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AN OPINION AND OVERVIEW ON ENDOWMENTS

The following comments are based on five years of providing 10 challenge grants to various non-profits in mostly the Greater Milwaukee Area. Six were startups that had not existed in the past plus two other startups that were not challenge grants.

Over that same period of time, I facilitated the improved effectiveness of 83 other endowments totaling $125MM at inception to approximately $200MM in assets over a five-year period. Nurturing the development of their mission, spending policy and investment policy, the development, recognition processes for new funds while reinforcing and maintaining the testamentary commitments.

In almost all cases, as a result of the efforts and the focus, endowments increased. However, I noticed some apparent opportunities for improving the overall management.

1. Donors generally don't indicate that testament type gifts shall go to the endowment. Many organizations do not have policy statements that say such testament giving shall go into the endowment program. Hence, on occasion, they remove endowment dollars that would permanently sustain the organization by using such funds to balance their budgets.

2. Those that are giving the endowment dollars do not give any permission or direction to maximize their returns.

3. On occasion it's not unusual that the operating boards borrow funds from the endowment on the premise of giving them a greater return than the returns they normally would get. A few of those end up becoming loans that have to be forgiven because the organizations aren't able to pay them back.

4. **It is not unusual to use the assets of endowments to guarantee bank loans. This eventually results in the endowment making good on the guarantee. Operating decisions that were delayed are then unfortunately made after the corpus of the endowment has been diminished or eliminated.**

5. Few endowment trustees are completely separated from the organization they serve, trustees are involved in commitments in the operating end of the organization. Each role has a significantly different set of responsibilities with conflict or lack of objectivity to the endowment. Passion in any organization usually lies in the operations area and their priorities are likely to prevail over preserving the endowment long term. The complaint that boards have with trustees that are completely separate is they can't control it, which is a **telling statement,** insight for which does not seem to be apparent. In the case of one board and trustee combo they weren't able to move the funds because of a conflict. In a second case a trustee was a broker in one of the funds and they selected a series that pays a significantly higher fee. Probably resulting in a higher commission to the broker. In a third case biases of trustees who were also operating people, including the paid executive of the operating end of the nonprofit, were looking to balance their budget and were conflicted. In a fourth case, operations people imposed on trustees to not move the money in a timely manner because of an operating donor's relation, costing the fund 15% of its total assets. They eventually made the decision, but it was a clear delay because of the relationship issue, annual support versus long-term trustee.

To say it another way, trustees of endowments should not be connected with the operating boards, should not have the vested interests in the operating decisions but should be working to maximize the returns to support the organization and protect its corpus from any operating decisions that might impose on it.

6. Best returns seem to come from those endowment dollars that are highly diverse and whose fund managers weight the funds based on their perception of where the best markets are in the immediate future. Further, the trustees that manage funds by consensus of the group do poorly, whereas those that select a qualified member to run the money with their oversight seem to do the best.

Conclusion: Of the 93 funds I've been drawing my information from:

1. With a few exceptions, they now all have a mission statement, spending policy and investment policy.

2. Currently 80%+ have annual programs of acknowledging endowment participants for testament, irrevocable commitments and assets received by level in the form of written materials and annual recognition events.

3. In their history, nearly all have invaded principle beyond spending policy and/or guaranteed operating loans. In some cases, resulting in the significant reduction of principle or elimination of principle. Several still have all assets exposed because of guarantees.

4. In no case were there <u>specific or irreversible prohibitions from</u>

    A. Guaranteeing operating loans

    B. Loans to operating units

    C. Trustees that do not have operations responsibilities or separate 501Cs.

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