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Planned Gifts, Endowments, and Quasi-endowments

There was a recent posting on a listserve that I follow that I found pretty interesting. The original post was as follows:

> *To all:*
>
> *We just received a CRT remainder distribution that was specifically designated to one of our colleges without any further restriction. Our board-approved policy states a preference for placing undesignated bequests and life income distributions into quasi-unrestricted endowment (i.e., in any way we see best to use it—spend some, endow some, spend it all, or endow it all), but according to our general counsel, our accountants (at a well-known national firm) tell us that it is contrary to the new FASB and General Accounting Practices for a charity to endow or otherwise place restrictions on an unrestricted gift without explicit donor instructions to do so. If this is true, it would undermine our efforts to promote gifts with lasting impact and enduring value, not to mention requiring an immediate redraft of our gift acceptance policy.*
>
> *Any accountants or FASB experts out there who can shed light on this for us?*
>
> *Peter*

After a day or two of silence (other than the responses that said, "Gee, I don't know—tell me what you find out"), one of my clients told me that I had to respond. So I did, as follows:

> *Peter:*
>
> *Everyone is right (when was the last time you heard a lawyer say that?). Subject to a few caveats here and there:*
>
> - *A true, legally binding endowment restriction can only be imposed by the donor—the board cannot impose a binding endowment restriction on unrestricted funds.*
> - *Accordingly, the auditors won't report these funds as "permanently restricted," as that fund balance category is for legally binding endowed funds.*
> - *A board can always decide to treat unrestricted funds as endowment—these funds are called 'quasi-endowment' or 'board designated endowment' or 'funds functioning as endowment'. That is what your policy says, so it's right, too.*
> - *However, the board can always un-endow quasi-endowed funds—just as they unilaterally decided to impose a spending restriction, they can decide to change it. The*

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auditors will thus classify them as unrestricted on the financials.

- *Finally, you are right—it's important for an organization to be able to build quasi-endowment funds. Some of my better-managed clients have both an endowment policy (for the true, legally binding endowed funds) and a quasi-endowment policy (which looks pretty much like the first one, but recognizes that the funds are not subject to a binding spending restriction).*

Hope this helps…

Erik

A few days later, another participant offered a response that included some sage advice for development folks:

Peter

[F]und agreements [i.e., gift agreements with the donor] are absolutely essential in our planned giving efforts. When we know in advance of an estate gift, we make every effort to engage the donor in a conversation about the use of funds, and when endowment is desired (as is usually the case) we try very hard to get a signed fund agreement. This has benefits apart from directing the use of funds: we are able to have a conversation that often creates a much deeper relationship, the donor's signed agreement becomes a tangible expression of generosity he or she may never see at work, and it is often the least threatening way to document a gift. We explain the need for a fund agreement every time someone contacts us for will language, and we urge attorneys to specify in the will or trust that the gift is "for the John Doe Fund," which means we have an opportunity to head off unacceptable restrictions and/or tamp down unrealistic expectations.

John

Peter's response to John was as follows:

John,

I agree with all that you say, especially with respect to the timely conversations we should have with our donors. In this case, the donor was a local music teacher who was only known to us because of the $100 gifts she would make from time to time to our music school's annual fund. She had never revealed the fact that she and her husband had included us in their CRT when it was prepared, or any time after.

Since the music school is a part of the University, the designation to "The [Music] School of the University" is considered, by the accountants, to be a gift specifically restricted by the donor to the [Music] School, and as such, their recommendation is to not even place the proceeds into quasi-endowment for the [Music] School, but to use the money where it is currently needed at the [Music] School.

No institution is going to complain about receiving current use funding from bequests, trusts, and other distributions, and the donor didn't see the need to tell us about her plans when she had the chance, but it should serve as a good reminder to have those conversations about intent with our donors whenever possible, and at the same time make sure that our gift acceptance policies are designed to foster the legacy we're always asking people to leave to us.

Thanks for your thoughtful response,

Peter