Endowment Funds and the Community Foundation

WAYNE STEWART
Executive Director, The Calgary Foundation

Introduction

Endowments are a funding mechanism whose time has come.

The stimuli to create endowments are coming from both sides of the funding equation. Charitable service agencies, whose traditional funding sources (government, corporations or private individuals) are in decline, are turning to endowments to reduce the stress and anxiety of annual appeals. Donors are increasingly frustrated with what is done with the annual drain on their hard-earned incomes, whether they are contributing to the general good through the tax system or simply making a donation to their favourite charities. The agency seeks security and a sound financial base on which to plan. Donors seek accountability and responsible use of their donations.

The recent emphasis on planned giving has further stimulated interest in endowments. Donors capable of making a large gift are attracted to the concept of planned giving, particularly for endowments. Estate planners are including consideration of charitable giving more frequently in forward financial planning for their clients.

Endowments appeal to planners, donors, and agencies. Endowments offer planners another option for their clients. For the donors, creation of an endowment ensures a lasting legacy that will bear their names and help to assure the future of their favourite charities. For service agencies, the potentially negative impact of a large one-time-only gift is mitigated and continuing support is assured.

With these apparent advantages, why haven't more charities rushed to create endowments?

Endowment – The Case For and Against

An argument can easily be made that the time for building endowments—when the economy was buoyant and Canadian donors were generally optimistic—is long since past. Charitable agencies of all sorts, from food banks to the opera, had the opportunity to accumulate funds in good times but the majority failed to do so because they apparently saw no need. The Canadian tradition of relying on government grants lured them into a false sense of security. If they did any fund raising at all, many agencies did so solely for special projects or new approaches that would ultimately, if proven, be supported by public funds. And for those agencies that did not rely on government grants, the flow of private funds appeared adequate and growing.

As cutbacks in traditional sources have occurred, agencies are having to replace them and are, in a word, scrambling. The anxiety level is high, the activity intense and often unplanned. In their rush to survive today, the last thing on their minds is security for tomorrow. They feel that an appeal for endowment funds will, by definition, reduce donations for annual giving. As one Calgary agency serving children told us, "...we don't want our money tied up in endowments when there are children crying at our door and we can't help them for lack of operating funds".

Both evidence and logic suggest that the opposite is, in fact, the case—appeals for endowment funds can complement annual appeals. Indeed, the appeal is to a different part of the donor's financial resources; annual donations come from annual income and donations to the endowment generally come from accumulated wealth. And, as endowments build, donors see evidence of future planning and feel that their annual donation will be used just as responsibly.

The argument that endowments reduce accountability is often advanced. In this line of reasoning, the agency with a large endowment is insulated from the accountability built into an annual appeal which enables the community to decide annually if the need continues to exist and the agency is the best way of meeting that need. The agency, so the argument continues, can become fat and lazy, resting on its laurels and carrying on its activities long past the time when the relevance of its mission has declined.

The evidence also refutes this argument. First, even successful agency endowments are unlikely to be large enough to cover total annual costs (a situation exacerbated by recent declines in income levels) and even a reduced annual appeal offers the opportunity for community assessment. Secondly, agencies with the foresight and skill to build substantial endowments are usually those which apply the same level of responsible planning to the causes and communities they serve. Often, innovation is enhanced as security and flexibility are heightened. In addition, the agency can devote a larger share of its resources to its program and less to fund raising. Finally, endowments discourage all-at-once spending of large gifts in favour of long-term planning.

Another objection to endowments lies in the attitude of funders to a large capital holding appearing on the agency's balance sheet along with a deficit operating budget for which the agency is appealing for assistance. Funders may reason that the capital should be spent before donations are sought. This has been true, particularly with government funders, but the attitude is changing and many funders are factoring the financial security of those seeking funds into their funding decisions.

On the evidence, the case for endowments appears sound. The added financial security allows effective forward planning which permits sound, rather than expedient, decisions and responsibility.

Creating and Building Endowments

(We have learned about creating and building endowments from Helen Monroe, who served as Executive Director of the San Diego Community Foundation during a period of significant growth.)[1]

To consider an endowment program we must first change our thinking; we must conceptualize endowment building as asset development rather than fund raising. We should look at endowments as a further service to our donors, an attitude that will be sure to appeal to our donor contact people.

Before we begin knocking on doors, we must develop a firm commitment to the program at the Board level. This must be accompanied by a policy statement, including a statement of intent regarding the disposition of unexpected gifts. Ms Monroe suggests that we commit a large portion (she recommends 100 per cent) of all gifts that arrive unexpectedly to the endowment fund. This policy avoids the scramble and debate that inevitably accompanies major unexpected gifts and it adds credibility when we are appealing to donors capable of making large gifts.

The policy statement can often be the most difficult step. From that point, the process involves developing a plan of action which should include a specific role for each board member and volunteer, developing materials, including a brochure and a pledge card, and implementing the plan. The fundamental tenet of fund raising holds true here as well—it is easier to ask if you first give.

Endowment funds are often built through donations from an estate, i.e., through a will or life insurance. It is, therefore, important that the agency and its endowment program become known to financial and estate planners. A direct appeal to the agency's current donors should also be made. One Calgary arts organization included information on the endowment with its annual appeal for operating funds. The message was, "We truly appreciate your ongoing support and request that you remember us in your charitable gift planning". This gentle message ought to serve as a reminder to donors who often forget their favourite charities when planning their estates.

There are also several administrative matters involved in creating an endowment. First, a separate entity, such as a society or foundation with separate charitable registration, should be created to operate the endowment and to keep it separate from the normal operation of the service agency. This enhances credibility with the donor and ensures that the agency service staff continue to focus on their core mission. Of course, the separate entity creates additional work. Government reports must be filed as required. A governing body must be set up to manage the entity, to attract funds, and to manage the funds effectively. Minutes must be kept and records maintained. Audits must be conducted and accurate accounting assured. And someone must remember to reinvest the T-bill or GIC as it comes due. Many agencies look at these tasks and conclude that they simply do not have the time and energy to pursue "that crazy idea about an endowment".

Certainly, donors ask questions before they will contribute to an endowment. They want assurance that the organization is in place to manage the funds effectively (this is pretty difficult when you're starting up). They want to know that sufficient funds will be attracted to allow a reasonable investment portfolio and that expertise to manage that portfolio is available. While they will want assurance that a separate entity holds the capital so that the agency cannot erode it, they will also be concerned about the cost of running this entity.

Endowment building is a long-term process (Helen Monroe suggests seven years from inception to maturity). Donors are demanding and administrative matters must be attended to. It is little wonder that most charitable agencies turn their attention to more immediate problems. Yet the need for financial security does not go away.

The Community Foundation as Partner

In 1921, the Winnipeg Foundation was formed as the first community foundation in Canada. Today, community foundations exist in some 60 centres across our country.[2] Their purpose is to serve their communities and their charitable needs and to contribute to the achievement of a better community. This service is manifested in a number of ways designed to serve donors, agencies and the entire community. The community foundation is a very flexible charitable vehicle whose time, like that of endowments, has come.

The basic purpose of a community foundation is to create a pooled endowment fund to help meet the needs of a whole community. Capital is owned by the foundation and held in perpetuity. Income is available to meet community needs at the discretion of the foundation board or at the direction of the donor. This direction is followed in all cases and forever.

A full range of services is available from the community foundation. Charitable receipts are issued, capital is invested carefully, income is invested until needed, audits and tax returns are completed as required, accurate records are maintained and reports are issued. Because of the pooling effect, the fund is usually large, allowing a diversified portfolio which offers better returns and keeps costs down.

Donors' confidence is enhanced as the separation of capital and effective management of that capital are assured. Long-term accountability is enhanced through a variance clause which directs the foundation to find "the nearest similar purpose" should the intended purpose cease to be relevant (the test here is a severe one) or a designated agency cease to exist. This is of particular benefit to the community at large but also of interest to donors who have no wish to have their generosity lavished on obsolete purposes. These factors and the additional support available from the foundation are very persuasive tools for endowment marketing.

Many agencies are working with community foundations to create their own endowment fund as a designated fund within the foundation's pooled fund. With a designated fund at a community foundation, the agency has the security of annual income with none of the attendant administrative requirements—the best of both worlds.

Because the foundation deals with investments as part of its core purpose, expertise is always available. Reinvestment occurs as a matter of course with no delay and no loss of income. Donor confidence is increased. Capital is preserved and its value protected (indeed, the capital is kept off the agency's balance sheet). Marketing support is available.

The community foundation serves as a good vehicle for designated funds and, as is the case with The Calgary Foundation, often actively encourages agencies to create endowments within the foundation. Several agency funds have been created at The Calgary Foundation in the past year. In all cases, the net investment return to the agency has improved. In one case, where an already existing agency fund was transferred, earned income came with the capital. Simply through inattention and lack of expertise, that income had averaged less than one per cent per year. The community foundation's performance proved to be a great improvement. Working in partnership, the agency and the foundation both benefit. The foundation's asset pool is increased and costs reduced. The agency is free to focus on its core mission while its financial security is enhanced.

Flexibility, simplicity, accuracy and care are the hallmarks of successful community foundations. They offer a real option for charitable agencies to establish endowments and help to secure their financial future.

Conclusion

Endowment funds should be an option in every agency's fund-raising plans. In addition to adding to the financial security of the agency, endowments allow effective planning which builds responsibility. Credibility is enhanced with donors and annual fund raising becomes less stressful and more successful.

Donors should encourage their favourite charities, whatever charitable field they are serving, to consider endowments.

Charitable agencies can create and build endowments without the attendant administrative fuss by working in partnership with their community foundations. The result is positive for both the agency and the community.

Working together, the agency and the community foundation build endowments for community needs and contribute to a better community.

FOOTNOTES

1. In private conversations with the author.
2. See M. Sharpe, "The Community Foundation" (1991), 10 *Philanthrop.* No. 1, p. 26.