Endowments for Global Health Interventions

December 2022
The Taimaka Project

Taimaka

The Taimaka Project is a joint Nigerian-American non-profit focused on tackling acute childhood malnutrition through treatment and scalable innovation. Its goal is to reduce the cost per child of malnutrition treatment by 20% in the next 5 years, freeing up $3.4 million to treat 50,000 additional children every year, in perpetuity.

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Disclaimer

About this report

This report was commissioned by the Taimaka Project, a joint Nigerian-American non-profit focused on tackling acute childhood malnutrition through treatment and scalable innovation. As an organization committed to cost-effectiveness and spending every dollar to do as much good as possible, we're always exploring innovative, evidence-based financing mechanisms to help maximize our impact.

This report on endowments-based financing is part of that mission. By providing an exploratory overview of the benefits, drawbacks, and logistics of financing an endowment to fund a program, this report shines a light on potential options for Taimaka to pursue in the coming years. Equally importantly, we hope that it provides a practical and well-evidenced overview of endowment-based financing options for other non-profits in global health pursuing cost-effectiveness and sustainable impact. We also hope that it can serve as a jumping-off point for further research and feasibility studies.

While this report centers on the context of global health programming, the lessons and financing modeling provided are broadly applicable to development interventions.

1. Executive Summary

This report on endowment-based financing for global health interventions has two purposes:

1. Summarize considerations for and against a non-profit raising an endowment, from a cost effectiveness perspective.

2. Accelerate the start of the diligence process for global health charities and potential donors interested in endowment building by providing a jumping-off point for future research and feasibility studies, acting upon the lessons and modeling from this report.

This report is motivated by an understanding that inconsistent funding is a barrier to achieving the potential of many global health interventions.

Health outcomes are often reliant on consistent patterns of service delivery (e.g., for chronic disease, or a course of vaccination) or high levels of population coverage (e.g., reducing the transmissibility of a disease). In these cases, the stakes of consistency are high. If the last 10% of an intervention is not implemented, it can undermine the utility of the first 90%. Guaranteed consistency in financing could help interventions better plan programs over the course of longer time-scales and avoid inconsistencies in program funding that translate to worsened outcomes and wasted funding.

Even outside of the specific context of global health interventions, inconsistent financing can reduce the cost-effectiveness of organizations seeking to do good. The time and resources put into fundraising and planning around inconsistent funding streams can drain organizations of resources that could be more cost-effectively spent on effective program implementation.

This report examines endowment funding as a potential solution to these problems.

The outcomes of our analysis in this report are based on the principle of **cost effectiveness**. Given a limited number of resources (especially money) put towards interventions that can improve the world, we want to determine how charities can do the most good possible for the people they serve. As such, the primary outcome this report considers is whether raising an endowment would likely result in better outcomes (deaths averted, disease burden reduced, etc.) than if the endowment were not raised.

Based on an examination of five factors regarding the impact of endowment-based financing on the cost-effectiveness of an organization's intervention, we find that endowment funding is a promising model for global health charities that provide cost effective interventions addressing long-term community needs.

In summary, endowments can help 1) charities provide sustainable coverage to the populations they serve, 2) run more efficiently, and 3) make management decisions better aligned with their mission.

In addition to a qualitative examination of these five factors, we have compiled an interactive model, referenced at various points in the report, which illustrates the potential cost effectiveness a hypothetical charity can achieve through endowment funding, as compared to a lump sum cash transfers baseline :

https://my.causal.app/models/111828.

The report proceeds as follows:

Section 2 provides background information on endowments, including different legal structures and spending strategies which may be relevant to global health charities.

Section 3 provides a qualitative analysis of five factors relevant to whether charities should start an endowment, including how an endowment will affect the charity's own operations, how to consider opportunity costs, and the implications of different endowment structures on organizational flexibility. An analysis of these five factors in the context of an organization's unique context and structure can provide a road-map for whether an endowment may be worth exploring.

Section 4 provides a timeline of the endowment building process, with an emphasis on organization, fundraising, and management. We summarize well-regarded sources not specific to global health to provide a starting point for further research. Our intent is for this section to be time-saving for readers interested in building an endowment, with recommendations for further reading provided.

2. What is an endowment?

An endowment is, broadly speaking, a pool of funds set aside today in order to fund a charity's future operations. The endowment is invested, either passively to track a portfolio (e.g., a mix of bonds and index funds), or actively managed by a financial firm (e.g., a hedge fund).

Restricted and unrestricted (quasi) endowments

The term 'endowment' is used to refer to a range of entities with very different legal statuses.

A **restricted endowment** is one where the charity's board is legally constrained by the donor's intent. It is common for restricted endowments to be permanent, meaning that the charity may only spend the investment income from the endowment, rather than the initial principal. Other donor stipulations restrict the causes on which an endowment can be spent. For example, a university endowment may be earmarked for a specific scholarship, in such a way that the university's board has limited legal options for changing this, even decades into the future.

On the other end of the spectrum are **unrestricted endowments**, also known as quasi endowments. These funds are entirely controlled by the charity's board of directors; although boards can and typically do set internal policies concerning how an unrestricted endowment should be spent, these are not legally enforceable by donors (i.e., charities can broadly spend this money however they want).

In the context of global health, restricted endowments are likely suboptimal, as circumstances and evidence change.

A 2022 Taft Law bulletin provides a hypothetical example of a restricted endowment set up to fund research into smallpox eradication.[1] Obviously, the restriction is no longer viable as smallpox has been eradicated worldwide. However, in the case where the original donor is deceased, removing this restriction requires legal action, which is intractable and potentially very expensive. In contrast, donors may be justifiably reluctant to donate to a quasi endowment because they have few legal protections against misuse of their donations. The 'Adaptiveness...' section discusses this problem in more detail, and provides recommendations as to how restrictions might be phrased to reconcile the preferences of both charities and their donors.

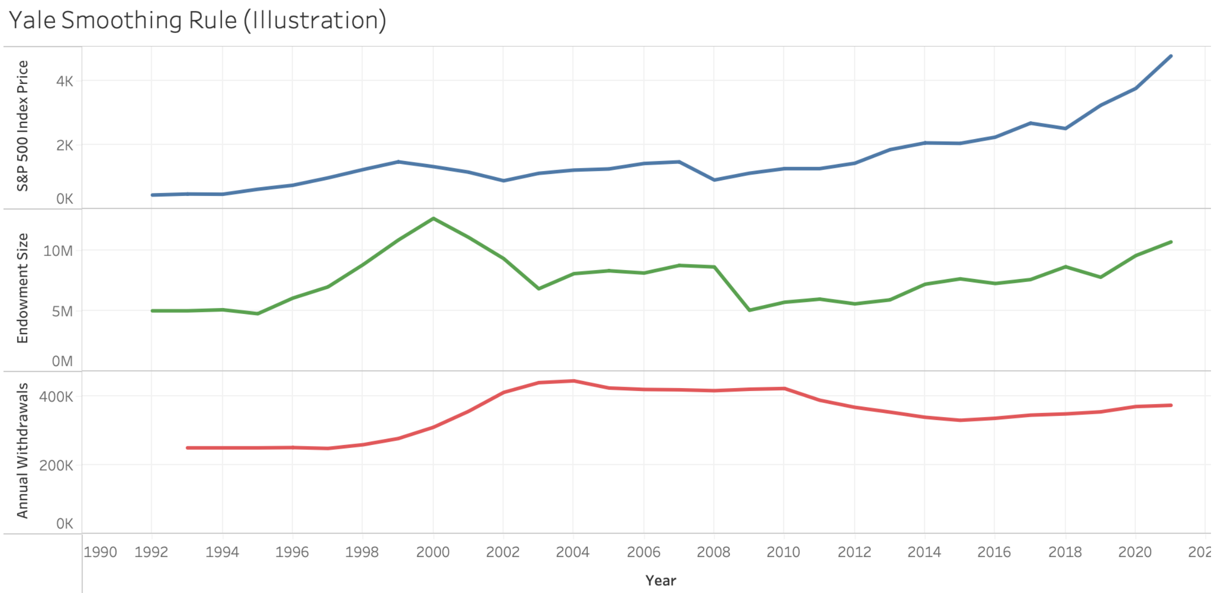
Market volatility and smoothing

Regardless of structure, an endowment can be a source of continuous funding for a global health intervention. But how can this be, in the context of recent (and historical) market volatility and macroeconomic uncertainty? Global health charities in particular need a far more consistent source of funding than global markets–even for risk-averse, lower-return portfolios–have to offer; pre-committing to a fixed spending rate (common among endowments) is a non-starter.

Thankfully, various smoothing rules have been developed in order to mitigate the challenge posed by market volatility. For example, the Yale Rule, used by Yale University, aims to reduce the extent to which idiosyncratic shocks disrupt the university's spending by setting its annual spending rate using a weighted average of previous years' performance, rather than exclusively the current year.[2]

One more drastic approach, which may be necessary to fund health interventions, is to fix the periodic withdrawal from the endowment to inflation-adjusted program costs which ensures that the intervention is fully funded regardless of the endowment's performance. We have constructed a simple model that helps to illustrate what this may look like over time, for a user-inputted market rate of return, initial endowment size, and annual inflation-adjusted withdrawal amount.

Overall, charities and their donors have flexibility to set up endowments in a way that may plausibly help enhance their social impact, and ensure a long-lasting community presence. The following section evaluates arguments in favor of and against building an endowment, specifically asking which charities are best suited to the endowment funding model, and in which cases such a model would be counterproductive.



Year-by-year endowment size and withdrawals prescribed by the Yale smoothing rule, assuming that the endowment was fully invested in the S&P 500 index, with a 5% spending long-term spending target and initial investment of $5M USD.

This section outlines **five factors** related to the advantages and disadvantages of endowment funding, with a strong focus on how an endowment might change a charity's effectiveness at serving its beneficiaries.

Factor 1: Long-term need

Section summary: Charities not in need of future support should not build an endowment.

The most basic criterion for starting an endowment fund is that the charity works on a problem in need of future support. For example, a charity using a variety of strategies to reduce the disease burden of malaria will likely be valuable for decades to come. On the other hand, short-term humanitarian interventions, such as an organization designed exclusively to rebuild critical infrastructure after one specific natural disaster, are less suitable candidates for endowment funding.

Two other factors influencing the suitability of an intervention for long-term funding is a) whether we expect the beneficiary population to become substantially wealthier in the future (potentially reducing the need for a charity to provide the intervention), and b) whether we expect our knowledge about the intervention to become more accurate in the future (potentially increasing the cost effectiveness over time).

One case we have not explored is the use of an endowment as an 'emergency fund' for charities to draw upon only occasionally when operations require it. For example, a charity might retain a $5M USD endowment fund, but draw upon it only when a certain disaster occurs to fund emergency operations. Our report focuses on instances where an endowment might provide consistent, year-on-year funding, akin to large university endowments.

Factor 2: Costs of continuous fundraising vs managing an endowment

Section summary: We predict that the costs of continuous fundraising for the average charity exceed the costs of managing an endowment in the long-term.

Costs of fundraising

Year-round fundraising in order to sustain operations takes time and money which could otherwise have been used to help people. For charities operating in economically more developed countries, it is often expected that fundraising costs as total expenditure (FCE) are approximately 15%.[3] Assuming similar costs for charities operating in the developing world, this is a sizable fraction of total funds that could have been spent on helping people directly, or funding the administrative support staff that allow charities to operate in the first place.

In smaller NGOs without dedicated fundraising departments, aid workers may attempt to balance important operational work with fundraising duties. This has the effect of increasing the number of aid workers NGOs need to hire, increasing the chance of operational problems, or (realistically) some combination of the two.

An endowment addresses this problem by either eliminating the need for fundraising entirely, or by reducing the amount of money that needs to be raised and the frequency with which fundraising needs to occur. This is particularly true over long time scales. While the initial principal of the the endowment may need to be raised over 1-2 years depending on the size of the endowment and the skill and connections of the fundraising team, the endowment can hypothetically generate returns that cover some, if not all, of the costs of a program, decreasing funding costs over time.

One important caveat is that, if an endowment does not fully cover operational costs, the costs of fundraising may not scale down linearly with reductions in the funding gap. Fundraising methods such as social media campaigns may require larger upfront costs, but easily scale once set up. For example, if it takes a charity 40 labor-hours to raise $20,000 through a social media campaign, it may still take about the same amount of time to set up such a campaign if the funding gap to be filled is only $10,000. Conversely, we would expect the labor and monetary cost of fundraising methods like phoning past donors to scale down linearly with the amount of money needed; a charity may only need to spend half the time and/or money to raise $10,000 than it did to raise $20,000 pre-endowment.

Costs of endowment management

Many experts recommend that endowment funds be passively managed. In these cases, fees to firms like Vanguard tend to be comparatively small, and–in most years–completely offset by the financial returns produced. However, there are other costs associated with an endowment, namely the costs of legal advice, the initial donation drive to raise the endowment (if raising from many smaller donors), and (potentially) staff labor spent on communicating with donors after the endowment has been raised.

This is a point of uncertainty in our research so far. On average, we estimate that the aforementioned costs are smaller than those associated with regularly taking in donations. Setting up an endowment is very likely to come with higher initial costs, but will ultimately consume less resources than the continuous fundraising efforts of many charities.

However, the following considerations are likely relevant in determining whether raising an endowment will reduce net costs?

1. Is the charity fundraising from a small number of high-net worth individuals and/or large grantmakers? If so, this might decrease the costs associated with a more grassroots fundraising drive.

2. In which country is the charity's endowment based? This will change the tax implications of endowment funding, as well as the financial markets in which the endowment can be invested.

3. Will the endowment be funded from primarily small donors gradually over time? In this case, the costs of fundraising may rise until the full endowment amount is raised. On the other hand, if an endowment will be funded primarily by one-off donations from very large donors who do not require a continuous fundraising campaign, costs are likely much lower.

Factor 3: Quality of decision making and incentive alignment

Section summary: On one hand, a de facto continuous source of funding reduces a charity's accountability to its donors. On the other hand, this can also enhance its ability to make better decisions in cases where social benefit and optics conflict. We argue that, in most cases, the second effect is larger than the first.

There are many considerations that should affect a charity's decision making. How can it achieve the highest social impact for a given amount of money? How can it ensure that the assistance it provides makes a long-term contribution to the fight against poverty and deprivation? When charities–and the people employed by them–rely on year-round fundraising to make ends meet, they must include another consideration when making important decisions: How will this affect donations?

Problematically, that which appeals to most donors may not be aligned with cost effectiveness. One notoriously ineffective, yet appealing, intervention is the Playpump, a merry-go-round that pumps water as children use it to play. Playpump International, the NGO behind the Playpump, attracted millions of dollars in US government aid, celebrity endorsements, and corporate partnerships. But this initial acclaim gave way to some unfortunate realities. Children did not want to play on a merry-go-round that required the constant force needed to pump water, let alone in the early morning when water demand was highest. Each Playpump cost as much as four hand pumps for conventional wells, and required extensive maintenance. As one water NGO leader put it, "their marketing is perfect, but the final idea does not work".[4]

Obviously, this is an extreme example, but this failure of incentives is not limited to one charity. From the Guardian:

> One director of an African water charity... described how corruption on the ground was rife, giving the example of how some international contractors paid more than $1,000 a day by water charities to drill boreholes had little concern for whether drilling was even appropriate, just as long as they kept themselves in a job. He concluded grimly: «If anyone ever told the truth, no one would give us anything.» And this is the catch-22 many good charities find themselves in. They can keep quiet and watch money wasted in massive quantities, or expose the waste and risk damaging charitable giving to the sector as a whole.

We believe that most charities have good intentions and the will to ensure they achieve their goals. However, even though most cases are not as egregious as Playpump International, NGOs may very well be pressured into optimizing for donor appeal at the cost of not doing what they know is most effective. One prevalent example across the NGO space is donors over relying on overhead costs as a proxy for effectiveness, as identified in a 2017 IZA World of Labor report.[5]

The subsequent emphasis on keeping overhead costs low "can lead to counterproductive outcomes for charities, such as underinvestment in staff and administrative support, which hamper their effectiveness". Although reducing overhead costs is obviously good when we hold impact constant, the report finds that refraining from hiring key staff ultimately impedes many NGOs in achieving their potential impact. The continuous need to appeal to donors prevents charities from helping as many people as they could.

Endowments better align the incentives of organizations towards impact (e.g., cost-effectiveness), as their funding is not as continuously tied to the optics of the intervention as it would be under a model that required constant fundraising. In short, NGOs that have a strong internal commitment to cost-effectiveness may become even more cost-effective under an endowment funding model that allows them to focus on impact, rather than optics.

On the other hand, the need to continually fundraise may provide an additional incentive for charities to achieve their goals. If a charity operates ineffectively, or spends excessively, leaders may fear a reprisal from donors. While this effect probably does exist, at least in some organizations, there is good reason to doubt that donors provide a sufficiently large deterrent from wasteful spending. As discussed above, donors often lack crucial information about the most important outcomes a charity causes. If a charity's leadership is not motivated by social impact, it is possible for them to successfully misrepresent the efficacy of their organization to prospective donors (e.g., "we have drilled 1000 wells", when, in reality, few of those wells are viable).

One exception to this is if charities are being consistently funded by grantmakers with the capacity and motivation to interrogate their effectiveness. Some grantmakers have a track record of consistently funding cost effective interventions, ceasing to fund less effective interventions, and not requiring charities to invest large amounts of resources into grant applications. In this specific case, appealing to donors may reinforce good incentives rather than undermining them.

This being said, organizations funded by endowments may still have an incentive to show results to the donor(s) who provided the original capital for the endowment.

Factor 4: Adaptiveness under different endowment structures

Section summary: There is a serious risk that an endowment constrains a charity's ability to adapt to changing circumstances and evidence. Following on from the legal options explained in the summary, we argue that raising an endowment does not necessarily come at a high cost to flexible decision making, provided the charity does not anticipate frequent shifts in humanitarian focus.

Many great charities change their approaches in light of new evidence and changing circumstances. The Malaria Consortium, for example, currently engages in a variety of approaches to reducing the disease burden of malaria, including bed net (LLIN) distributions, chemoprevention, and rapid diagnostic tests.[6] It is also involved in the coordination of public, private, and philanthropic actors in some countries to improve each sector's treatment of malaria. As new technologies, such as malaria vaccines and gene drives, come to fruition, it would be reasonable to expect the Malaria Consortium to adapt its strategy over time. Being adaptive, for many charities, is not only conducive towards achieving the ultimate mission–it is necessary.

Certain kinds of endowment funding may be overly restrictive, and get in the way of achieving the charity's goals. Two concerning types of restrictions are:

1. **Time restrictions** that require charities to hold funds donated to their endowments in perpetuity may force them to keep yearly spending consistent, when this is not suitable for the charity's needs.

2. **Purpose restrictions** that require charities to use funds for a particular purpose (e.g., to address a particular disease, or region) may cause a suboptimal allocation of resources. This might persist over exceptionally long periods of time without legal recourse.

Fortunately, options exist to mitigate concerns about inflexibility. We briefly outline them here, with the caveat that this is not legal advice, and is based exclusively on our research of US policy and practice. Endowments domiciled elsewhere may face very different laws and norms. One key takeaway from these options is that the legal structures of endowments are not straightforward, and that seeking professional legal advice is prudent for charities considering endowment funding.

1. Quasi-endowments are made from unrestricted donations, and restricted only by the charity's board. One use of a quasi-endowment is to completely fund a charity's operating costs. In the United States, these are not legally classified as endowments, and appear to completely side step the concerns listed above.

2. Soliciting donations with broad, rather than narrow, purpose restrictions (e.g., "to address malnutrition" instead of "to implement X specific intervention in Y location") can allow charities to allocate resources flexibly.

3. Establish sunset clauses that stipulate that the endowment should be dissolved if certain conditions (e.g., WHO statistics show fewer than 1,000 cases annually of child malnutrition in the region) are met. Dissolution may involve either "sunsetting", whereby an endowed charity intentionally spends much more of its endowment than is sustainable, with the intention of spending all of its funds in a specified number of years.[7] It can also entail–with the right legal structure–transferring endowment assets to another organization, such as a large NGO working in the same space (e.g., UNICEF).

Overall, ensuring adaptiveness for charities with endowments is not a neglected field. Although the needs of global health charities may be unique among other charities with similar funding strategies, we consider it likely that existing legal structures and accommodations can allow for suitable flexibility.

Factor 5: Opportunity costs for donors

Section summary: Asking donors to commit funds that will only be spent later seems potentially harmful. Instead, they could spend that money on alleviating current suffering. This opportunity cost is, at first glance, concerning because there are many people deeply in need today. Additionally, many interventions produce social returns; money in hand for a family today invested into human and physical capital results in more money in hand tomorrow. We think these objections should deter some charities from starting an endowment, but become relatively unimportant under certain conditions, as quantified in our publicly accessible quantitative model.

Opportunity costs

It is first important to establish a baseline for where donors would have spent their money otherwise. For example, you could compare a donation to its endowment with a lump-sum donation towards **cash transfers** directly to those in poverty. This represents an intuitive principle: we should not spend money on health interventions if that same money would produce more social good if simply given directly to those in absolute poverty. We extend this principle to endowment-building: we should not raise money for an endowment, if it would produce more social good if directly distributed to households in poverty today, as a lump sum.

Depending on where and how a charity is fundraising, a reasonable baseline might be much lower. For example, if raising money from donors in wealthy countries who would have otherwise spent on luxury goods, or substantially less effective causes, being more effective than cash transfers may be an overly punishing baseline.

Social returns

Providing healthcare and other forms of assistance to people in absolute poverty can make them more economically productive. They can then spend the additional income on productivity-raising investments, such as in accessing better healthcare. This effect of this virtuous cycle is sometimes called the "social rate of return". One disadvantage of keeping funds in an endowment is that the charity loses out on this social rate of return.

The social rate of return for some interventions is indeed higher than the rate of return on global stock markets. Installing iron roofs in certain kinds of family homes produced a social return of anywhere between 7% and 48%, depending on the trial, whereas a charity might expect a 5% annual return on an endowment.[8] In other words, up to 48% of the cost to a charity of installing an iron roof may be recouped by the recipient families in the following year. In contrast, an endowment might only grow by 5% on average each year.

However, the unique advantage of investing through an endowment is that the returns **compound** consistently over time at the ~5% average rate. In contrast, the social returns are gradually diluted towards the ~2% world rate of economic growth, as the income spent by recipients spreads through the global economy.

This is a somewhat confusing, yet extremely important distinction. Crucially, this argument does not require us to believe that we know better than people in poverty how best to spend money. Even direct cash transfers to households facing poverty may face this objection; when we provide people with cash transfers, they spend the cash on things that will improve their lives. For example, a subsistence farmer may buy a tractor, which makes them 50% more productive in the coming year.

However, this high rate of social return does not compound forever; the tractor manufacturer does not donate its increased profits back to the direct cash transfer charity. Instead, the positive effects of the donation spread out over time, until those positive effects grow at the world rate of economic growth. The world rate of economic growth is about 2.25%–less than we can make by investing in financial markets.[9]

Although the social rate of return argument is not as pressing as it initially seems, it does reveal an important lesson for charities considering an endowment. If donors to an endowment would otherwise directly fund interventions of a similar level of cost effectiveness, then dispersing funds over a longer period of time may be less effective than spending money now.

Quantitative model

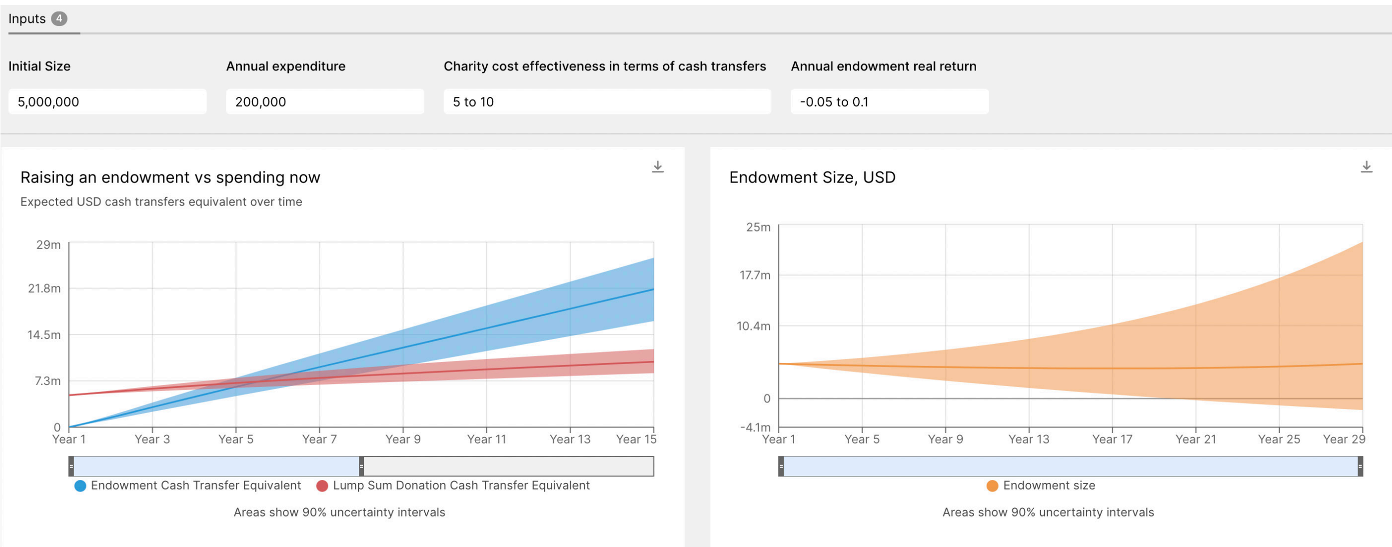
We summarize these considerations in a quantitative model that can be publicly accessed through the following link, along with one of the output figures, for Taimaka's own parameters.

This model can be used as a back-of-the-envelope estimate of how a charitable endowment can grow over time, and the impact it would generate, depending on some simple background assumptions.

The result illustrated by the model, as in the screenshot below, is that for a charity sufficiently more cost effective than the counterfactual baseline, a donation to the endowment can quickly overtake a lump sum donation to the baseline cause in terms of good produced.

The model can be accessed at the following link:

https://my.causal.app/models/111828?token=049d761e16514deb8c91d393fecb6104



Section Summary

None of the factors discussed can conclusively decide whether an endowment is right for a particular charity. However, evaluating the charity's context in line with each facto can help identify 1) disqualifying factors (e.g., charities performing humanitarian interventions with unpredictable spending), 2) factors which make endowment funding worth exploring in-depth.

To illustrate this more clearly, here are two stylized examples of charities. **Charity A is a very good fit for an endowment, while Charity B should not raise an endowment.**

Charity A (fit for endowment):

This charity provides Vitamin A supplementation (VAS), a program critical for child health in the regions in which it works. Historically, VAS coverage has suffered from inconsistent funding, leading to incomplete treatments. The charity currently spends 15% of its funds on fundraising from small, individual donors. This takes substantial staff time, which would be better spent elsewhere.

A high net worth individual has expressed interest in contributing to an endowment fund that would cover the VAS program permanently in some of the regions where the charity currently operates.

Charity B (not a fit for endowment):

This charity provides aid after humanitarian disasters, such as hurricanes and flooding. It tends to receive sufficient support from donors and government agencies in the aftermath of disasters to conduct its aid effectively. The charity's donors are exceptionally well-informed of its efficacy, so future funding mostly relies on successful implementation of its past humanitarian aid.

The charity would have to raise an endowment by diverting donations from small donors into a quasi-endowment structure, which would be taken out of necessary funds to assist in emergencies, and ultimately increase its fundraising costs.

5. Steps to implementing an endowment

Here, we provide a brief outline of the steps to building an endowment, alongside recommendations for further in-depth reading.

Step 1: Establish a plan and purpose for the endowment.
Step 2: Raise initial funds.
Step 3: Manage and grow the endowment.

Step 1: Establish a plan and purpose for the endowment.

The endowment-building process often starts with a series of questions:

How much should be raised for the endowment, and how should it be raised?

How much of the endowment should be distributed and when?

How should the endowment be managed?

Who should oversee the process?

What legal requirements need to be considered?

These questions concern two main areas: (1) the specifics of how the endowment should look like and (2) the administrative infrastructure to facilitate the building process. To deal with the former, Diana Newman, an experienced charity consultant, recommends in her book, 'Building an endowment right from the start', to issue a series of documents to specify the details of the endowment-building process.

The first of these should be **a written report specifying the reasons for building an endowment**. Creating this document is not only useful to establish whether there is enough reason for the organization to build an endowment but can also function as the basis for an endowment-specific fundraising program.

After this, Newman recommends letting the board approve **a resolution to commit to the endowment-building process**. By definition, building an endowment involves committing funds without seeing immediate results which could lead to conflicts among board members. To deal with this issue, it is helpful to vote on a binding resolution in advance to either avoid future conflicts or to choose not to build an endowment if there is not enough support among board members.

Lastly, to clarify the specifics of the building process, Newman recommends bringing together everyone involved and affected by the endowment (for instance, board and staff members, major donors, constituents, and community members) to work out **a roadmap specifying next steps and important milestones** for the endowment. This document can also be used to answer questions in the second area, i.e., the administrative infrastructure necessary for building an endowment. For smaller organizations, one member of the fundraising team could spend one day a week on starting the endowment.

Additionally, Newman emphasizes the importance of **deciding who is responsible for overseeing the process** and assessing whether agreed-upon milestones are achieved. Depending on the size and the structure of the organization, this could either involve establishing an endowment committee or the endowment matters could be added to the responsibilities of another pre-existing committee (like the executive committee or the fundraising committee).

Step 2: Raise initial funds.

With these documents and structures in place, the organization is ready for raising the first funds for the endowment. In the long run, the endowment should be an integral part of the organization's funding program. This could include separate campaigns for the endowment, integrating endowment fundraising into other projects, and redirecting unrestricted funds to the endowment. To get started, Newman suggests two possible strategies to initiate the endowment:

1. Asking for donations specifically to invest in the endowment

This could include developing a campaign that demonstrates the organization's need for an endowment, having 1-to-1 meetings with potential donors, or simply issuing a statement about the endowment in a regular newsletter by the organization. If contributors determine beforehand that the donated assets are intended to be permanently held by the organization, these constitute part of the "permanent endowment" and are classified as permanently restricted assets.

2. Setting aside funds from other fundraising streams

In this case, the board has to actively put money aside for the endowment that could also be spent differently. Here, the pre-commitment to the endowment is useful – previously agreed-upon goals and a general commitment to building an endowment help convince the board not to spend money right away. Funds acquired this way are called "quasi-endowments" and are classified as unrestricted assets.

Step 3: Manage and grow the endowment.

After an endowment program is written, a roadmap is agreed upon, the fundraising program for the endowment is in place, and the first funds for the endowment are available, a structure is needed for managing the endowment. There are different strategies that can be pursued, each with its own advantages and disadvantages. This section presents possible ways to manage and monitor an endowment, including for which organizations each strategy could be suitable.

Who is in charge of investment decisions?

There are several viable options:

1. Self-managing the endowment

Whether this strategy is successful is subject to the experience and ability of staff members and directors. Depending on the administrative structures and size of the organization, there are different ways to organize the management of an endowment within the organization:

- By establishing an investment committee (usually appropriate for larger organizations)
- By assigning responsibilities to one staff member who reports to the board of directors (in larger organizations someone could be hired for this or it added to the responsibilities of a development officer)
- By directly involving the board in investment decisions (as opposed to just monitoring them); usually appropriate for smaller organizations)

2. Hiring a professional manager

Another possibility is to assign the management of the endowment to a professional investment manager. There are several important considerations when choosing the right manager:

1) Does the investment manager have experience working with similar clients i.e., charities of a similar size and purpose? How have their endowments performed in the past?

This helps the investment manager understand the needs of the organization, simplify cooperation, and indicate whether they can be trusted with managing this endowment successfully.

2) How expensive are the services of the investment manager?

Usually, the fees for letting an endowment lie at about 1% of the returns, although these can vary. These fees should also be compared to how expensive it would be to pay someone within the organization to manage the endowment.

3) Does the manager offer socially responsible investment?

This could not only be important for donors that do not want their funds invested in bad causes, but also impact the cost-effectiveness of the organization.

3. Cooperating with local community foundations:

For small charities, a third option is to turn to local organizations that pool donations into collaborative investments, often with the stated purpose to contribute to social improvements of their region (so called local community foundations). Since endowments usually perform considerably better when they are large, this might be an especially cost-effective option for charities that do not expect to raise large endowments.

After deciding who makes investment decisions, **a further central question is whether the assets should be managed actively or passively**. There is no general consensus on which is better, and both options present advantages and disadvantages.

On one hand, proponents of passive management often point to efficient market theory, i.e. the view that since stock prices instantaneously react to all publicly available information, it is extremely difficult to systematically outperform passive management, in large part due to the low management fees under passive investments. In contrast, empirical findings suggest that, especially in some asset groups, active management can significantly outperform passive investment. To complicate the issue, whether active management is useful also depends on the size of the endowment. More sizable endowments appear to benefit more from active management than smaller endowments.

Consequently, small charities in particular should consider passive investment while also saving managing fees. A further option is to partly manage the endowment actively while investing most assets passively in ETFs or index funds.

5. Further readings and references

The following are helpful sources to more comprehensively understand the endowment building process, and are summarized in Section 4.

Useful short articles for getting an overview are:

1. “Building an Endowment: Is it Right for Your Organization?” (4 pages)

This short article describes the process of starting an endowment by dividing it into four stages (accessible here).

2. “Five steps to starting an endowment: even smaller nonprofits can“ by Scott Stewart

This article, similar to the first, summarizes the necessary steps to start an endowment. It also touches on the permanently incorporating the endowment into fundraising efforts as part of an “endowment program.”

Introductory books with more detail:

3. “Building an endowment right from the start” by Diana Newman (120 pages)

Newman is a charity consultant with several years of experience in helping organizations establish and manage an endowment. Her easily readable book summarizes the main points in the process. In contrast to the articles, she goes into more detail for each step, including practical advice and examples (e.g., example board resolutions etc.).

4. “Building Your Endowment” by Edward Schumacher (112 pages)

Like Newman, Schumacher comprehensively summarizes main points including specific advice about how to formulate the endowment building program. Although it is slightly shorter than Newman’s book, it might be useful as it focuses on different points, especially how to include the endowment in the fundraising program and how to approach potential endowment donors.

5. ”The Time for Endowment Building is Now – Why and How to Secure Your Organisation’s Future“ by Deborah Kaplam Polivy (150 pages)

This book might be interesting as it not only summarizes what is generally needed to build an endowment, but also analyzes it by using the LIFE & LEGACY Program of the Harold Grinspoon Foundation as a case study. This gives the reader a real-life example to compare with, including planning guides, partnership agreements, proposals, letters etc.

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