Raising and Investing Endowment Capital in the US Education Sector

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Raising and Investing Endowment Capital for the Education Sector

This paper is a resource for those tasked with raising and investing endowment capital on behalf of educational institutions. It draws on the combined experience of:

- **CCS Fundraising**, a global fundraising consultant working with some of the world's leading educational institutions; and
- **Koda Capital**, an independent investment governance adviser and endowment portfolio manager advising secondary and tertiary education institutions.

For educational institutions, fundraising and investment functions are often governed by the same people. For many school foundations and university councils, the desire to raise endowment capital is a top priority.

Despite some challenges in raising endowment capital, education has been one of the few charitable sectors to have had widespread success. There is an opportunity for the sector to build on this success by adopting the right mindset and dedicating resources to pursuing the appropriate strategies.

Part A of this paper explores endowment fundraising best practices, and Part B looks at how to invest endowment capital successfully. We hope that these sections are valuable to you and your organization.

Part A – Raising Educational Endowment Capital

Many educational institutions ask, "Can we raise money for an endowment?" While this is not a new question, institutions ask it with increasing frequency and urgency as they grapple with the need to increase tuition fees to balance the budget.

The question is urgent for many schools. The COVID-19 pandemic exposed how critical endowments are to school growth, sustainability, and financial security. It exacerbated the affordability challenges and the impending budgetary constraints from diminished tuition revenues, leaving schools with insufficient endowments feeling financially vulnerable. Without the safety net of endowment savings or the operating dollars drawn from investment income, some educational institutions faced a real threat of closure. Unsurprisingly, there would be renewed interest in raising money for an endowment.

However, the question, “Can we raise money for an endowment?” suggests a doubt that it is possible. The question reinforces a popular perception that endowment dollars are much harder to raise than capital project dollars because they lack the tangible aspects of campus facilities. While the impact of a facility on a school’s programs may be more obvious, the power of an endowment is far greater in its long-term, positive effect on these programs and the people they serve. Indeed, educational institutions can raise money for an endowment by focusing on some critical strategies.

1. DEMONSTRATE IMPACT

It is often more compelling to “show” than “tell,” which holds in making the case for an endowment. Showing prospective donors how endowment gifts directly support students and faculty goes a long way in helping them understand the gift’s critical impact. For example, profiles of those students for whom the educational experience would not otherwise be possible can demonstrate the importance of an endowment gift to support financial aid. A thoughtful impact statement demonstrates to the donor that their gift does not disappear into a nebulous savings account but creates access and opportunity for a deserving student.

The same is true of faculty support. Specific stories and examples of faculty work and travel reflect a gift to endow professional development opportunities. Consider hosting a donor open house at the beginning of the year when the faculty display experiences and outcomes of their summer travel and study. A successful event creates a moment when a donor can engage directly and personally with a faculty member who shares learnings from a meaningful experience. The donor will leave with a lasting sense of personal impact and a clear understanding that their gift creates a legacy of these life-changing opportunities.

PRACTICAL TIPS:

- *Tie the endowment’s growth to sustaining the institution’s mission for future generations. Create thoughtful impact statements to demonstrate tangible results of endowment gifts.*
- *Identify opportunities to engage donors through events or campus tours to demonstrate outcomes from their generosity.*
- *Highlight long-term endowment gains by reporting on performance regularly.*

2. CREATE RECOGNITION AND STEWARDSHIP OPPORTUNITIES

Named endowment funding opportunities are an essential strategy for countering the common misconception that endowment gifts do not have a direct impact. An organization can establish named funding opportunities, such as a student scholarship, a professional development fund, or an entire program. These opportunities allow an institution to celebrate the donor while sharing their gift's direct and lasting impact. The moment when a donor meets the student recipient of a scholarship or the impacted teacher is a powerful stewardship opportunity that reflects the deeply personal and lasting effect of an endowment gift. These interpersonal moments humanize endowment giving. They create powerful stories of personal and professional enrichment for the donor while also celebrating the donor as an inspiration to the rest of the community.

These stewardship opportunities can be significant for emerging philanthropists. Families building their wealth might establish a fund for a partial scholarship, hoping to grow it to a full scholarship over time. The fund provides natural opportunities to update the donors and deepen their relationship with the organization. For families with multiple connections to an educational institution, a family fund provides opportunities to cement a common bond and allows multiple members to participate meaningfully, regardless of capacity.

A word of caution — stewardship and recognition of minimal endowment funds can be difficult. Not only are small funds an administrative headache for the business office, but their returns are so small that recognition opportunities are limited. For example, a $10,000 endowed fund may generate just $500 annually at a standard 5% draw. To avoid this, many institutions have set minimums for establishing named endowed funds to ensure that the administrative costs are worthwhile; $50,000 for a faculty development fund, $500,000 for a partial scholarship, and so forth. A higher investment threshold also has the added benefit of ensuring that stewardship opportunities are more meaningful.

PRACTICAL TIPS:

- *Frequent communication is a key component of stewarding an endowment donor.*
- *If the opportunity is available for donors to meet the actual recipients of their endowment gifts, seize these moments! They humanize endowment giving.*
- *Before launching named funding opportunities, ensure clear policies and minimums are in place to avoid future confusion or complications.*
- *An endowment gift with a naming opportunity in perpetuity may increase a donor's gift, especially for donors interested in naming a capital asset.*

- *When setting a threshold for an endowment gift, consider the increase in CPI in future years, ensuring the 5% draw will cover rising costs.*

3. DEMYSTIFY ENDOWMENT MECHANICS

Even with demonstrated impact and recognition opportunities, an organization risks struggling with endowment giving if it has yet to explain what an endowment is clearly. We often take for granted that our donors and communities have a shared understanding of what an endowment is and how it functions, but without regular illustrations of utilization basics, donors think of an endowment as little more than a savings account. Without explanations and illustrations of endowment mechanics, the endowment can seem like an abstract data point that merely reflects an institution's competitive position in the marketplace but has little bearing on the institution's daily operations.

Only some donors will understand the ins and outs of financial management. (Even the trustees on a finance committee might be surprisingly misinformed about the role of an endowment in the institution's revenue strategy!) For example, donors may equate endowments with reserve funds, even though endowed assets often have legally binding restrictions on their usage.

Educational organizations can demystify the endowment through regular updates and examples of uses of endowment funds. For instance, a recurring feature in the institution's newsletter could highlight a scholarship and share the donor story behind the gift. Or setting and sharing a goal for long-term endowment growth provides more opportunities to articulate the impact of the incremental gains that, over time, lead to a larger endowment. This becomes particularly important when an institution can show the human-scale impact of the endowment today and what the potential impact will be from a right-sized endowment.

PRACTICAL TIPS:

- *Provide a clear explanation of an endowment's purpose and importance through frequent communications.*
- *Featuring endowment gifts and donors in existing publications is a great way to keep endowment giving top-of-mind.*
- *Clear charts and data will demonstrate the power of an endowment and illustrate its impact.*
- *Use routine cultivation opportunities to educate donors on endowment as a long-term strategy to increase their knowledge and comfort.*

4. TEACH FINANCE 101

Beyond defining endowment and its mechanics, it's essential to provide a clear understanding of how the endowment functions within the operating budget. Educational institutions have limited revenue sources, typically defined by tuition, annual fundraising, and the draw on endowment income. Institutions with little or no contributed endowment income to their operating budget put tremendous pressure on tuition as the primary source of revenue. While many educational institutions publish pie charts showing the revenue breakdown for tuition, annual fundraising, and investment income, few institutions take the extra step to explain the key role of each pie slice and, specifically, how a larger endowment – and the subsequent endowment draw – becomes critical in containing the growth of tuition. Regular communication outlining the role of each revenue source creates important context and helps even those closest to the institution (board members, insiders, and leadership) understand the need to raise endowment funds.

PRACTICAL TIPS:

- *Consider using an interview feature in a publication, a website landing page, or a campaign event to help donors understand important endowment metrics and their role in the broader financial strategy.*
- *Use your endowment to show the prudence and long-term commitment of the organization to create an impact for decades to come.*
- *An endowment can help demonstrate financial sophistication, building confidence in donors and potential donors.*

5. CREATING AND NURTURING A GIFT PLANNING CULTURE

Planned giving is one of the most effective opportunities to grow an endowment over the long term. Donors can stretch their support for the organization in ways they couldn't with a cash gift.

Small organizations may not feel equipped to handle complex planned gift conversations. Some educational institutions leverage the experience of alums and parents with wealth management expertise to be informal pro-bono advisors to donors considering a planned gift. And several firms provide off-the-shelf planned giving website plug-ins for smaller institutions.

The most successful planned giving programs nurture relationships when donors start to build their legacy. An organization might begin conversations about joining the bequest society when donors are in their 50s, 60s, and 70s. Including basic questions like "Have you considered including our organization in your estate plans?" in regular annual fund and campaign solicitations can inspire donors to think differently about their legacies and to move beyond thinking that cash gifts are their only philanthropic option.

Our experience at CCS suggests that many donors, particularly alums, increase their annual fund giving after documenting a planned gift intention. Through their long-term investment in their organization, they feel more ownership and commitment to the institution today and in the future.

Establishing a bequest society is simple and provides a straightforward recognition and stewardship opportunity. An organization can recognize donors in every issue of its magazine, on a plaque on campus, and through profiles on the website. Regularly featuring bequest society members in its publications and featuring them prominently on the website will provide compelling stories of those committed to making a profound and lasting impact on generations of students and faculty.

PRACTICAL TIPS:

- *Consider incorporating planned giving into your endowment growth strategy.*
- *Review your donor lists for loyal donors in their 50s, 60s, or 70s. These donors are your best prospects for planned gifts made to the endowment.*
- *Establish a bequest society to create a clear pathway towards recognition and stewardship.*
- *Speak to your donors about their giving legacy and how leaving a bequest to your endowment will enable their philanthropic legacy to impact your organization in perpetuity.*

PART A – SUMMARY

With thoughtful communication, educational institutions can make endowment fundraising as tangible as fundraising for capital projects. Context matters, though! Clearly communicating the endowment's role in the organization's broader financial strategy and the power of planned gifts to grow the endowment help build a culture of endowment giving. Creating recognition and stewardship opportunities and demonstrating human-scale impact are critical to making the endowment a tangible, rewarding gift opportunity.

Part B – Managing Educational Endowment Capital

A comprehensive investment management program for educational endowments is critical for prudent stewardship of invested capital and fundraising success. Demonstrating that you will professionally manage and govern an endowment well can help attract donors and comfort them that their gift, and subsequent legacy, is nurtured now and in the future.

Having a long-term mindset, focusing on governance, and properly addressing the following topics should put endowment investors on the right trajectory.

1. FORM AN EFFECTIVE BOARD/COMMITTEE

For most groups, delegating investment management oversight to a highly functioning investment committee committed to the institution's mission represents best practice.
It is important to determine what kind of investment committee to establish. Should it be a committee that will run the portfolio, make, and monitor individual investment decisions? Or a committee that oversees a full-time professional investment adviser? Determining this will impact who should be on the committee, how often it meets, and what strategy is implemented.

The most effective investment committees make time in the agenda for key strategic conversations that fall outside items typically focused on (e.g., portfolio performance and investment decision-making). These strategic conversations may include the following:

- Reviewing the organization's investment governance documents
- Assessing if the investment strategy aligns with the capital's purpose
- Evaluating the performance of the investment committee
- Formulating a stakeholder engagement and communication strategy
- Hearing from the executive of the institution to ensure the committee's work aligns with the organization's mission and strategy.

The world never remains static, and new opportunities and challenges constantly exist. What worked in the last decade is unlikely to be the correct answer in the next decade. Investment committees that continually look to educate themselves and for opportunities for improvement are the most effective.

PRACTICAL TIPS:

- *Dedicate time to considering what type of committee to form and what skillsets are needed around the table, over and above technical investment ability.*
- *Ensure sufficient focus is on establishing and reviewing your investment policy statement; it's the cornerstone of success for endowment investing.*
- *Stress test your portfolio to ensure you have the optimal asset mix to achieve your objectives with the least exposure to risk.*

- *Ensure you surround yourself with the right people and advice; paying to get it right will often be less costly than getting it wrong.*
- *Work with your investment adviser to get the right information in the right format to enable you to be fully informed and to make effective and efficient decisions.*

2. UNDERSTANDING OBLIGATIONS AND COMMITMENTS

Having robust records and governance processes to manage endowments is critical to ensuring an institution complies with legal obligations, fiduciary duties, and donor commitments. It is not uncommon for investment committee members to approach managing a portfolio by applying their professional investment skills per se without fully understanding the fiduciary context in which the assets exist. Over time, institutions can also lose this institutional knowledge and awareness, putting them at risk. Understanding obligations and commitments is crucial in investment strategy and management. Funds must be managed according to applicable laws, governing documents (for example, a trust deed) and in line with formal and informal donor contracts. It may be vital to segregate and quarantine assets to avoid co-mingling assets on separate legal terms. This question may arise with donors wanting assurance that their endowment gift will be preserved, with the capital, its identity, and its purpose all protected over time. Demonstrating the integrity of accounting and reporting processes is critical, as is the ability to rely on sound governance practices.

PRACTICAL TIPS:

- *Complete and audit your endowment's legal and regulatory makeup, including all records of commitments made to donors and bequests received.*
- *If there are trusts in operation, locate the original trust deed(s) and any deeds of amendment.*
- *Work with your investment adviser to model the sustainability of gifts to ensure you are setting the right thresholds for potential donors.*
- *Capital must be segregated at many institutions into separate portfolios with differing conditions, objectives, and strategies. This may be due to different capital requirements (e.g., a building fund versus a scholarship fund), different donor commitments (e.g., a sunset clause versus a perpetual endowment), and the need to quarantine donated assets for legal and/or reporting reasons.*

3. DEVELOPING INVESTMENT GOVERNANCE PRACTICES

Good governance is essential for effectively managing endowment capital and fundamental to raising endowment capital. Demonstrating effective governance will give donors confidence that their gift will be well stewarded now and into the future.

Good investment governance of an endowment typically involves having clear delegations of authority, a well-run investment committee with the right people around the table, and a thoughtful investment policy that is adhered to and regularly reviewed.

The two key investment governance documents are:

1. **Investment Committee Charter** — this document should be clear on delegations and clearly articulate what type of investment committee the organization has put in place. It should unequivocally state how you make decisions.
2. **Investment Policy Statement** — this document is critical to successfully investing endowment capital. It clearly defines objectives and parameters, addressing responsible investment, liquidity, risk, and return.

Clear spending policies and cash-flow budgets are critical, and you should communicate these to the investment committee to help to ensure two equally important outcomes. Firstly, the appropriate liquidity is in place for distributions back to the school or university. Secondly, funds not required for liquidity purposes can be invested optimally.

PRACTICAL TIPS:

- *Take the time to get your investment policy right. Putting the time into this document will give you confidence that you have the right investment framework in all market cycles.*
- *Make sure your investment policy reflects the legal and fiduciary context in which you hold the assets, and make sure investment committee members understand this context.*
- *Remember that the investment process is a means to an end — the end being the purpose of the donated funds, be that the institution's overall mission or a more specific purpose.*
- *From time to time, endowment donors may want to see your investment policy, so write it with external stakeholders in mind.*

4. FORMING AN EFFECTIVE INVESTMENT STRATEGY

Investing on behalf of a long-term, potentially perpetual endowment comes with distinct benefits. Institutions can take a multi-generational mindset and invest through market cycles, using illiquidity premiums and long-term global thematics to generate additional alpha (excess returns above the market). Leading global educational endowments have understood this for decades and, over that time, have looked to invest in a broader and more diverse set of asset classes to help drive returns and reduce risk. Educational endowments are beginning to finesse their approach and move their portfolios away from simple listed equity and bond allocations. This shift requires a series of adjustments, which often involve reviewing and updating:

- Investment policy settings - allowing for options like a more diverse group of investments and greater illiquidity, where appropriate.
- Investment fiduciaries – to ensure the right skill sets and attitudes are in place for prudent oversight of a new strategy.
- Investment advisory arrangements- identifying the right partner to provide research and access to global investment opportunities across core and niche asset classes.

Educational endowments must also adjust their strategy to consider the community and environment their institutions operate within. Responsible investment is mainstream today, and investors expect educational bodies to invest in line with their mission, values, and stakeholder expectations. A comprehensive approach to responsible investment can help reduce risks, create new return drivers, and enhance diversification.

PRACTICAL TIPS:

- *Review your investment approach. Do you do what is best for the organization or follow historical methods?*
- *Be careful of having your investment strategy influenced too heavily by your immediate sphere of influence. Many schools feel obligated to invest in using their alums' or parent groups' services and skills. This can add significant value, but it only sometimes leads to the best outcomes, and often an arms-length approach, using a professional, independent adviser is preferable.*
- *Expect internal stakeholders to get to grips with the concept of an endowment and how it is managed in different ways and at different rates.*
- *Community expectations are rapidly changing when it comes to responsible investment. Ensure you regularly review your investment policy and engage with your stakeholders to meet their expectations.*

- ## EFFECTIVELY COMMUNICATE WITH STAKEHOLDERS

Many donors will come up with their own ideas of how the capital they donate should be invested, and fundraisers need to be prepared to respond. A comprehensive investment policy should be a powerful engagement tool for such donors, giving them comfort that a well-thought-through investment strategy is in place. An overview of the investment management program for less detail-oriented donors might include the following:

- Who makes the decisions (e.g., an investment committee)
- A summary of the investment policy and strategy (objectives, responsible investment parameters, etc.)
- How the investment portfolio helps to achieve real-world outcomes
- A breakdown of the investment portfolio and its historical performance
- An overview of the professional investment adviser(s) appointed to manage the endowment

Donors aren't the only stakeholders who need communication. Students, faculty, and the institution's board or council should all be considered in a communication strategy. Transparency, especially around responsible investment, is critical to managing risk.
A communication strategy is not just about risk mitigation; it can also show the power of an endowment over time and the legacy donors can create for themselves and future generations of their families. Endowments provide a powerful income stream for an organization, and despite fluctuations in markets, they are often more reliable than other sources of revenue.

PRACTICAL TIPS:

- *Work with your investment adviser to find ways to demonstrate the power of endowment giving (e.g., modeling expected financial outcomes).*
- *Work with your investment adviser to showcase the endowment's prudent management.*
- *Educate your fundraising team on the basics of endowment investing and involve them in the investment process to help with their communication with donors.*
- *Take the time to map out your stakeholders, their expectations of your investment approach, and how best to communicate with them.*

PART B – SUMMARY

Endowment investing is about using the power of time, the magic of compounding, and the benefit of available tax concessions to generate exceptional outcomes for educational institutions and their students across generations. Having the luxury of time and the courage to build for the future allows institutions to invest optimally without fear of short-term needs or disruptions that comprise long-term gains.

In Conclusion

Raising philanthropic funds for educational endowments is critical to ensuring educational institutions' long-term financial stability and sustainability. The current economic environment and shifting demographics have made it increasingly difficult for institutions to rely solely on traditional funding sources, such as tuition and government grants. Philanthropy provides a valuable source of support for institutions and their mission.

The key to success in raising philanthropic funds for educational endowments is to have a clear and compelling case for support that resonates with donors. This case should include information about the institution's mission and priorities and how their gifts will support students, faculty, and the institution.

Effective stewardship and communication with donors are also essential to building and maintaining strong relationships with donors, including:

- Regularly updating donors on the impact of their gifts.
- Providing opportunities for donors to engage with the institution.
- Recognizing and acknowledging their contributions.

Investing in educational endowments is crucial to ensuring educational institutions' long-term financial stability and sustainability. As the education landscape continues to evolve and change, educational institutions need to build a diversified investment portfolio that can withstand market fluctuations and provide consistent returns.

Additionally, it is important for educational institutions to have a clear investment policy and strategy in place and to review and update it regularly as needed. This allows for a consistent and transparent approach to endowment investment and helps meet the institution's financial goals and mission.

Educational institutions must work closely with development professionals and other experts who can help them create and execute effective fundraising strategies. By taking a strategic and comprehensive approach to raising philanthropic funds, educational institutions can secure the resources they need to support their mission and provide students with the best possible education. Once philanthropic funds are secured, educational institutions need to work with experienced investment professionals and independent financial advisers who can help them navigate the complexities of investing for the long term. Ultimately, by taking a thoughtful and strategic approach to investing precious capital, educational institutions can ensure their long-term financial stability and ability to provide students with the resources and opportunities they need to succeed.

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