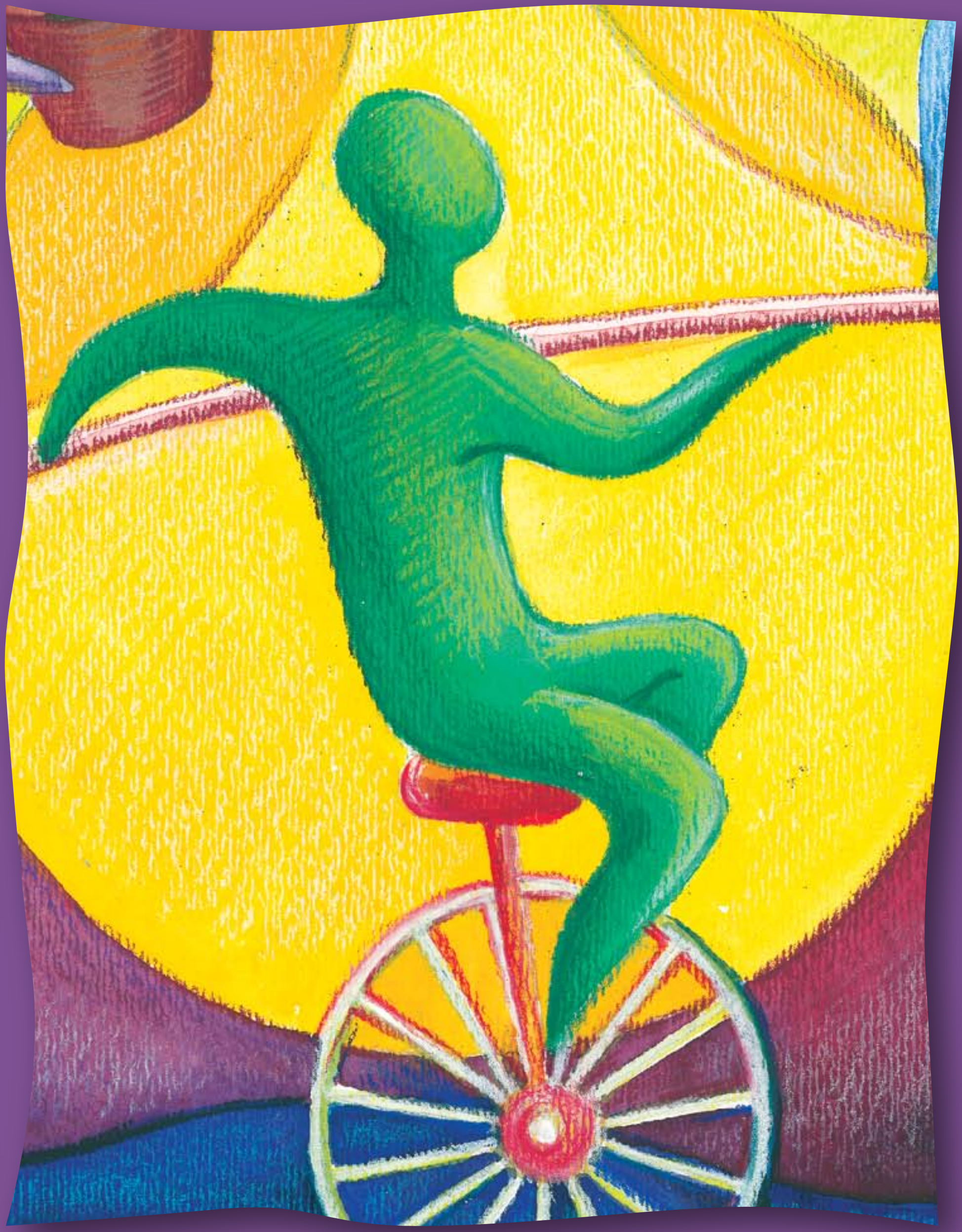
The Balancing Act



II. The Role of a Community Foundation as a Vehicle for Philanthropy

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MOTT FOUNDATION

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Close to home ... close to the heart

Over the years, we have come to embrace a simple, but inherently human, concept of the charitable impulse: Philanthropy begins on Main Street. In other words, we believe that people support causes close to home and often close to the heart.

Through our grantmaking in our hometown, our state, our nation and in selected parts of the world, we've come to view community foundations as powerful — and empowering — vehicles to nurture individual giving and to foster community.

We have witnessed repeatedly the flexibility and creativity of community foundations and community-based philanthropy not only to channel financial resources to local charities, but also to establish partnerships, foster collaborations, nurture vitality and build endowment — all to benefit communities for the long-term.

During the past 30 years, we have provided more than $122 million in grant support to the community foundation movement around the globe. But our support has gone beyond grants. We also have underwritten the cost of technical assistance given by recognized experts to individual community foundations, as well as their networks and infrastructure organizations.

Our most recent technical assistance efforts have been largely undertaken by Dorothy "Dottie" Reynolds, whom we came to know and admire when she served as the CEO of the Community Foundation of Greater Flint (CFGF) from 1990 through 1997. Her energy, enthusiasm and knowledge were constantly on display in our hometown and played a big part in the growth of CFGF.

Since leaving that post, she has served as a consultant to our community foundation grantees. In this role, Dottie, who also worked for many years for the Columbus (Ohio) Foundation, has provided advice and assistance to community foundations and support organizations in a number of countries throughout Africa, Asia, Europe and North America.

Her expertise is in such demand that we decided we wanted to share her insights more broadly through a series of three monographs that explore the various roles a community foundation can play, including as a grantmaker, a vehicle for local philanthropy and a community leader.

We hope you find this series helpful and we welcome your comments.

William S. White
President

Preface

Simply put, a community foundation has three functions. It is a grantmaker. It is a vehicle for the philanthropy of individuals, corporations and organizations that have concern for a specific geographic area. It provides leadership in the community it serves as an effective, independent arena for addressing difficult issues and/or advocating for needed programs, services or policies.

Throughout most of the nearly 100-year history of the movement, community foundations have built endowments and used income from these funds to make grants to address changing community needs and opportunities. Building endowments is a slow process, and, although it still remains central to the development of most community foundations, more attention has been paid in recent years to raising funds for immediate use.

But, that gets us ahead of our story … so let's begin with a short and simple summary of what is a long and fairly complicated narrative.

In the U.S., the history of the community foundation movement can be divided into three periods: 1) the era of the "dead donor," in which program officers recommended grants from unrestricted funds left to the foundations through estate plans (1914 until the late 1980s); 2) the era of the "living donor," in which donor-advised funds (funds that allow donors to recommend grants) dominated the field (late 1980s until the mid-2000s); and 3) the current era of "community foundation leadership," in which program officers, donors, foundation executives and their boards are forging solutions to community problems and developing strategies to take advantage of community opportunities.

The evolution of the movement outside the U.S dates to the late 1980s, and has followed a zigzag path. Many of these foundations started by playing a leadership role. Most have relied on re-granting funds secured from organized philanthropies external to their home locales. Endowment building has been spotty. Creating local donor bases has depended far more on combining the gifts of many individuals/families/groups, rather than relying on major gifts from the relatively affluent.

Nevertheless, this balancing act of being a grantmaker, a vehicle for local philanthropy and a leadership force within the community is widespread, no matter where the community foundation is located.

Over the past decade, I have had the rare privilege of working with community foundations in a number of settings, both in the U.S. and internationally. In the course of this work, I have found far more similarities than differences in the ways they operate, and I welcome this opportunity to tell the story of this balancing act through personal observations and case illustrations.

I should add that the opinions and observations presented in this monograph are mine alone, and may not reflect the views of the monograph publisher, the C.S. Mott Foundation.

Dorothy Reynolds

Dorothy Reynolds

The role of a vehicle for philanthropy

One of the most important functions of a community foundation is that of serving as a vehicle for the philanthropy of local individuals, corporations and organizations. This capacity has positioned these foundations to serve as mechanisms for sustaining programs provided by nonprofit organizations. And it is this attribute that has enabled community foundations to become one of the fastest-growing forms of philanthropy worldwide.

In the U.S., this growth became so explosive in the late 1980s and throughout the 1990s that maintaining the proper balance among making grants, developing assets and providing community leadership became difficult. When community foundation directors got together, often the first question they asked each other was not “What difference have you made in your community?” but rather “What’s your asset size?”

The flexibility of community foundations has been key to their rapid growth. Their ability to accept almost any kind of gift (cash, securities, real estate, mineral rights, even cattle or goats in some parts of the world), their ability to satisfy almost any donor interest, their careful stewardship of funds and their independent governance structures – all have contributed to the success of the community foundation movement.

Permanent endowments

In the beginning, community foundations were created to separate the management of funds in trusts from the uses of the income produced by those trusts. Traditionally, community foundations have focused on permanently endowed funds. This sets them apart from other community-based philanthropic activities.

Providing the critical vehicle *through* which donors can give back to their communities remains one of the three critical components of a successful community foundation’s mission. The others are serving as a grantmaker and providing leadership to address changing needs.

Certainly, permanently endowed funds enable the community foundation to have a stable source of revenue to meet the needs of the future. Because the foundation has this secure source of income to support its administrative and programmatic functions, it is not subject to the whims of any one donor and enjoys a certain degree of independence as it goes about meeting community needs.

Historically, community foundations in the U.S. have focused their attention on building endowments, and income from these endowments has enabled the foundations to respond to community needs by making grants. This was particularly true when most asset growth in the foundations was generated by bequests. In the U.S., most community foundations’ discretionary funds have been received after the donors’ deaths.

Benefits to donors of endowed funds

- The ability to satisfy donors' charitable instincts to "give back" to the community.
- The knowledge that a gift made at a point in time will provide income forever, and that the foundation will invest the gift so that its buying power is maintained.
- The ability to indicate the purpose for which the permanent endowment is established, accompanied by the knowledge that the community foundation has the responsibility to alter that purpose, should it become obsolete over time.
  The recognition that will be accorded to the donor, or the person for whom the fund is named, forever.
- The knowledge that decisions concerning use of income from the fund, as far into the future as can be imagined, will reside with a group of knowledgeable local citizens who will understand the needs and opportunities within the community.

It is common practice to establish minimum levels of funding to set up named funds in community foundations. This allows the donor, or another individual or entity identified by the donor, to enjoy a certain amount of immortality, because grants are made in the fund's name. This often appeals to those who do not have direct heirs or choose not to leave their entire estates to their heirs.

Most importantly, benefits from permanently endowed funds span generations. Mayors and town councils can come and go, civic leadership can be generous or mean-spirited, but permanently endowed gifts from the past continue to provide for the present and future. And the good fortune enjoyed in times of plenty produces income to fund services in times of need.

It is quite common in the U.S. for community foundations to hold endowments to benefit specific organizations. The community foundation becomes a "firewall," preserving and protecting the permanently endowed fund from the whims of an organization's board of directors whose members might see an endowment held inside the organization as a "rainy-day" fund. The community foundation also can change the beneficiary of endowed funds, should that original recipient organization go out of business or substantially change its mission. Thus, donors are assured that the cause they cared about – or something very similar – will continue to be supported in perpetuity.

For example, the Columbus (Ohio) Foundation once held an endowment to benefit a tuberculosis hospital. When that hospital closed, the governing committee of the foundation made the local chapter of the American Lung Association the beneficiary of the fund's income.

The stability that a community foundation brings to the nonprofit arena, its flexibility in accepting gifts and establishing funds that satisfy the charitable needs of local donors, and its efficiency and effective financial stewardship combine to make it an essential partner in community-based philanthropy.

Although building endowments will not address all the charitable needs of a community, there is a real place for the development of community foundations and their permanent endowments in almost every community around the globe.

As the movement to build community foundations has widened beyond North America, an immediate focus on endowment building has become less practical, because donors in many countries do not have opportunities to amass substantial wealth, the nonprofit sector cannot invest its assets in publicly

traded markets, and the urgent needs of local populations means funds that are generated must be put to use immediately.

This does not mean that there are no endowed funds outside North America. Rather, more emphasis has been put on securing regranting funds from other foundations or from government gifts, and using them immediately.

Donor-advised funds

Donor-advised funds have long been a staple in the asset development portfolios of many U.S. community foundations.

In the U.S., a donor-advised fund is one in which the donor is allowed to deduct the gift from his/her tax return in the year in which it is made, even though distributions of income and/or principal may be made over many years. The community foundation is responsible for ensuring that the recommended distribution is for a charitable purpose that is consistent with the foundation's mission. And, as is the case in all foundation distributions, its board must approve suggestions from donors about how funds are to be distributed.

However, it is important to acknowledge that there are community foundations that have not pursued this kind of fund development and have opted instead to focus their attention solely on the acquisition of discretionary, permanently endowed funds.

For the most part, the more successful and larger community foundations have achieved significant portions of their assets as a result of their enthusiasm to create advised funds and to work with donors during their lifetimes, all the while encouraging those donors to include the foundation in their estate plans.

An important conceptual rift between those foundations that largely have ignored substantial donor-advised fund development and those that have actively pursued such funds must be acknowledged. The former tends to view a community foundation primarily as a grantmaker; the latter feels comfortable with the concept of a community foundation as the vehicle through which local individuals are able to satisfy their philanthropic goals.

Some community foundations require donor-advised funds to be endowed permanently, while others encourage distribution of principal as well as income. This latter approach often results in more interaction with donors and provides more money to meet immediate community needs.

However, most U.S. community foundations are somewhere in between. They promote the development of donor-advised funds, but they are always anxious to enlarge their permanently endowed, unrestricted and broad field-of-interest resources.

As noted earlier, donor-advised funds provide the community foundation with the opportunity to develop a relationship with an individual, and this can be parlayed into the foundation's inclusion in that individual's estate plan.

When I was at the Columbus Foundation in the mid-1980s, we found that two-thirds of the individuals who had established donor-advised funds included the foundation in their estate plans. (Because the foundation was more than 40 years old at the time, many of its early supporters had passed away.)

Donor-advised funds provide the community foundation with the opportunity to develop a relationship with an individual, and this can be parlayed into the foundation's inclusion in that individual's estate plan.

The donor-advised fund really came into prominence in the 1990s, when many young donors were making significant sums of money but did not want to establish private foundations.

Many community foundations took advantage of this situation and focused their asset development efforts on the creation of donor-advised funds. In fact, quite a few almost abandoned traditional endowment-building strategies and focused all their energies in this arena.

This has been widely questioned in many quarters, and is labeled by some as the "American model," because of the perception that donor-advised funds are distributed solely for programs that interest wealthy donors and do not address community needs or the plight of the poor.

However, community foundations share with these donors grant applications for which they lack sufficient discretionary income. Because the foundations know these donors and their interests, this is often an effective means of funding important community causes.

Since the early 1990s, commercial donor-advised funds – created by investment houses as "commercial charitable gift funds" – have offered new challenges to community foundations. The latter are unlikely to outperform the investment portfolio of a Fidelity or Vanguard Fund. And they never will be able to process grant suggestions as quickly as the commercial providers.

On the other hand, community foundations know their communities and the nonprofit sector and can offer donors valuable information and insight. That will continue to be their primary advantage over the commercial donor-advised funds.

Because the investment houses are not in the business of building endowment, the entire corpus of their donor-advised funds can be distributed, which is highly valued by many of those donors who establish these funds. However, community foundations are flexible. They can allow distributions of principal from an advised fund and not restrict distributions to income only. This allows significantly more money to be made available for community use in the near term.

Many foundations have developed well-organized programs that encourage donors to support specific community causes. These efforts, which also increase interaction between the foundation and donors, appear to be working well.

At the Community Foundation for Greater Atlanta, for example, staff members become familiar with local nonprofits through discretionary grantmaking and then educate their donors about the effects of these grantees and encourage support for them. Thus, their discretionary grantmaking is supplemented significantly by distributions from donor-advised funds.

Donor-advised funds have not become widespread outside North America, but they do exist elsewhere. The community foundation in Togliattti, Russia, has created several corporate-advised funds. And community foundations in the United Kingdom allow donors to become more involved in grantmaking decisions. For example, donors might want to receive information about pending proposals, select projects to support from a short list provided by the foundation or nominate grant recipients. These donors also may meet with foundation staff to discuss expanded interests for future grantmaking.

Benefits to community foundations of donor-advised funds

Donors with advised funds comprise a natural constituency for planned gifts to community foundations. They work with foundation staff and board members as they suggest distributions from their funds and learn to respect the foundation and develop confidence in its stewardship.

Because endowment building requires focus on major gifts of assets, the community foundation usually finds that the time spent on working closely with living donors as they realize their charitable dreams will result in the establishment of a substantial planned gift. It is vital that the community foundation talk to these donors about the importance of sustaining their charitable concerns in perpetuity, and successful foundations do so.

How the vehicles are created

After a community foundation has developed policies about the kinds of gifts it will accept, created an investment policy that sets guidelines for return rates and asset mix, and established policies outlining the kinds of funds it will create, the stage is set for serious asset development.

Community foundation asset development strategies vary throughout the world. They can include coin canisters placed in strategic places in Ukraine or appeals to high-powered financial advisers in North America and the United Kingdom. The one common element essential to raising money is the “ask.” If the request is made often and strategically enough, funds will be forthcoming.

Board members almost always play critical roles in asset development. The board provides credibility and has ultimate fiscal responsibility. It should have at least some members who have connections with prospective donors, and all members must be willing advocates for the foundation as the appropriate recipient for gifts.

In North America, successful asset development efforts are relationship-based. That relationship can be between the community foundation and an individual donor, a corporation or a financial adviser. This sets the community foundation apart from other organizations such as United Ways, which also raise substantial amounts of money, but mostly through mass workplace-based giving campaigns. This is a much less individualized approach than those usually employed by community foundations.

In fact, most community foundations in North America and the United Kingdom try to avoid fundraising that competes with other charities and nonprofits. Special events such as raffles or bowling tournaments are avoided as ways to build assets. Rather, the focus is on major gifts, and the development efforts are targeted on sources who have the financial capacity to provide them. While small gifts are welcome, not much staff time and energy go toward raising them.

Asset development activity in the U.S. often is focused on securing major gifts through attorneys, certified public accountants, financial advisers, stock brokers and trust officers. These professionals have clients with resources to share. Often, they know their clients' charitable inclinations, and they understand tax implications and provide estate planning.

If professional advisers understand the flexibility and stewardship of a community foundation, if they understand that the foundation is not just another charity to give to, but rather to give *through* – they will be comfortable discussing it with clients. This approach also has proven successful in Canada and the United Kingdom.

In other parts of the world, tax benefits associated with giving are not generous, and opportunities to amass wealth, even modest wealth, are not as common. Rather, most asset development activity is focused on soliciting small gifts from individuals, on obtaining larger sums from corporations, on securing funds from local governments, or on seeking grants from private foundations.

Most community foundations in North America and the United Kingdom try to avoid fundraising that competes with other charities and nonprofits.

Many private foundation grants to community foundations outside North America have required local matching funds, thus encouraging local giving. In Germany, Poland, Russia, Slovakia, South Africa and Zimbabwe, strenuous asset development efforts have resulted in the creation of permanently endowed funds. Private foundation gifts also have provided seed money to cover administrative costs and grantmaking funds to spread the community foundation concept.

A Global Fund for Community Foundations has been created through the efforts of the Ford and Charles Stewart Mott foundations, the World Bank, the European Foundation Centre, and the Worldwide Initiative for Grantmaker Support (WINGS). By supporting community foundation development throughout the world, this resource already has provided training and technical assistance resources, as well as modest levels of seed money.

As national economies continue to grow and wealth becomes more widespread, the community foundations in Central/Eastern Europe, the former Soviet Union, the Middle East, sub-Saharan Africa, Asia, Central and South America will be well-positioned to expand both asset levels and grantmaking capacities.

Summing it up

Whether a community foundation creates permanent endowment or pursues funds for immediate grantmaking is a decision made by its board. Permanent endowment is usually thought to be an integral part of the definition of a community foundation. But perhaps a more practical definition would require that the fundraising activities of the foundation focus primarily on providing a vehicle for the gifts of local citizens, corporations or organizations, whether the end results be permanent endowment or immediate grantmaking.

Arguments can be made to support both positions. However, changes in circumstances may dictate different approaches at different points in a community foundation's life cycle. Sometimes, pursuit of a permanent endowment needs to be deferred. However, if sustainability is the ultimate goal, there is no question that creating permanent endowment is preferred. In either case, community foundations have proven to be flexible, efficient vehicles with the potential to help communities take advantage of opportunities, as well as address needs.

This has been demonstrated throughout the world, and we should expect the continued growth, expansion and evolution of this important form of philanthropy.

Limited copies of this monograph (and the others in the series) are available through the Charles Stewart Mott Foundation's Web site (Mott.org). Each monograph also can be downloaded from the Web site.

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