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## FOCUS On: Payout With A Purpose- Grantmaking In A Time Of Economic Crisis

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In mid-October, amidst the chaos and fear triggered by plummeting stock values, Steve Gunderson, President of the Council on Foundations, urged donors to “continue to serve the common good in these uncommon times”. Gunderson’s comment was triggered by the growing material and psychological “belt tightening” of high net worth donors who were watching the value of their financial portfolios drop.

Gunderson’s concern is well founded. The volatility of the stock market has created a more conservative approach to spending in virtually all economic sectors. The question of how much to spend today and how much to save for tomorrow is not limited to personal or corporate spending; it affects foundations as they look at year-end payout to support the organizations and issues of greatest concern to them. In the face of shrinking endowments (from a median return rate of 13.7 percent in 2006 to 9.9 percent in 2007), serious questions emerge for trustees struggling with how to fulfill their obligations as donors and simultaneously protect the corpus. This is particularly germane given that under the five percent distribution requirement, foundations need a minimum return of 8 to 9 percent to stay even after inflation and expenses—a rate that may be difficult to achieve given the current rate of decline in foundation investment returns.

The current economic environment is not a permanent condition. Most experts feel that there will be sustainable growth and stability in the market within 12 to 18 months, but donors committed to making a difference can seize this opportunity to simultaneously be more strategic and aggressive in terms of fulfilling their philanthropic mandate. You and your clients may want to explore certain strategies that will take into account both the impact and return yielded by every charitable dollar spent. For example:

- **Accelerated Payout.** It’s important to remember that market conditions will change and investment portfolios will regain value over time. Therefore, despite, and because of, current economic conditions, this is an important and very real opportunity for a foundation to increase its payout from the traditional five percent payout rate established by the Tax Reform Act of 1969. The Act intended to establish a set of limited regulations to ensure that foundation assets were effectively being used for charitable purposes,

not to limit charitable giving. Leading philanthropy scholar Peter Frumkin urges donors not to be restricted by the five percent minimum, rather to approach the payout question as if no mandated payout rate existed.

Since payout rates need not be fixed for the life of a foundation, trustees can establish flexible annual payout rates that respond to the need and opportunities of the day. By making large, concentrated investments in specific issue areas, foundations can invest in solutions when solutions are most needed. Consider this: every one percent increase in the annual payout rate of all private foundations translates into approximately \$4 billion in new grant funds for the nonprofit sector.

Responding to economic, political or natural crises is what philanthropic dollars should be doing. The New York City-based HKH Foundation, for example, a \$30 million dollar family foundation that typically gives between \$1.5 and \$2 million in grants each year, increased its giving by one-third before the 2004 elections, a moment in time that trustees felt was auspicious to increasing civic engagement. By accelerating payout in 2004, trustees were able to leverage the opportunity provided by a changing political environment.

- **Adopt a strategy of fewer, larger gifts.** Consider creative ways to offset the detrimental effects of the economic crisis, whether or not you are increasing payout. Clients might decide to focus giving on the causes that have been most deeply impacted. By narrowing their grantmaking foci to the areas of greatest need—such as mitigating the effects of home foreclosures and job loss—and by forming close partnerships with grantees working on these issues, foundations stand to not only leverage millions in capital and assist thousands of people, but also, to prevent future unemployment and homelessness, thus ensuring a return on their charitable investments.

- **Rethink the life of the foundation.** Typically the implications of the life of a foundation are not always viewed in light of the impact of the philanthropic activities. Current social, political and economic conditions may be an excellent catalyst for introducing this topic to clients and have them consider a sunset option so that the bulk of the giving is done during the family's, or individual's lifetime. Advantages of this "give while you live" approach include greater assurance of donor intent as well as the opportunity for hands-on donors to exert greater personal control over how their money is spent. Further, it delivers a message to grantees that the funding from the foundation is not in perpetuity and they will need to secure additional funding sources as a means of ensuring their financial health

after life-limited foundations sunset. Setting foundation time limits may actually serve to protect both donors and grantees against future economic crises.

One of the most influential philanthropists of the 20th century, Julius Rosenwald, former Sears, Roebuck & Co. President, believed that “real endowments are not money, but ideas”. He advised foundation trustees to spend down their assets to address immediate needs and to trust in future generations to guide their own philanthropy. A more recent example of the life-limited foundation perspective is the Bill and Melinda Gates Foundation, which will sunset 50 years after the death of its last founding trustee. In explaining his rationale for limiting lifespan, Gates said, “I hadn’t planned on getting involved in philanthropy until later in life, when I was in my sixties, when I could devote full time to it, but the more I learned, the more I realized there is no time. Disease won’t wait.”

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