a lot of financial literacy with our students. So that's not just about how to save and how to reduce expenses while you're in college for our scholarship recipients, how to plan for your future, giving, how to start your own scholarship if you were a scholarship recipient, thanking and meeting your donors in person. So kind of introducing the cycle of giving in hopes that one day when they have the financial resources that they would consider our organization in the future. So I don't think it's ever too early to start those conversations, but certainly I think some overarching financial literacy or financial planning workshops with a really reputable financial advisor or attorney in the community would be a great way to gather folks and to ask them some really great questions.

Heather Shanahan:

So speaking of economic turbulence and the things that impact us, let's talk about, Dan, you mentioned spending policies. If we can go to that slide and kind of take a dive there. Should organizations adjust spending policies in our current environment? Do you see that? What are some of the guidelines for a well-written investment policy statement and spending policies? Dan, do you want to take that?

Dan Simon:

Yeah, sure. There's a spending policy slide. I think. I believe it's the next one. If we could go one forward and then [inaudible 00:37:02] we'll talk about investment policies. But if you look at spending policies, I think as it relates to endowments, there's not just one spending policy for all organizations and they vary by organization. And so there are different ways to create a spending policy the most widely utilized. At CAPTRUST, we do a survey each year, and you can see about half of our survey respondents use a moving average. And so it can be a 12 quarter moving average. It can be a longer moving average, but it's a way to avoid huge shifts in spending from year to year and just create some more predictability for an organization.

There's also what's called a hybrid methodology. Some of the larger university endowments use this where there's an inflation component. So it's last year's spending plus inflation, which was kind of tough when we had a 9% inflation year and the markets were choppy. But there's that methodology and you combine that and you can combine that with a moving average.

So there are different ways. There's also just a simple percentage as well. You could say 4% of the last year's market value. So different spending methodologies.

I think one interesting data point, NACUBO puts out an annual survey. We don't have the 2023 survey yet, but their 2022 survey, spending across organizations was right around 4.2%, just as kind of a frame of reference. So if you think about expected return inflation, long-term of 2 to 3%, spending at 4%, that would require an overall expected return over 7%, which is actually this is, it's getting a little easier for endowments to meet that expected return just with the rise in interest rates. Just recently, the yield on the Bloomberg aggregate bond index, kind of like the S&P 500 for the bond world, it's 5.3%. We haven't seen the yield that high in some time. And so the fixed income component was really a big drag on expected returns, and now we're not seeing that drag going forward. So it should enable a lot of endowments to potentially increase their spending policy when they're looking at some of those asset allocation models that financial advisors such as myself put together.

Heather Shanahan:

And this slide is from our 2022 survey of endowments and foundations that we do on an annual basis. And so you see, and even though there's been conversations about inflation adjusted changes or making some changes that the vast majority of organizations didn't react to that and make changes, so that was kind of an interesting data point as well. Ed, anything to add here in terms of conversations you're having with clients about spending policy?

Ed Chaney:

Not really. I mean, I think Dan captured that beautifully. There's a wide variety of ways to calculate a spending policy. I care more about the process. Really, are you taking time to think about things? And the more you are, the better position you are from a legal perspective.

Heather Shanahan:

Yeah. That makes sense. So speaking of processes, let's back up to that other slide then and talk about investment policy statements.

Dan Simon:

Sure. So these are what we believe are our best practices of what we call a well-written IPS. And I'm just going to focus on a couple of the more significant ones.

Upfront, it's always very important so everybody knows what their specific responsibilities are, whether it be the board, the finance committee, investment committee, or the consultants. So that's very good to just put in writing right at the front.

But also importantly is, and this goes right into spending policy, is liquidity needs and incoming cashflow. And what we see is a lot of endowments, liquidity is very manageable. If you think about on average a 4.2% average spend, what that means is that you have about 96% of the portfolio that's not called for the next year. And so that allows a lot, a much more longer term investment horizon and the ability to incorporate longer dated illiquid assets like private equity, private real estate, which we do see in a lot of endowment portfolios.

Just some of the other key specifics, this is an exercise that we like to do is develop a risk tolerance survey for our clients. And essentially what this is making sure that the key decision makers are on board with what the overall long-term allocation should be. I was getting a little noise in the background there, but hopefully it's not too disruptive for anybody else.

Heather Shanahan:

No, it's good.

Dan Simon:

So that risk tolerance survey we think is important. And then just capturing everything, all this information within the investment policy. There's obviously a lot of time that we'll go into developing the investment strategy in terms of a MIFA and just best practice, making sure that everything is well diversified, but capturing that all in investment policy statement and then reviewing it on an ongoing basis. It's not just a document that organizations should put together, put it in a drawer. It's something that should be revisited each year. And as endowments go, and I'll just use the St. Louis Zoo as a great example, this is a document that evolves over time. When the St. Louis Zoo decided to create an endowment, the overall portfolio structure and sophistication was different when it was starting off than where it is right now. It is at a much more significant size. And so it is something that the investment policy statement will evolve over time as an endowment grows.

Heather Shanahan:

Good point. So best practice from either you, Dan, or Ed, how often should an organization [inaudible 00:43:43]? We worked on an RFP earlier this year where the investment policy statement was from 1992, and I'm guessing that wasn't best practice. So how often do you suggest that this gets reviewed?

Dan Simon:

I'll let Ed address that from a legal perspective, and then I can comment on what we do with our clients.

Heather Shanahan:

Perfect.

Ed Chaney:

Yeah. So from a legal perspective, again, it's more about process and prudence. You should definitely not let one go from 1992 for sure. I typically ask folks to take a look at all of their governing documents every three to five years, and that would likely include the investment policy. But also, the investment policy document is one that is a collaborative with the investment managers. So I think that is somewhat dependent on the relationship that the organization has with their investment managers.

Heather Shanahan:

And on that note, then, Dan, what do you do with your clients?

Dan Simon:

Yeah, so we have a governance calendar that we work with our clients on. And there's the review of the investment policy statement, we recommend once a year, not more frequently or generally less frequently. And even if we-

Dan Simon:

... not more frequently or generally less frequently. And even if we review, it doesn't mean that there are going to be changes to the investment policy statement. It just means that this is a document, we're taking active action to review it and see if there are any changes that are warranted. And we do think that is a good practice.

And then typically what we'll see is less frequent is an asset allocation review. That's probably every two to three years. We don't believe an asset allocation review needs to be done each year in conjunction with the review, the investment policy statement. But asset allocation is a big part of the document. So, that's something that's generally done probably every two to three years.

Heather Shanahan:

Great. So, let's switch back to donor conversations with Lori and Christina. So, we don't always know what donors are doing. Certainly as somebody that's given to your organization on an annual basis may not be the same person who leaves you a gift by bequest and vice versa. How do you handle that? How do you try to stay out ahead of that? How do you steward it? This is lots of questions. [inaudible 00:46:12] time. But how do you steward those relationships when you do know that these gifts are coming?

Christina:

[inaudible 00:46:19] you touched on something, Heather, the fact that you may be having all these conversations simultaneously with a donor at any given time [inaudible 00:46:25]-

Heather Shanahan:

I've had a little hard time hearing you. Do you want to move up a little tiny bit and make sure we can hear you?

Christina:

Oh, is that better?

Heather Shanahan:

Yes. Thank you.

Christina:

I was sharing that at times, you may be having these conversations simultaneously with a donor. They may start by saying, "I'm only going to give you this one time gift to award this one scholarship.", for example. But then you start the conversation about legacy giving. You talk about its impact, you talk about making it something that's very honorable and memorable for them and their future and for their family, for example. So I think it's kind of all woven into one sometimes, but you most certainly don't want to push it. But you do share the importance, you share your current staff, and where you're at with your endowment portfolio. You talk about what the potential is and what your spending policy is.

And so you can really, again, going back to educating your donors or perspective donors on where your organization is at, what your mission is, where you see yourselves in the next 5, 10, 15, 20 years, and how their gifts can play a significant role. And somewhat selfishly, from a PR marketing perspective, it's great for them to lead by example. So sharing that information with the organization upfront, it's just got more perks, even if the donor chooses to remain anonymous, which is fine. But again, it's leading by example. It's being able to share a story with the community to potentially encourage others to do the same thing.

Heather Shanahan:

That's great. Lori, how about you?

Lori:

Well, to add a parallel to what Christina just said, when you're in these conversations and people hesitant, they want to stay private, blah, blah, blah, you say, "Well, even if you don't want us to share your story with the rest of the world quite yet, the reason we would like to know the details of your legacy plan is to make sure that we can fulfill your wishes. Because after it's too late to ask you, it's too late to ask you." So let's, again, if we haven't said, "I want to do a scholarship for a zoo camper from X, Y, Z neighborhood.", and we're like, "You want us to be able to award this, right?" Have those conversations. So just assuring them that you want to make sure their dream comes true, we need to have that conversation, if the reticent is one reason.

But the other response I would have to Heather's inquiry is, we're not going to talk to a lot of the legacy donors. They're going to be very private. We're not going to find out anything until they're gone and we hear from an estate planning attorney. And that was the hardest thing for me as a major gift officer of 20 years coming into this space 10 years ago. What do you mean they don't want to meet with me? I'm fun. I've had wonderful relationships, blah, blah all these years. Nope, arms length. So, that's where marketing is your best friend.

And like Christine said, you get a couple of really good juicy stories, you market the heck out of them. And that does either overtly or quietly inspire others. And a lot of the job is really just after the fact, making sure those wishes get fulfilled when you didn't have the benefit of a conversation, or the person in the chair before you had the benefit of the conversation. So, it is just drip marketing and showcasing those stories and inspiring others. And assuring them that this mission will continue well after all of us are gone. And don't you want to be a part of that?

Heather Shanahan:

Thank you.

Ed Chaney:

I do have somewhat of a good war story here that's kind of a cautionary tale. Because as you are having, to the extent that you can have conversations with donors about their legacy planning, those conversations need to be documented appropriately. Just a couple of years ago, one of my clients received a $25 million bequest, which they were expecting, because the donor signed a fund agreement back in the 90s. Well, the problem was, the will or the trust instrument that transmitted the gift over to my client had completely different language than what the client had expected. And what had happened was, they had all these conversations over time. And we think probably what happened was that just he never changed his will to match. And we ended up having to let the judge sort it out. And it got worked out, but it was a big deal. A $25 million gift is something that you don't want to get confusion over.

Heather Shanahan:

Yeah, for sure. I'm going to shift gears for just a second for the sake of time. We've got some questions that have come in, and so I'm going to make sure we get to those, and then we'll hop back and wrap up. And this is probably a question for Ed. If you have multiple donors into an endowment, do they each set up their own restrictions on the use of funds? Or is each donation held to the same terms that the overall endowment has in the bylaws?

Ed Chaney:

That is a very good question. Okay, I'm going to make sure I'm not on mute. That depends on the work that you do upfront. If you draft a sort of endowment agreement with a donor and you have language in there that says, "This is for this purpose and all other gifts made to this fund will be subject to the same gift instrument.", all of that is going to be wrapped up together. But if you don't do that advanced work and you've got donors sending you money for an endowment and some of them say for X, Y, or Z, then you do have multiple endowments, mini endowments instead of one endowment for the same purpose.

Heather Shanahan:

Yep. Next question. Can funds you collect as part of a fundraising campaign be put into a quasi endowment?

Ed Chaney:

Yes. So when you create a quasi endowment, it's similar to what I just said. You have the board have a resolution, and you create a fund. And say, "This is our quasi endowment and these are our expectations." And then you permit the management to make contributions from fundraising to that quasi endowment from time to time. Or the board sort of makes an allocation at the end of the year.

Heather Shanahan:

Okay. Next question actually kind ties back to a question I'm not sure we fully answered. And that is, does a quasi endowment need to submit a 990? And I think this also circles back to the question of, do we set up a separate entity or an endowment? So, maybe we can answer both of those with this question.

Ed Chaney:

That's also a good question. So, most endowments are not separate legal entities, they are just...

Heather Shanahan:

We've lost your sound, Ed.

Ed Chaney:

Okay.

Heather Shanahan:

[inaudible 00:53:38].

Ed Chaney:

Let me back up. It was pure poetry that you all missed. So an endowment in and of itself is not a separate legal entity. It's a fund that has some legal restrictions on it, but it belongs to the legal entity. So the only way an endowment would be a separate legal entity if it was created as a separate trust, or the organization decided to create a separate sort of fundraising or endowment management entity on the side. So, the answer's, no, you would not have to have a separate 990, unless you created a separate organization.

And when it comes to that, it's sort of a form follows function thing there. I've created as many as I've unwound. Good intention, it kind of makes sense, but then 10 years later, why do we have this complex structure? I think there are kind of three reasons to create a separate endowment or a separate entity, one of which if you're a public body, like a public university or some public museum or something like that. It's often good to have a private fundraising arm that manages the funds for public records requests, sort of loan, sort of issues around what's what information about donors is in the public sphere.

The other two reasons are for private organizations, which is a liability shield between your assets and your operations. Creating them separately, if you've got a high risk... doing a function where there could be a major lawsuit, you want that lawsuit sequestered over here. And not to tap into any unrestricted funds that you might be raised over here.

And the third would be if your organization just wants a separate governance structure for this type of thing. And it wants to put a different kind of board member on that board, somebody who's sort of more financial oriented or fundraising oriented or whatever, as opposed to somebody who's got the operational expertise or the organizational expertise. I think you just have to sort of sort through the pros and cons through all of that and come to a good decision about whether to spin it off.

Heather Shanahan:

Yep. Thank you. Lori, you had a situation at the zoo where you actually went from a more complex model to a less complex model too, so it could kind of go both ways. So, simple isn't bad either.

Lori:

We started out with the endowment trust. And then melding some 501c3 together that we had running around, we decided it was time to just have the confidence that no unwelcome hands were going to reach into that pot and we can all be one big place now. So I had to grin when you said you've unwound as many as you've wound.

Heather Shanahan:

Yeah. Let's go ahead and hop onto our takeaway slide, as we wrap up here. And there was a question about handouts. Handouts we're not making available, but the recording of this we are. So if you want to go back and revisit that if you participated, then certainly, that'll be an option. Or if you had to hop off, you don't know anymore. But anyway, you could go back and listen to the rest of it.

But so key takeaways, and I think, Lori, you said this one, forever is a long time. Governance and good policies are required. And steward your donors and communicate the needs of your organization. Anything else from our panelists that you would add in closing here that you want folks to be mindful of?

Christina:

[inaudible 00:57:24] jump in. I think there's something to be said, circling back to the earlier conversation about asking the donors to share their story or allow us to share their story and make an announcement. If there is a donor that you're working with at your organization that's pretty hesitant to do that, I would ask them to maybe put together a reason why they chose your organization. And just have something in writing documented so that you can share it, even if it's after the fact.

So, we talk a lot about stewarding our donors and cultivating our donors. We can do that once they've passed as well. And I think there's something really symbolic about going back to Lori's conversation about forever. Honoring them, whether it's with something that's a physical feature like a plaque or a naming opportunity on a campus or organization. But just having a quote, having a testimonial, I think again, it just will inspire future donors.

Heather Shanahan:

That's great. Wonderful. Well, I can't thank you enough, Ed, Lori, Christina, and Dan for joining us this afternoon. I hope this was helpful information for everyone who joined us in attendance today. And appreciate your expertise and your time. And I hope everybody has a great rest of the afternoon. Thank you very much.

Ed Chaney:

Thank you.

Dan Simon:

Great seeing everybody. Bye.