From Grantmaker to Leader

Emerging Strategies for Twenty-First Century Foundations

Edited by
Frank L. Ellsworth
and Joe Lumarda

JOHN WILEY & SONS, INC.

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About the Editors

Frank L. Ellsworth joined The Capital Group Companies in January 1997 where he works primarily with Capital Research and Management Company (CRMC) and Capital Guardian Trust Company (CGTC). At CRMC he oversees and coordinates CRMC's various programs and services to endowments, foundations, and other non-profit institutions. He is President and CEO of Endowments, a series of mutual funds managed by CRMC that are offered exclusively to non-profits. The American Funds Group, managed by CRMC is the third largest mutual fund complex in the United States. CRMC and its affiliates manage assets in excess of $350 billion.

Prior to joining the Capital Group, Dr. Ellsworth spent his entire career in higher education. Born and raised in the college town of Wooster, Ohio he received his A.B. *cum laude* from Adelbert College, Case Western Reserve University. He received Masters degrees from The Pennsylvania State University and Columbia University in the City of New York. He was awarded his Ph.D. from the University of Chicago. He recently was awarded the honorary degree of Doctor of Laws from Pepperdine University.

For nearly twenty-five years he combined teaching and administration at Penn State, Columbia University, and Sarah Lawrence College. For nine years at The University of Chicago he served as a dean in its law school and taught the "Great Books" course in the College. In 1979 he was hired as President of Pitzer College, the youngest President in the history of the Claremont Colleges. He is an authority in intercultural and interdisciplinary education. After twelve years in the presidency, he became President of the Independent Colleges of Southern California.

He is also active in many community affairs and serves on the Boards of Trustees of the Japanese American National Museum, Southwestern University School of Law, Pitzer College and the

Japanese Foundation for International Education. He is the Chairman of the Board of The American School of International Training in Seattle, the National Center for the Preservation of Democracy, and Global Partners in Canada. He is a member of YPO (Young Presidents' Organization).

His daughter, Kirstin, is a graduate student at Indiana University. Dr. Ellsworth currently resides in Pasadena.

Joe Lumarda has held the position of Executive Vice President for External Affairs at the California Community Foundation for the past five years. He chairs the Foundation's management team and oversees its asset development program and donor-advised fund grant making. He started at the Foundation in 1990 as a program officer in the area of children and youth, was appointed Vice President for Development in 1991, and was named Executive Vice President for External Affairs in 1997.

Joe is a board member of the Saint Joseph Health System Foundation, Southern California Association for Philanthropy, Coro Southern California, the Peter F. Drucker Graduate School of Management, and the Council on Foundation's Community Foundation Leadership Team. He is also a board member of Endowments, Inc., a mutual fund company serving nonprofit organizations nationwide.

Before coming to the Foundation, Joe served three years as an officer in the U.S. Navy, flying in the tactical navigator seat of the P-3 Orion aircraft. Prior to the Navy, he was Associate Director of Government Relations and Campaign Associate for the United Way of Orange County. He is a graduate of the Coro Foundation Orange County Public Affairs Leadership Program.

Joe received his bachelor's degree in philosophy at Saint John's Seminary College in Camarillo, California. In 1999 he attained an executive MBA at the Peter F. Drucker Graduate Management Center at the Claremont Graduate University. In 2000 Joe was named a German Marshall Fund Community Foundation Fellow. This fellowship sent him to Poland, where he studied and consulted with that country's growing community foundation movement.

Joe currently resides in Pasadena with his wife Denise and two sons, Malone and Elias.

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Corpus Diem

You and Your Foundation: A Plea to "Seize the Day" before it Seizes All of Us.

How should you handle your foundation grantmaking if your investments produce a higher rate of return than you anticipated, thereby boosting your corpus to significantly higher levels? Naturally, you are likely to feel proud, even relieved, but this is the time for strong strategy rather than braggadocio. Let us assume that you favor a strategy of taking a reasonable risk on an ambitious project or two that promises to have significant positive impact on a community, group, or cause. Or perhaps, if being a strong advocate of the great philanthropist Andrew Carnegie, you concentrate on one or two major goals by emulating how Carnegie endeavored to improve the country's literacy through the building of libraries. Granted, Carnegie controlled his foundation, but it was his willingness to focus and spend money on a strong conviction that was responsible for his being revered as a champion, even a half century later.

Unfortunately, too many foundations today carry reputations more for their massive corpus rather than for their abilities to make major, positive impacts on society. Granted, it is a lot tougher for a leader who is more of a public servant or is seriously constricted by rigid rules emanating from a deceased founder of the foundation than it is for the "big boss" who controls the pot of gold; however, a strategy such as Carnegie's for a reasonable portion of corpus (therefore not held to small percentages) presents greater opportunities for creative work than making scores of small commitments that might become merely mediocre impacts at best.

Okay, Carnegie's fortune was the equivalent of multi billions of dollars today, but here is an example of a more common $10 million foundation that broke ground in 1977 with a plan to give money to nonprofit organizations at the (typical) 5 percent of their $10 million corpus, or $500,000 per year. Investing two thirds in common stocks and one third in bonds set their expectations at a 9.2 percent total annual return (a conservative long-term historical average) assuming a 5 percent fixed-income yield. This allowed the foundation to anticipate a corpus by the twentieth year of around $17 million, but which in reality benefited dramatically from unexpectedly stronger stock returns that grew the principal instead to a whopping $44 million!

Naturally, this was cause for some challenging dialogue within the foundation, where the powers that be decided to continue with their 5 percent annual grant making. Here you had assets that had risen by $37 million, yet annual grant making (*the foundation's reason for existence*) rose by only $350,000. Was that generous and effective? Should not the entity have thought bigger? They could have easily looked for a more powerful, "dream investment" and still earmarked, say, a $13.5 million reservoir to fund grants for a "rainy day" environment in which some additional grants would look mighty important (something that less fortunate nonprofits should be able to put to exceptionally good use).

Why do so many shy away from giving while they have so much? To begin with, many people simply procrastinate and/or find multiple excuses about why they are not doing more philanthropically. And many more simply ignore the goals for their special dreams and suddenly realize late into their lifetimes that they lack the energy to realize them. Others simply worry that their finances will fade away and leave them headed for poverty. Or, just the opposite, some prosperous people think that by compounding their annual returns at a very high rate, they will help society most by postponing their giving. Instead, they focus on making even more money—the bulk of which they plan to donate to charity upon their deaths.

I disagree with this, "give much later" strategy, simply because I believe strongly that it is far more effective and rewarding for the wealthy to make the bulk of their charitable donations during the prime of life rather than concentrating on making yet more money for the good of philanthropy. Most important, however, there is a hidden yet strong and compelling reason for so many of us to proceed more quickly with our intelligent grants, due to the following thesis that makes important arithmetic sense:

> Societal ills generally increase at an exponentially greater rate than does return on capital.

Even exceptional capital returns can rarely keep pace with societal problems, which if ignored, cascade through the generations, as more and more disadvantaged descendants come into the world. Even grandiose plans for a future foundation, while well intentioned, have less long-term impact on empty tummies and uneducated minds than far less money invested in charity now. Think of the many youngsters whose major problems stem from neglect, abuse, or the lack of a supportive home life. The probability of a "cure" increases dramatically the earlier they are exposed to positive environments. If not, these troubled youths often become troubled adults, who are ill equipped to provide their own children with a healthy environment, who are in turn ill equipped to help their children, as the cycle continues and expands exponentially, even with normal population growth. So, acting now versus later is a right and prudent thing, as it is a protective effort. Hence, it is important that more philanthropists think in terms of "effects on generations" realizing what is missed if plans are made too far out. We should constantly remind ourselves that our country (and others) cannot afford to neglect those who desperately need near-term, even immediate, attention.

As a philanthropic research organization committed to educating people on how to budget for charity, my firm, NewTithing Group (*http://www.newtithing.org*), estimates that households with adjusted gross incomes of $200,000 or more and assets of $500,000 or more (excluding personal homes and possessions) can comfortably afford to give substantially more to charity, including to their private foundations. In fact, our IRS-based research conservatively estimates that average households with adjusted gross incomes of $1 million or more can indeed give comfortably nearly ten times more each year to charity than they have been giving.

In planning ahead, you should consider what your actuarial lifetime is likely to be; whom you picture running your foundation; and, whether your chosen non-profit recipients will understand the urgencies that "societal ills" demand. By making significant charitable investments now through your foundation, you will be deciding what is most important—whether your legacies and others grow up in an unhealthy, unsafe, and tentative future—or in a society that has a clean, safe, and more fulfilled environment for most everyone. Making substantial charitable investments earlier rather than later can stem many "societal ills" before they have a chance to increase at an exponentially greater rate than typical returns on capital. Thus, investing more of your foundation corpus now embodies the ancient Latin adage, "Carpe Diem," "Seize the Day". . . . before it seizes all of us. Or as foundations might think of it, "Corpus Diem."

CLAUDE ROSENBERG

NewTithing Group
San Francisco
August 15, 2002

Acknowledgments

First, we want to acknowledge our authors. The reader glancing through the table of contents will see that we are fortunate to have the "best of the best" to present their ideas and strategies. Frank Ellsworth wishes to acknowledge the help of his assistant, Christine Imaoka Curry, and the support of Capital Research and Management Company, The Capital Group Companies. Joe Lumarda wishes to acknowledge the support of the California Community Foundation, in particular its president, Jack Shakely. Additionally, Joe wishes to convey his gratitude to fellow staff members at the community foundation who shared their wisdom, discriminating eye, forbearance, and good humor, in particular, Peter Dunn, Robin Kramer, Catherine Stringer, Judy Spiegel, Amy Fackelmann, and Sylvia Moraton. And, finally, a very special thanks to Joe's wife Denise and two boys Malone and Elias for their patience, care, and smiles even when dad was pounding on the computer or dragging in late.

Introduction

Remarkable changes characterized American foundations in the twentieth century. The history of that time reveals the profound impact foundations have had on our society. The history is not without controversy. The issues and themes are diverse and broad ranging. The impact of the sheer growth of the number of foundations and the substantive increase of assets remains undefined and replete with issues. The evolution of conflicting views of the relationship between public policy and attitudes toward social change could fill volumes. The maturation of the control and governance of foundations from founder to family to professionals to institutional has been bumpy and not without consequences. The constant arrival of new foundations, often entrepreneurial in nature, has provided healthy tension between classical and innovative—and occasionally radical—views of the role and influence of foundations in our society. The strong and rapid emergence of community foundations has brought growing strength to building permanent assets, strengthening the relations between philanthropic individuals and families and organizations within their communities. As community foundations strengthen the essential fabric of their communities helping all organizations gain financial foothold, they find themselves at times in conflict with commercial gift funds whose transactional nature between the donor and the organization stimulates philanthropy in a different fashion.

The Tax Reform Act of 1969 provided a huge impetus regarding the shape of philanthropy, providing new structures for the immense transfer of wealth, strengthening organizations and spawning a flood of family foundations. The specialization of foundations focusing on issues and needs has become commonplace. Themes including the reform of public education, medical education, the health sciences, AIDS, libraries, the environment, social services, the arts, and public policy, and many others are now integral to foundation life and the philanthropic dialogue. We are fortunate to have excellent histories to give us perspective on the century past, beginning with Merle Curti and Roderick Nash's *Philanthropy in the Shaping of American Education,* and continuing through the classic work of Barry Karl and Stanley Katz, "The American Private Philanthropic Foundation and the Public Sphere," and other Karl and Katz publications. For readers interested in pursing the wealth of literature available, an outstanding bibliography has been compiled by Susan Kastan, which appears in *Philanthropic Foundations: New Scholarship New Possibilities,* edited by Ellen Condliffe Lagemann.[1]

This book looks to the twenty-first century. The conversations in philanthropy today continue those from the last century while emphasizing emerging themes and issues, including the transfer of wealth, legislative concerns, IRS audits, and the role of foundations in public policy issues previously ignored, like campaign spending, accountability, planned giving, assessment of the effectiveness of giving, social responsible investment and social return on investment. Time will tell whether these issues weather the realities of time and place and translate into major ones with significant consequence for our communities. A great deal has been written on the grantmakers, although the time is here for an analysis of the commercial gift funds. And much continues to be said about the motivation of philanthropy. Mark Dowie, in *American Foundations: An Investigative History,* suggests that organized philanthropy must become more democratic, and that we are at the beginning of a fundamental shift with foundations becoming more transparent.[2] Guidestar is a much-welcomed vehicle that allows the public more scrutiny of the previously undisclosed operations for most foundations. Conversations continue about how influential and powerful foundations really are. Certainly, the assets and gifts of foundations pale in comparison with individual giving or, indeed, the trillions of dollars in government hands. Do they cater to the right? To the left? Numerous books and articles address these issues. Fast emerging into the dialogue on foundations are global foundations. The extensive bibliography of books on foundations covering these and other topics reveals that the common genre is one of narration and description, usually focusing on one aspect or theme. The reader is left with good and often interesting information but rarely with any sense of the practical implications of the information.

The purpose of this book is to move beyond information gathering and present strategies for leadership. Our audience is the practitioner: the trustee, the chief executive officer, the chief financial officer, members of the investment committee, the information and publication relations staff, the program officer, and committee members. Our audience is the people who work with foundations in a variety of roles. Our distinguished authors in this book come to the task of writing with extraordinary experiences and keen analytical abilities. But their assignment was to move to the practical. They are writing for the individual who not only wants to understand an issue, but also wants and needs to gain insight on how to deal with the issues and create strategies, whether they are of leadership or management in nature, or both. This book presents topics and issues that reflect the unspoken and spoken language of the world of foundations today with an eye toward helping the reader address them effectively. Our intent is to be pragmatic and, at times, provocative, as we attempt to provide a comprehensive and "user-friendly" guidebook for Strategy and Leadership.

The book organizes this practicum of information around three themes. We begin with Section One, "From Carnegie to Gates: The Changing Faces and Needs of Philanthropy." First, we look at family philanthropy and foundations, followed by the promise of community foundations. Given the role of the New Economy at the turn of the last century, we then look at the carryover of the impact of that period today.

Continuing themes and history from the last century, the second section addresses "The Foundation's New Reach: The Emerging Role of Leader, Communicator, and Facilitator of Change." The chapters in this section examine the Meta foundation as venture philanthropy takes a stronghold. How can foundations convey the new wealth and purpose through their messages? Is the message of a foundation important, and, if so, how can the message penetrate the media and other communication venues? Finally, we look at a classic example of how one foundation has successfully addressed public policy issues.

The third section addresses a fundamental fiduciary question which influences crucial management and leadership issues: How Do boards of directors direct foundations? What should the foundation board of the twenty-first century look like? Responsibilities? Backgrounds? What is the role of planning, and how is this accomplished through board policies and interaction with the professional staff? Who else needs to be involved? Why?

Are we in a new era where the very nature of foundations will change as a result of the projected huge transfer of wealth? Will foundations emerge as the twenty-first century passes with a stronger, more pervasive role in our societies around the world? Some would argue not, claiming that the role and influence of foundations will always at best be elitist and selective. Peter Frumkin, Harvard Professor of Public Policy, believes we are at the beginning of significant change as a new generation of visionary philanthropists ". . . signal that donors of large amounts are beginning to assert themselves as never before. This new period of personal giving is challenging us to think differently about the meaning and rationale for philanthropy." Although the editors might like to believe that Frumkin is right in his belief that "we should encourage a broad and active market of competing visions of the common good, while celebrating the huge wave of unfiltered pluralism that donor driven philanthropy is beginning to unleash on American Society," neither of us have seen in our experiences immersed in foundation management and leadership, yet more than a mild ripple in this direction.[3] However, we do subscribe to the belief about the mission of foundations articulated by Adele Simmons, Rebecca Rimel, and Peter Goldmark, whose leadership with the MacArthur, Pew, and Rockefeller Foundations give them credibility in stating:

> America's independent foundations—their best—can serve four distinct ways: First they can identify nascent dangers

> and alert the public before such dangers reach a grave level. Second, foundations can spark initiatives to respond to these dangers. This work usually entails an examination of the root causes of problems rather than their symptoms. Third, foundations can support those who are not well represented in the mainstream of political and social discourse, ensuring that their voices are better heard. Finally, foundations can bring together the energies and talents of many diverse—sometimes adversarial—groups to build new solutions to problems.[4]

Our readers will have differing views of the present and future roles for foundations. That is understandable and the way it should be. We hope, however, that these chapters will be useful for all of us playing our respective roles in management and leadership for The Foundation of the Century.

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JOE LUMARDA
The California Community Foundation
August 15, 2002
Los Angeles, California

NOTES

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Condliffe Lagemann. Bloomington, IN: Indiana University Press, 1999, pp. 377–403.

2. Mark Dowie, *American Foundations: An Investigative History.* Cambridge, MA: MIT Press, 2001.
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Section One

From Carnegie to Gates: The Changing Faces and Needs of Philanthropy

CHAPTER 1

Family Philanthropy in Twenty-First Century America

by Virginia M. Esposito and Joseph Foote

PERSPECTIVES

Philanthropy in many ways starts with family. It extends from familial ties to community connections to wider society. It is often said that philanthropy is a learned behavior. The habits of the heart are almost always taught at home.

Family foundations make up almost 80 percent of all the foundations in the country. More often than not, the dynamics around the family business boardroom and the Thanksgiving table are mirrored in the formal representation of the family's philanthropy, the foundation. The individuals around those tables change, yet the vision of the founder endures. The manner in which future board members honor this vision is an ever-present issue.

No one is better suited to address this topic than Virginia Esposito and Joseph Foote. Virginia is the founding president of the National Center on Family Philanthropy. The National Center was founded to encourage families and individuals to create and sustain their philanthropic missions. A 501(c)(3) nonprofit organization, it was established in 1997 by a group of family philanthropists. It is the only national resource center that focuses solely on matters of importance to families engaged in philanthropy and their effective giving. Joe is a professional writer and editor who specializes in philanthropy and social policy.

The bedrock of American philanthropy today is the family. Families create the most giving vehicles and provide the most funding in formal philanthropy. They bring far more than money, however: they bring family resources, energy, passion, and compassion in measures that constantly refresh the field and remind us all of what philanthropy is truly about.

In sheer numbers, family foundations dwarf every other category of foundation. In aggregate assets, grants awarded, and numbers of nonprofit organizations supported, family philanthropy surpasses corporate, community, and operating foundations combined.

The Internal Revenue Service estimates that some 60,000 private foundations exist in the United States; we estimate that more than two-thirds (35,000 to 40,000) have family involvement at some level.[1] Furthermore, we estimate that most of the 30,000 private foundations created over the past 20 years likely have family involvement. Many of these are still relatively small (less than $1 million in assets), but they often grow substantially over time and particularly on the death of the founder. At least several hundred family foundations have assets of $100 million or more, and at least 20 have assets of $1 billion or more.

The story of family philanthropy begins in the earliest years of American history, when families formed the fabric of communities and family philanthropy reached into every corner of American life. From rural villages to the growing cities of the new nation, family philanthropy took shape wherever families lived, worked, and cared about their neighbors and their communities. This remarkable phenomenon became so enmeshed in American life that it hardly warranted notice.

Rather, in the past century, American philanthropy became marked—and largely defined—by the presence of a few great families with names linked to huge fortunes made in the building of American industry. Although family philanthropy involves far more than foundations, today many Americans think of these families—Ford, Rockefeller, and now Packard and Gates—as much for the foundation bearing their name as for their other works. As well known as they are to the public, however, these families represent only a tiny fraction of the number of families who support foundations and other formal giving vehicles.

As the nation enters the twenty-first century, family foundations are attracting much greater attention as one of the most powerful forces in American philanthropy. Family foundations account for much of the stability, tradition, and financial strength of grantmaking in this country. At the same time, these foundations accounts for much of the dynamic of change, the refreshment of values, and the injection of new and energetic leadership into the field of philanthropy.

Yet little attention has been paid to family philanthropy in general or to the unique nature of family foundations in particular. Myth and reality about family foundations diverge. When standard texts describe the typical family foundation, they often portray a group of wealthy but forever disagreeing people who govern erratically, manage foundation affairs haphazardly, and are amateurish in their grantmaking.

Most families in philanthropy are truly two things—they are families, with all their strengths and weakness, and they are deeply committed and passionate philanthropists. The motivation of families to engage in philanthropy is often the desire to "give back" and to continue or initiate a family tradition of formal giving. Many families find guidance in their spiritual faith.[2] Family philanthropy often involves endowing a foundation, but it also includes volunteer service, lending the family name to worthy causes, personal charitable giving, providing community support through a family business, and other expressions. Society benefits from the compassion and commitment of family philanthropy. The family receives something as well: the privilege of giving back and the joy and sense of accomplishment that attend it.

This overview makes family philanthropy sound rosy and easy. It is not, as any family in the field will attest. The founding, governance, and management of a family foundation come with an extra dimension—it's not only philanthropy but also *family* philanthropy. The founder (often a founding couple) usually considers questions such as: How do we provide for our children as we contemplate committing large sums of money to an endowment? Who among our family members, friends, and trusted advisors should be invited to sit on the board? How long should our foundation exist? How tightly should we bind the foundation to a specific mission, or should we empower future boards to modify the mission? What role do we foresee for future generations of the family in assuming responsibility to govern and manage the foundation?

Management of a family foundation is particularly fascinating. Most family foundations rely on family members to govern, manage, and administer. Typically, all board members are family, at least at startup. The founding couple sorts through grant applications and prepares a list for board review. A daughter with an MBA serves as executive director, and a nephew who is a CPA handles the books. A lawyer cousin acts as general counsel; children too young for board duty sit on an advisory committee and suggest grants in areas of concern to them. The enterprise is truly a family undertaking.

FAMILY PHILANTHROPY IS UNIQUE

Family philanthropy consists of any formal charitable activity that a family (however it defines itself) may undertake. Family philanthropy embraces weekly giving at a religious institution, year-end contributions to a public charity, or giving through a formal charitable vehicle. Before turning to the subject of this chapter, which is family foundations, it is useful to keep in mind that many and perhaps most family foundation founders employ various philanthropic vehicles in addition to their foundation.

The Hunt family of Pittsburgh, Pennsylvania, for example, demonstrates how different giving vehicles can be used for different members and generations of a family, and for different purposes. At the hub of the family's philanthropy is the Roy A. Hunt Foundation (2001 assets: $85 million), formed in 1950, located in Pittsburgh, and governed by a board consisting entirely of family members: Richard M. Hunt and his brother, three of their children, and eight nieces and nephews. They employ an executive director (who is a family member) and a program officer (who is not a family member); the family board members oversee grantmaking in education, the arts, religion, international relations, medicine, and large grants in three areas: community development, youth violence, and protection of the environment.

Richard Hunt, who is The University Marshal of Harvard University, and his wife, Priscilla Stevenson Hunt, also make use of other philanthropic vehicles. They operate their own foundation, the Miramar Fund, named after their honeymoon *albergo* in Italy; they formed this family foundation to support educational projects. Miramar is small today, but is expected to grow.

Richard and Priscilla have also set up a charitable lead annuity trust (CLAT), named Cup Clat (so named because "our cup runneth over," Richard says), which is designed to support what the couple hopes are worthy causes in the world. "Its mission is to support selected projects of our three grown children who have become astute and realistic philanthropists," Richard says. He and Priscilla channel $10,000 of the revenue to charities annually, and their three children can direct an additional $10,000 each to charities of their choice.

Two years ago, the Hunts set up the Magic Mountain Fund (named for Richard's favorite German novel, by Thomas Mann), a donor-advised fund in the Scudder Charitable Fund in New York. Starting with a corpus of $1 million, Magic Mountain now holds $2 million. The Hunts make recommendations on charitable distributions of the income and principal for grants in health care and social service. This fund provides solid growth of the corpus, flexibility in changing grantees, and a steady flow of family charitable gifts to established nonprofit organizations. Management fees are modest, Scudder performs all due diligence on prospective grantees, Scudder also satisfies all the required tax reporting obligations, and the family finds the arrangement virtually hassle-free.

"We give these highly personal and eccentric names to the funds in order to keep them straight and to be able to refer to them in a quick way," Richard Hunt observes.

Richard and Priscilla have also established two charitable remainder unitrusts that provide income to members of the family