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# Endowments

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### Overview

An endowment is a permanently restricted net asset, the principal of which is protected and the income from which may be spent and is controlled by either the donor's restrictions or the organization's governing board.

An endowed *fund* is a charitable gift established in perpetuity in which the principle is invested and a small portion of the fund's balance is paid out, generally on an annual basis. An organization may have several endowed funds, established by one or more donors and for one or more purposes, in its endowment.

Endowments can be established to support the ongoing operating expenses of the organization or for designated purposes such as scholarships, projects, programs, institutes, professorships, or any aspect of its charitable work. Endowments can offer organizational stability in that they can supply revenue in years in which donations are down, or charitable need increases, and they can be a resource for new programs and innovations in prosperous years.

### Types of Endowments

In the United States, the Financial Accounting Standards Board (FASB) has identified three types of endowments:

- 1) True endowment (also called Permanent Endowment). In a true endowment, the donor states that the gift is to be held permanently as an endowment, either for general purposes or for specific programs as identified in a written agreement.

- 2) Quasi-endowment (also known as Funds Functioning as Endowment - FFE). Reserve funds, financial windfalls, or unrestricted gifts that the board elects to put into endowment are quasi-endowments. The principal may be spent.
- 3) Term endowment. An endowment created for a set period of years or until a future event (such as the death of the donor) is known as a term endowment. After the term runs out or the event takes place, the principal may be expended.

The endowed funds in the organization's endowment must be clearly labeled as one of these three types for accounting purposes. Each of the three types may be used for designated or undesignated gifts - for general purposes or to benefit specific projects.

### **Should Your Organization Establish an Endowment?**

An endowment may not be appropriate for every organization. If the organization's purpose is to solve a problem and then dissolve, it should not build an endowment. If the organization is new or does not have a solid donor base, it should focus on building infrastructure and developing supporters rather than on establishing an endowment. Endowments are most appropriate for organizations that are reasonably established and have stable income from contributions and other revenue sources and that plan to be in existence for the long term. Before starting an endowment, the organization should have adequate non-endowed reserve funds to allow it to meet unexpected challenges or to absorb major, non-annual expenses.

### **Endowment Size**

An endowment can be started with any amount of money. To determine the best endowment size for your organization, a general rule of thumb is to consider the payout amount you would like to receive annually from the endowment. Then calculate how much endowment would produce enough interest to fund that amount. An organization with a \$25,000 annual operating budget that wants a portion of the budget to be covered by the endowment might create a \$100,000 endowment that yields \$5,000 a year. An organization with a goal of developing a new program or opening a new office might need an endowment of \$1 million or more, from which they can draw \$50,000 each year.

### **Establishing the Endowment Action Program**

Once the organization has determined that it is ready to move forward with building an endowment, it should develop a comprehensive endowment action program. This begins with a board resolution designed to integrate the endowment into the organization's strategic plan. The resolution should include the purposes of the endowment and what the board intends that the endowment will provide for the organization in the future.

Included in the comprehensive endowment action program should be the case for support, measurable goals, strategies and tactics to reach the goals, and the time frame, as well as staff and budget requirements. The action program should also include plans for prospect research, management and investment of gifts, donor and volunteer stewardship and recognition, marketing, and evaluation.

The process of developing the action program should include the identification of potential endowment champions and donors. It goes without saying that the board of directors must embrace the value of an endowment to the organization and must be willing to commit the resources and time necessary to develop the endowment.

## **Endowment Campaigns**

An endowment campaign is a fundraising campaign that raises money for the organization's endowment. Like a capital campaign, it is an intensive, organized effort, executed within a specific time period. And like a capital campaign, it offers the organization a number of clear benefits:

- build familiarity with the organization
- encourage donors to "think big"
- push annual giving to new levels
- build volunteer leadership
- increase the organization's visibility among stakeholders and the community
- enables donors to pledge over several years, which allows them to consider giving larger amounts of money

For more information on campaigns -- including internal audits, feasibility studies, preparation of the gift-range table, campaign components and phases, go to **[Capital Campaigns \(/afp-ready-reference-series/afp-ready-reference-getting-ready-capital-campaign-preparandose-para-una\)](https://afpglobal.org/topics/endowments)**.

## **How Does the Endowment Campaign Relate to the Organization's Other Fundraising Efforts?**

It is critically important to integrate the endowment program into all of the organization's fundraising programs and activities and ensure that organizational resources are devoted to promoting and supporting it. If it is ignored or brushed aside in the organization's comprehensive development plan, neither the board nor the staff will be encouraged to work for its growth.

It is a myth that raising endowment funds will diminish funds for other fundraising efforts such as the annual campaign or special events. The organization should position endowment building as a separate opportunity for donors - and educate them about the role and purpose of the endowment, why operating and other expendable funds are still needed, and the importance of increasing the endowment to provide long-term support for the organization.

Annual gifts usually come from current income and are dedicated to the operating support of the organization. Most endowments are built through planned giving. The donor typically wishes to create a long-term legacy gift and will make that gift out of his/her principal asset base, not annual income. The gift may be made at death or through some other deferred giving strategy. A planned giving strategy that enhances the cash flow of the donor may positively impact the donor's annual giving commitment.

Endowment building might be part of a capital campaign that involves bricks-and-mortar projects - to provide financial stability for the long-term maintenance and upkeep of new facilities. There might be a general or specific purpose stand-alone endowment campaign, or endowment building could be part of a special mini-campaign within a larger program, such as a scholarship fund. Other ways to building endowment include earmarking proceeds from specific special events for the endowment, or transferring a percentage of annual fund revenues into the endowment.

### **Managing Endowments**

The three most commonly used endowment management structures used by nonprofit organizations are:

- Internal: development office raises funds and business office oversees investment and reporting.
- Affiliated foundation: organization establishes a separate foundation that either raises or manages endowment funds, or both.
- Community foundation: organization places endowment in a community foundation, which oversees the investment of the fund's capital and distributes a portion of the fund's year-end value back to the organization at least annually.

Organizations might choose one its approach based on the organization size, financial resources, types of endowment funds to be managed, and expertise of staff and board members.

## **Endowment Policies**

Written policies are important to ensure the trust and confidence of board and staff members, prospective donors, and professional advisors. Written policies protect the organization and its board of directors from their own and staff's mistakes and lack of knowledge. It is useful to engage financial and legal advisors in drafting policies for approval by the board.

Policies should include the purpose of the funds and how the organization will use the endowment income and principal in its operations. They should address how to handle the limits and conditions of contributions designated by the donor for a particular purpose. If there is any chance that a particular program or service funded by a restricted gift might be discontinued in the future, there must be a clear understanding with the donor at the time of the donation regarding an acceptable alternative application of the funds.

In the U.S., most states have adopted some or all provisions of the Uniform Management of Institutional Funds Act (UMIFA) approved in 1972, which provides some alternatives for giving the donor and the organization influence in defining future uses of an endowment. The act also provides a process for releasing restrictions that are no longer appropriate by mutual agreement between the organization and the donor. Most state statutes require an action of the organization's governing board to adopt and act under UMIFA.

Endowment policies should also include minimum funding levels for the endowment, guidelines for gift acceptance, allowable restrictions, provisions for investment, oversight and reporting of endowment funds, and spending rules (the percentage of principle to be distributed annually if the organization chooses not to use only interest/dividends). Historically, only endowment income could be spent and never principal, but today most endowments use a spending rule (usually about 5 percent of principal value).

## **Marketing the Endowment Program**

The purpose of endowment marketing is to give prospective donors reasons to contribute - either through outright or planned gifts. Important elements of a successful marketing strategy are consistent promotion, personal contact, and positioning the organization's mission. Some goals might include:

- Creating visibility for the organization and the people it serves
- Increasing awareness of the endowment and its purposes
- Identifying potential endowment donors
- Educating prospective donors about the various ways to make endowment gifts
- Generating donor inquiries about endowment and planned giving information and services
- Recognizing endowment donors

Key concepts to be emphasized in the marketing program might include:

- Naming opportunities
- Fulfillment of mission
- Permanence (long-term support of the organization)
- Memorial (contributing to a fund to honor an individual)
- Specific purpose (e.g., scholarship, program support)
- Funding flexibility (endowment can be funded by various combinations of outright gifts and planned gifts)

Developing and implementing the endowment marketing plan should involve staff, board members, and volunteers, and it should be an integral part of the organization's strategic plan. All appropriate departments should incorporate endowment marketing into their work plans.

A good case statement is the foundation of a good marketing plan. For more information on developing case statements, see **[Case for Support \(/topics/case-support\)](#)**.

The organization's website can be an effective tool for marketing the endowment program. You might include giving options, endowment reports, sample endowment language, and sample agreement formats. You could also explain your investment and spending policies and offer donor testimonials.

## Resources

### AFP and Other Resources on Endowments

#### AFP Resources:

- View a **[Sample Endowment Fund Agreement \(/sample-fund-agreement\)](#)**

#### *Advancing Philanthropy* Articles:

- Wolfe Everly, Josephine, "**[Donor-Advised Funds – The New Paradigm in Philanthropy \(/news/innovation-donor-advised-funds-new-paradigm-philanthropy\)](#)**," *Advancing Philanthropy*, April 2020.
- Ackerman, Deanna, "**[New Growth: Tips for Launching an Endowment Campaign \(/news/new-growth-tips-launching-endowment-campaign\)](#)**," *Advancing Philanthropy*, Spring 2017, pp. 42-44.

#### AFP Micro-Learning Videos:

- Peña, Ligia. "**[KPIs for Legacy Programs \(/ligia-pena-kpis-legacy-programs\)](#)**" 2019

#### AFP Webinars:

- Newman, Diana, "**[Four Steps to Successful Endowment Building \(https://www.pathlms.com/afp/courses/6429/sections/9586\)](https://www.pathlms.com/afp/courses/6429/sections/9586)**," 2017.

#### Links to Other Resources:

AFP provides the following listing of hyperlinks to other Internet pages as a privilege to the user. AFP does not necessarily endorse, support or attest to the accuracy of information posted on those Internet pages.

- **[“How to Start an Endowment for Your Nonprofit](http://nonprofit.about.com/od/fundraisingbasics/a/startendowment.htm?nl=1)**  
**(<http://nonprofit.about.com/od/fundraisingbasics/a/startendowment.htm?nl=1>)**”

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**01 Apr 2020** Advancing Philanthropy

**[Innovation: Donor-Advised Funds—The New Paradigm in Philanthropy](/news/innovation-donor-advised-funds-new-paradigm-philanthropy)**  
**(</news/innovation-donor-advised-funds-new-paradigm-philanthropy>)**

Josephine Wolfe Everly

**28 Feb 2019** Guides & Resources

**[Strategies to Leverage Donor Advised Fund Philanthropy](/strategies-leverage-donor-advised-fund-philanthropy)**  
**(</strategies-leverage-donor-advised-fund-philanthropy>)**

Claire Axelrad, J.D., CFRE

**07 Jan 2019** Micro-Learning Video

**[Ligia Peña: KPIs for Legacy Programs](/ligia-pena-kpis-legacy-programs)**  
**(</ligia-pena-kpis-legacy-programs>)**

**20 Dec 2018** Micro-Learning Video

**[Ligia Peña: Launching a Legacy Program / Lancer un Programme de Dons par Legs Testamentaires / Empezar un Programa de Donaciones por Herencias \(/ligia-pena-launching-legacy-program\)](#)**

01 Oct 2018 Advancing Philanthropy

**[In Chocolate We Trust: The Hershey Company Town Unwrapped – A Book Review \(/news/worth-look-chocolate-we-trust-hershey-company-town-unwrapped\)](#)**

Peter Kurie (Reviewed by Stephanie Cory)

23 Oct 2018 Tools & Templates

**[Sample Fund Agreement \(/sample-fund-agreement\)](#)**

18 Feb 2019 Guides & Resources

**[Legacy Giving Webinar: Five Questions with Ligia Peña \(/five-questions-ligia-pena\)](#)**