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The Four Steps to Setting up an Endowment Fund

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The dream of establishing long-lasting community change through your organization is possible – especially with the right financial decisions. Endowment funds are an excellent way to establish financial security and a solid reputation for long-term community transformation through your organization or institution.

The basic concept of an endowment is to set aside financial capital, then only spend from the capital's interest while leaving the principal untouched. This allows the investment to grow and further secure your organization with a solid financial foundation; however, it requires your organization to operate off of only interest earned and other available funds.

Organizations just getting started may need to implement frugal spending and creative fundraising strategies to set up their endowment fund. But once established, endowments prove to supply organizations and institutions with the strong financial platform needed to survive for decades, even in economically difficult times.

Types of Endowments



Permanent

Asset amounts are restricted for the purpose of securing an organization financially; no spending without special approval.



Term

Donor-restricted gifts are intended for a specified period of time or upon an event, such as death.



Quasi

Net assets are unrestricted by donors. The distribution of funds is internally regulated by a board of directors, which may include preserving the amount or spending certain percentages elsewhere.

STEP ONE

Analyze Your Options

An established endowment fund becomes a bedrock of financial stability, which attracts the attention of donors and investors. However, you'll need to analyze your options and make appropriate decisions before moving forward.

Ask yourself and your organization the following questions:

- Is your organization willing to make a long-term commitment to delegate funds for the future?
- Are you willing to implement relevant policies and procedures to your endowment fund?
- Are you prepared with the leadership board necessary to follow through with oversight of the endowment? Or would you prefer a third party to manage the endowment?
- Does your organization have the internal capacity to administer, track, and report endowed funds?
- What level of restriction would you like to place on your endowment? Would you like it to be flexible or rigid when accessing, and for what purposes?

STEP TWO

Establish Endowment Support

Proper preparations for an endowment fund are helpful in every phase of its growth and development. It is equally important that your board members understand the long-term benefits of incorporating endowment funds into your organization. When economic difficulties arise and an organization lacks sufficient capital, programs and/or workers often need to be reduced, and the organization may take on debt. Adequate capital protects an organization through economic downturns or other negative impacts.

A main part of the endowment process is gaining more clarity around your vision for the future, and ensuring that your organization is ready to take the necessary steps for implementation.

Here are some appropriate preparations:

- Establish in-depth training for your board members, leadership team, and staff
- Make arrangements for a third-party overseer or in-house management of the endowment
- Outline and budget a marketing plan

Get a more in-depth look at the preparation process as part of our [professional financial planning services](#).

STEP THREE

Understand Policies and State Rules

Policies apply in accordance with the type of endowment fund enacted. For example, with permanent endowments, grants of at least 5% of the foundation's investment assets need to be acquired annually. Grants must be made only to nonprofits, and the foundation must pay a 1 – 2% excise tax on the organization's investment assets each year. A tax reporting on form 990-PF also needs to be filed annually.

Investment, withdrawal, and usage policies govern how endowment funds operate.

Investment policy	Withdrawal policy	Usage policy
Dictates what type of investments a manager is allowed to make, and how aggressive the manager can be when seeking to meet return targets.	Establishes the amount the donee organization is permitted to take out from the fund each period.	Explains the purposes for which the fund can be used and ensures that funds are being used appropriately and effectively.

State endowment fund restrictions

The [Uniform Prudent Management of Institutional Funds Act \(UPMIFA\)](#) offers guidelines that may affect endowment spending rates. These guidelines protect an organization from spending frivolously from its capital.

Several factors are considered when determining spending levels, including:

- Local and national economic conditions
- Longevity and maintenance history of an endowment fund
- The organization's investment policy
- Anticipated investment appreciations and total income return

STEP FOUR

Sign Agreements and Implement Growth Strategies

After establishing preliminary decisions and understanding all policies and rules involved, agreements will need to be drawn up and finalized.

Agreements typically include the following criteria:



Date of agreement



Initial endowment
amount



Signatures



Governing policies and
other guidelines



Timeline of forecasted
assets and their amounts

Market to donors for continual endowment support

Implementing targeted marketing tactics for your new endowment fund is a smart way to grow your initial investment. You might consider using donor testimonials (video or written) to gain visibility and generate interest. Testimonials powerfully showcase the success of your mission statement and help others see the value community members place on the future of your local partnership.

Overall, multichannel marketing through regular communication is key to visibility and gaining recognition. In time, you will see the benefits of your marketing efforts as the endowment increases.

Endowment funds are meant to anchor your organization. With the right preparations and marketing tactics, they can help secure a financial foundation that will benefit your organization well into the future.

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