BUILDING A *Legacy*

An Endowment Policy Handbook

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United Church Funds

Established in 1909 to administer the Pilgrim Memorial Fund for the benefit of retired pastors, United Church Funds has developed into a unique ministry that puts the power of the financial markets to work for the local churches and organizations of the United Church of Christ.

United Church Funds (UCF) offers a family of eleven professionally managed, well-diversified and socially responsible investment funds to over 1,000 churches, conferences, associations and other ministries of the United Church of Christ. At present, UCF manages over half a billion dollars in assets — from small church reserve accounts to some of the denomination's historic endowments — along with the assets invested in planned gifts through the UCC's Financial Development office.

Investors in UCF's funds benefit from a range of advantages, including —

- A range of funds offering broad diversification to minimize risk
- Lower fees for active management by top managers using a range of styles
- A socially responsible portfolio and active shareholder engagement
- Continuous evaluation of manager performance to strengthen returns
- A not-for-profit structure that reduces costs

Investing with United Church Funds, churches and other UCC ministries enjoy solid performance, the best practices of modern portfolio management, and responsible portfolios that help to strengthen ministry.

Letter from the President

Endowments can prove a confusing topic for many. As the investment manager for both the historic endowments of the UCC and many of the newest programs created by contemporary church members, United Church Funds frequently fields questions and concerns about structure, investment, promotion, management and spending of endowments. So we've created this resource to appeal to both newcomers to the topic and veterans looking to strengthen their understanding and skills. We believe that the better prepared a church is to accept and manage long-term gifts, the greater the generosity that will be inspired among church members whose gifts will help strengthen and broaden ministry and impact local communities for decades.

To be well prepared for bequests and the happy surprise of unexpected gifts, every church — large or small — needs policies in place to ensure that when gifts do arrive, the church is prepared to manage them effectively to support its mission and ministry, its financial health and its future. A pre-established policy helps a church avoid unfortunate decisions and outright conflicts, and move forward quickly to put gifts to use — honoring both the donor and the church's ongoing ministry.

Of course, developing a well-considered endowment policy requires several months of preparation, discussion and collaboration within and among committees and the entire congregation. This handbook was created to assist churches in their policy development, and contains educational information and guidelines to consider. Supplemental materials and sample endowment policies can be downloaded from the United Church Funds website at www.unitedchurchfunds.org.

As always, the staff of United Church Funds stands ready to respond to questions and to assist your church as you seek to build an endowment that will support ministry for years to come.

Donald G. Hart

Donald G. Hart
President

The better prepared a church is to accept and manage long-term gifts, the greater the generosity that will be inspired among church members.

Defining Endowments

In the simplest terms, an endowment is like a permanent savings account: a pool of money that a church and its donors have set aside and invested for the really long term. Unlike a personal retirement account, however, an endowment is an institutional fund that anticipates no end date — a fund intended to be held in perpetuity, its return supporting ministry for generations.

Consider the justice ministries of the UCC. A number of present-day justice programs are funded by money first collected in 1839 by Congregationalists seeking to aid and defend the Amistad prisoners. Money that was not needed then created an endowment that remains an important source of funding today. Now that's long term!

The distinction between personal and institutional (church) funds influences the manner in which endowments are promoted, managed, invested and spent. Most endowments are funded by and built with bequests, direct gifts to the endowment from members, memorial and planned gifts like Charitable Gift Annuities and Charitable Trusts, and even by special capital campaigns. This pool of funds is then invested for the long-term — usually in stocks and bonds — so that the fund will grow in value as the years go by, giving the church a steady source of revenue that can be used for a variety of purposes.

An endowment is a permanent fund given to accomplish a specific purpose.

The Endowment Policy

A well-considered endowment policy is really a set of policies, all of which work together to support a church as it makes decisions about its assets. For the purposes of this handbook, an endowment policy will be assumed to include the following documents, each of which is important in its own right —

- **a gift acceptance policy**
  describing how and when gifts will be accepted or declined
- **an investment policy**
  guiding a church in its choice of investment instruments and management
- **a spending policy**
  determining how funds given and invested will be managed and used

Developing an endowment policy requires the involvement of a number of individuals who work together to create a policy that the congregation votes to accept. The process generally involves the following steps —

1. Prepare the way
2. Build and charge committees
3. Draft the policy components
4. Present the draft to the congregation
5. Refine the final document
6. Vote on the policy
7. Promote the endowment
8. Review the policy at regular intervals

Depending on the issues and discussion points that arise, a committee or congregation may need to work through a step more than once before the group is ready to move on. While the end product is important, the process itself can be a valuable experience for a congregation as it defines itself and its hopes for the future. Engaging a wide range of people at appropriate points in the policy development process not only ensures important transparency in transacting the business of the church, but also generates a sense of ownership and excitement that can lead to future gifts to the established endowment.

Good plans shape decisions. That's why good planning helps to make elusive dreams come true.

— **Lester R. Bittel** The Nine Master Keys of Management

INITIAL

Steps

Prepare The Way

While some members of the church and its leadership may be anxious to create an endowment policy, others may be uncertain about the value of an endowment at all. Some may have seen a church decline because it depended more on its endowment to keep the church going than on the effectiveness of its ministry. Others may be concerned about the stewardship implications of maintaining an endowment.

Before embarking on a policy development project, communicate with the congregation and engage people in the process.

- Hold a series of discussions — among committees, in Sunday School classes, and with the congregation as a whole — to establish the purpose of creating an endowment. Ensure everyone gets an opportunity to be heard and understands the terminology being used.
  - What is the congregation's mission?
  - How would an endowment benefit that mission?
  - What might the endowment allow the church to do that it cannot do now?
  - What issues will the church need to address and monitor if an endowment is created?

- Consider a Bible study, looking particularly at Jesus' teaching around money — both the warnings and the praise. Several passages, studied together, may be particularly helpful —
  - the rich young ruler (Mark 10:17-31)
  - the builder of bigger barns (Luke 12:16-21)
  - the parable of the talents (Matthew 25:14-30)

- Think about the memorials, named funds, unrestricted and designated gifts — that have been serving as an informal endowment. How might these funds be rolled into a larger pool of resources?

- Review the current spending pattern for endowment-type funds. Does spending need to be adjusted to comply with current law for endowments? Do existing gifts offer a guide for sub-funds (ie, education, missions or youth) that might invite additional gifts to the overall endowment?

It is thrifty to prepare today for the wants of tomorrow.
— Aesop

Build & Charge Committees

Depending on the size of your congregation, policy development may be managed by a single committee, or divided among several committees that will draft the various policy components. Whether your church will be served by one committee or several, the same range of issues must be considered.

While financial and legal professionals can be helpful committee members, be sure each committee includes a range of perspectives and voices. If several committees are used, the tasks might be divided as follows —

- **Gift policy committee**
  to establish the types of gifts that will be encouraged, and the types that will be discouraged.

- **Investment policy committee**
  to select the types of vehicles in which endowment funds may be invested, and how the investments will be managed.

- **Spending policy committee**
  to determine how the proceeds from the endowment fund will be spent.

- **Endowment policy task force**
  One or two representatives from each committees might form a separate "task force" that meets regularly to review the direction each group is pursuing, to resolve issues or overlaps that have arisen, and to guide the overall process to ensure the goals and dreams of the wider congregation are represented. When the committees have completed their initial round of work, the task force might then be charged with consolidating all of the committees' work into an initial endowment policy for review.

Here's a bit of good news: in one form or another, endowments have been around since the Middle Ages, so many churches and organizations have already developed endowment policies which can be very helpful in guiding your own policy development.

For samples of language and policies, visit unitedchurchfunds.org

Outline of an Endowment Policy

As you begin to develop your policy, review policies established by other churches that share similar structures and goals, and incorporate those elements that seem particularly valuable. The following list outlines the basic elements of an endowment policy, although the various components maybe arranged differently. Use this list as a jumping-off point for your discussions and deliberations, keeping in mind that you want a policy "in perpetuity" — one, like the US Constitution, that can guide you through rotating leadership and changing times.

Preamble

- The church's mission statement
- The name of the endowment
- The endowment's general purposes and objectives

Definition of Terms

- General or Unrestricted
- Designated
- Temporarily Restricted
- Permanently Restricted
- Other terms

Gift Acceptance Policy

- Guidelines for acceptance and rejection of gifts
- Disposal of non-cash gifts
- Guidelines for donor restrictions and named gifts

Investment Policy

- Investment objectives
- Asset allocations and diversification
- Acceptable and non-acceptable investments
- Investment manager selection
- Results monitoring and measurement
- Socially responsible investing

Spending Policy

- How the amount to be distributed will be determined
- How distributions will be directed
- What limit will be placed on funds available for the general operating budget
- Conditions for "excessive" spending

Recordkeeping & Reporting
- Who will maintain records and what records will be kept
- How will the congregation be kept informed
- Financial controls and policies, including conflict of interest

Other Legal Issues
- Auditing the endowment
- Amending the policy
- Fiduciary responsibilities of managers, officers and committees
- Protection from liability

Endowment: Pro & Con

While the benefit of having policies in place can never be underestimated, not everyone agrees that endowments themselves benefit a church or organization. Let's take a look at some of the arguments put forward regarding endowments.

Arguments for endowments

Ministry is stronger & broader
An endowment can support expansion of existing ministries, fund special programs, and provide seed money for new or experimental efforts.

Emergencies are covered
While every church should maintain a regular reserve for emergencies, an endowment can sometimes mean the difference between calm and crisis.

We honor the past
An endowment permits the "cloud of witnesses" that supported the church during their lifetimes to continue to support the ministry they valued after they have passed on.

We can offer grants to other programs
Many churches seek ways to strengthen the community beyond their doors. Part of an endowment can be set aside to fund grants to organizations outside the church to broaden the church's outreach and impact.

We help ensure the future
Most people want the organizations they value to continue influencing the world for good, even after they're gone. An endowment can help a church develop a thriving ministry that will impact generations of Christians in the community.

Arguments against endowments

People may stop giving
Churches with endowments must constantly guard against reliance on endowment income to cover its basic operating expenses. Good spending policies and a consistent emphasis on stewardship help to ensure current giving at appropriate levels.

The church has too much money
An endowment can give potential donors the impression the church doesn't need their gifts. Pastors and church leaders must work to help congregants understand that giving is about our gratitude to God, and our need to give, not about the church's need for our money.

Churches shouldn't stockpile funds
Endowments reflect the desire of people to support the mission of their church even after they're gone. Many churches, universities and other institutions would not exist today but for the generosity of preceding generations. The challenge for a church is to use its endowment to keep expanding and advancing its ministry.

POLICY

Components

Preamble

Although this section may be the shortest, it may take the longest to develop. Drafting the preamble to an endowment policy gives a church a terrific opportunity for self-examination.

- **The mission of the church**
  Who do we say we are? Why do we come together? What impact do we want to have in our community and in our world? Be sure the entire congregation votes to accept the mission statement. If your church has not developed a mission statement, consider creating a group to steer the process concurrently with the work of the endowment policy committee. Establish goals and time lines to ensure the process is completed in a reasonable amount of time, and work to prevent delays in creating your endowment policy.

- **The name of the endowment**

- **The general purposes and objectives**
  How does the endowment relate to the mission? Does our purpose for the endowment inspire contributions?

Definition of Terms

You will want to define the different types of funds and uses that can be established within your church's endowment fund —

- **General or Unrestricted**
  Funds donated with no donor restrictions regarding the purpose, timing or use of the principal or income earned

- **Designated**
  Funds donated with no donor restrictions, but which the church has voted to designate for a specific purpose

- **Temporarily Restricted**
  Funds donated with a donor restriction that will be released upon a certain date or occurrence of a specified event

- **Permanently Restricted**
  Funds donated with a donor restriction regarding the purpose, timing or use of the principal or income earned. Acceptance of a permanently restricted gift legally binds the church to respect the restriction in perpetuity

Your church may also consider defining the various types of funds that may comprise the overall endowment fund: memorial, contingency, emergency, discretionary, and'special funds, to name a few popular options. Remember, however, the less compartmentalized your endowment, the more flexibility your church will enjoy as it seeks to respond to ministry needs and opportunities.

Non-Cash Gifts

Not every gift made to a church comes in as cash. Donors maybe able to enjoy significant tax advantages, for instance, by making direct gifts of stock or real estate. In developing an endowment policy, a church needs to establish procedures to be followed whenever a non-cash gift is made. Generally, the best course is immediate sale of the asset. In determining your policy, consider the following —

- Establish a procedure for determining the marketability of non-cash gifts prior to acceptance. While a donor may desire to give real estate to the church, for example, a piece of property that is not immediately salable can end up creating new expenses for the church in taxes, maintenance fees and realtor commissions. If a gift cannot be sold quickly and easily, consider declining the gift.

- Determine how gifts of stock will be handled. Again, the best course of action is usually immediate sale. However, in rare instances, the church may wish to hold the stock. Consider a policy that isolates the stock from the rest of the endowment's investments so that asset allocations remain balanced and the church's portfolio remains well diversified.

- Avoid gifts that come with restrictions on sale, as they can become costly, cumbersome or both.

Restricted!

These days, donors increasingly seek to designate their gifts. Some desire to support a particular ministry near to their hearts, others enjoy the pleasure of identifying the program or asset they helped to provide, while some simply want to control the use of the money they give. Restricted gifts pose a range of challenges for a congregation — from creating accounting headaches to erecting obstacles to a church's ability to respond to changing needs and times.

Encourage unrestricted giving

To limit new restricted gifts to your endowment fund, consider the following suggestions —

- State the purpose and objectives of your endowment in a clear and engaging manner, inspiring participation in the greater, collective goal
- Create funds within the endowment to which a donor may allocate their gifts
- Include all members of the congregation in the development of the endowment and its policies to enhance a sense of collective ownership
- Regularly educate the congregation about the ministry being accomplished thanks to the endowment
- Establish minimum gifts requirements that must be met before restrictions will be accepted
- Be prepared to decline gifts that pose restrictions that will unreasonably encumber the church and its ministry

Manage restrictions

Because some donors will insist on making restricted gifts, be sure your endowment policy includes language that gives the church flexibility in accepting these types of gifts —

- Consider establishing a minimum for gifts that will be restricted and/or named after the donors (see Gift Acceptance Policy on page16)
- Encourage donors to include wording in the gift documents that permit a change of use if the stated restriction becomes impossible or not feasible for the church to continue. Churches and ministries can change significantly over time, leaving restrictions outdated and funds sitting idle — a situation no donor desires for their church.

Release restrictions

If your endowment already includes restricted gifts that are creating difficulties in management or spending, discuss concerns with donors (if still living) and/or legal counsel to determine whether restrictions may be lifted or otherwise eased to allow more money to be used for your church's ministry. In some states, UPMIFA permits release of restricted gifts that are 20 years old and under $25,000 with a simple letter of notice to the state's attorney general. Visit www.upmifa.org for links to your state's law.

Gift Acceptance Policy

Endowments are generally comprised of a variety of gifts accumulated over the years. Sometimes an endowment begins with one large gift — perhaps one made generations ago — and grows with gifts made through wills, planned gifts and outright contributions. A gift policy helps to ensure the gifts offered to the church suit the church's needs and objectives.

- What kind of gifts will we accept? What will we reject (ie, timeshares, real estate, furniture)? And who will determine whether or not a gift fits the church's Gift Acceptance Policy?
- What types of funds will comprise the endowment (ie, memorial funds, cemetery funds, special purpose funds)?
- How will undesignated gifts be directed?
- If property or non-cash gifts are given to the church (real estate, stocks, bonds, etc), how will we dispose of it? Is a proposed gift of real estate free of environmental hazards like asbestos or in-ground contaminants?
- What conditions will we accept from a donor? Must a gift be above a certain dollar amount before it may come with restrictions?
- Will we allow "named" gifts? If so, under what conditions?
- If gifts are subject to donor restrictions to spend income only, how will the gift amount be determined as its market value changes?
- What happens if the goal of a restricted gift no longer exists or is needed?
- Will the church seek to attract new gifts to the endowment through planned giving programs?
- How will gifts be recorded and honored?
- What committee or officer is responsible for ensuring the gift policy is followed?

Give donors a choice of designated funds within the overall endowment to limit the perceived need to restrict gifts. Primary ministry areas (education, missions, youth, etc) can offer guidance for the creation of designated funds

Even if a church chooses not to develop a full-fledged endowment policy, the governing body should insist upon a gift acceptance policy. Gift policies help to ensure that the church is not burdened with inappropriate gifts like cast-off furniture, out-dated and energy-hogging appliances, hard-to-sell securities and problem real estate.

Here's a case in point: a true story from a UCC church —
A church member could not sell a timeshare he owned, and so decided to give the timeshare to the church. Because the church did not have a gift policy in place, the gift was accepted and the donor took a sizable tax deduction for his "charitable contribution." The church soon discovered, however, that not only would the property be difficult to sell, it would actually cost money for the church to own! The church spent thousands of dollars on taxes and maintenance fees before finally unloading this "gift."

A gift acceptance policy helps keep everyone honest, and prevents the church from facing difficult — even expensive — gift conundrums.

Fiduciary Responsibility

When an individual, committee or organization is entrusted with the management of investment decisions for assets that belong to others, that trusted partner becomes a fiduciary, charged with serving as a prudent steward of the entrusted assets. Over the years, the standards of prudent stewardship have become increasingly well defined; and in June of 2006, were written into the new Uniform Prudent Management of Institutional Funds Act (UPMIFA). As a church or other organization makes decisions regarding the management of its assets, an understanding of fiduciary responsibility becomes important. When enacted by your state, UPMIFA becomes the mandatory standard to which your investment committee and manager must adhere.

The word "fiduciary" derives from the Latin fide or "faith" — the same root for fidelity, faithfulness and confidence. When we trust a fiduciary with our assets, we expect their actions will be carried out in a manner that is faithful to our intentions. We place our faith and confidence in their judgment, virtually without reservation. When you become a member of the governing body of a church or other not-for-profit organization, you take upon yourself fiduciary responsibilities on behalf of the organization's past, present, and future members. Such fiduciaries are expected to render comprehensive and continuous advice, and must take care to maintain their undivided loyalty toward the organization that places its trust in them. Investment or endowment committee members assume three primary duties of fiduciary responsibility.

1. **The Duty of Loyalty —**
   acting solely in the best interest of the institution, rigorously avoiding even the appearance of a conflict of interest while managing the organization's affairs. The duty of loyalty means that church or committee members cannot serve as the organization's investment broker or agent, even if they agree to return any commissions or earnings they may derive.

2. **The Duty of Care —**
   operating in a reasonable and informed manner, insisting on the information needed to monitor investment managers, and using best practices in decision making. The duty of care also assumes that investment committee members will attend committee meetings regularly.

3. **The Duty of Obedience —**
   operating in accordance with the stated mission, goals and objectives of the organization; remaining in compliance with both the law, and with the policies, guidelines and covenants established by the organization. Church members nominated to serve on investment or endowment committees need not be investment professionals — a range of voices are needed to ensure each committee represents the church as a whole.

Consider requiring all lay leaders sign a Conflict of Interest agreement. Visit unitedchurchfunds.org for sample documents.

Investment Policy

Endowment funds must be wisely invested in order to both ensure good stewardship of the fund and to meet legal standards of prudence. An investment policy is, therefore, an essential element in an endowment policy — but is also important for all of the church's funds, including reserves and savings invested for differing time horizons. Remember: because church leaders bear a fiduciary responsibility for the church's investments and their management, careful attention to this policy is essential.

- What are the church's primary investment objectives: return and income? growth? security?
- What is the church's philosophy and tolerance of risk? How much volatility can the church tolerate to achieve the return results desired?
- Most endowments are considered investments "in perpetuity" — does the church have any other time horizon requirements?
- What kind of liquidity needs does the church have where the endowment is concerned?
- How important is diversification: across asset types, industries, asset management styles (large cap, small cap, growth, value, etc.)?
- Who will determine allocations among the various investment categories: cash and equivalents, fixed-income, equity, real estate, other?
- Which investment vehicles are acceptable and which are not (investment vehicles include stocks, bonds, mutual funds, real estate, precious metals, commodities, etc)? Must they all be marketable?
- Who will manage investments: an internal committee? an outside manager or firm? United Church Funds?
- Who will supervise the progress of the managers and the portfolio, and what standards of measurement will be used to evaluate results?
- What is the church's perspective on socially responsible investing? Who will determine the screens and monitor investments for compliance?
- What officer or committee will be responsible for monitoring the investments of the endowment, and reporting back to the congregation on a regular basis?

Measuring Performance

The performance of investment managers is generally measured against an industry standard or index, determined by the type of investment being measured. An index offers a statistical indicator that represents the average value of the index's underlying securities, and often serves as a barometer for a given market or industry and a benchmark against which performance may be measured. For the most accurate comparison of performance, calculate returns net of fees (UCF's performance is always reported net of fees).

United Church Funds uses the following five indices to measure the performance of its investment funds —

Standard & Poor's 500 Index (S&P)
A basket of 500 US large cap stocks considered to be widely held. The S&P 500 index is weighted by market value, and its performance is thought to be representative of the stock market as a whole.

Barclays Capital Government/Credit Index (BCGC)
A fixed-income measurement tool, this index includes US Treasury obligations with remaining maturities of more than one year, government-related bond issues, and US Corporate bonds.

Russell 2000 Index
Published by the Frank Russell Company, this index measures the performance of the smallest 2,000 companies in the Russell 3000 Index of the 3,000 largest US companies in terms of market capitalization.

Europe, Australia & Far East (EAFE) Index
Created by Morgan Stanley Capital International, EAFE offers an unmanaged, market-value weighted index designed to measure the overall condition of overseas markets.

Lipper Money Market Funds Index
A mutual fund performance tracking and rating system, the Lipper index allows an investor to compare a particular money market fund to other money market funds.

The Problem of Internal Management

Endowment funds may be invested many ways — in mutual funds or in individual stocks and bonds —and may be managed by trust companies, investment advisors, portfolio managers, and by United Church Funds. Sometimes, endowment and investment committees choose to manage their church's portfolio internally — but such a choice often proves cumbersome and difficult, fraught with opportunities for conflicts of interest, conflicts among church members, even legal challenges posed by fiduciary responsibilities.

With rare exception, churches are well advised to select an outside investment manager to handle their endowment portfolio. In selecting an investment manager, a committee should consider the potential manager's —

- company structure
- management history
- performance history with the types of assets your church has selected
- fee structure
- commitment to investing with your values in mind

The UCF Advantage

For many churches, investing with United Church Funds resolves a host of investment policy issues with —

- nine funds among which an endowment may be invested
- expert management with a strong track record
- well-diversified funds that are actively managed and continuously monitored by investment professionals
- low fees
- an active program of socially responsible investing and share holder engagement
- regular quarterly reporting

To review the Investment Manager Questionnaire, visit unitedchurchfunds.org

UPMIFA Highlights

The Uniform Prudent Management of Institutional Funds Act

In July of 2006, the National Conference of Commissioners on Uniform State Laws approved the Uniform Prudent Management of Institutional Funds Act (UPMIFA), and urged states to adopt the Act as law to replace the 1972 Uniform Management of Institutional Funds Act (UMIFA). The new Act updates and modernizes the prior, providing stronger guidance for investment management and establishing more precise rules for prudent investment. Highlights of UPMIFA include —

- **Investment freedom**
  Portfolio managers are not limited in the kinds of assets that may be sought for the portfolio.

- **Costs**
  Costs must be managed prudently in relationship to the assets, the purpose of the institution and the skills available to the institution.

- **Expenditure of funds**
  Total return expenditure is expressly authorized under comprehensive prudent standards relating to the whole economic situation of the charitable institution. Seven criteria guide the determination of the percentage of total return an organization may select —
  1. duration and preservation of the endowment fund
  2. the purposes of the institution and the endowment fund
  3. general economic conditions
  4. effect of inflation or deflation
  5. the expected total return from income and the appreciation of investments
  6. other resources of the institution
  7. the investment policy of the institution

- **Historic dollar value abolished**
  UPMIFA abolishes the historic dollar value limitation on expenditure in UMIFA. "Historic dollar value" is the fair value of the original gift and subsequent gifts along with accumulations to the permanent endowment.

- **Seven percent rule**
  States may adopt an optional rule that presumes expenditure exceeding 7% of total return is imprudent.

- **Release of restrictions for small institutional funds**
  UPMIFA provides new procedures for releasing restrictions on small institutional funds (less than $25,000) held for a long period of time (20 years), requiring only notice to the Attorney General 60 days in advance of the release.

As of June 2010, some form of UPMIFA has been become law in all states except FL and PA, with legislation pending in MS and NY.

Spending Policy

How will distributions be determined?

UPMIFA anticipates endowment spending will be based on Total Return, which permits a certain percentage of the portfolio's value to be spent each year (see glossary for Essential Terms).

- How will the average portfolio value be calculated?
- What percentage will be withdrawn?
- At what intervals will the church take distributions: annually? quarterly?

How may distributions be directed—

- to specific programs? which ones?
- to the church's annual budget in either a fixed amount or at a fixed percentage?
- to programs and particular budget items (ie, building maintenance, missions)?

Under what conditions will your church allow excess distributions?

- What is the maximum distribution permitted? May the entire endowment be spent?
- How may excess distributions be spent? in what circumstances?

Who will ensure the spending policy is followed?

- What officer or committee is responsible for ensuring funds are spent as specified?
- What kind of reports must be prepared regularly?
- Who will report to the congregation on endowment-based spending?

Trusts managed by United Church Funds use a 5% spending rule calculated on a five-year trailing average balance.

Valuing Gifts Over Time

The value of a gift when contributed is generally an easy amount to calculate — but over time, establishing the "original value" can become a bit more tricky. Is the original amount an adequate number to track, or must the gift's value be adjusted for inflation? UPMIFA eliminates the need to maintain historic dollar valuations as long as the church avoids excessive expenditure and considers the following criteria —

1. the duration and preservation of the endowment fund
2. the purposes of the institution and the endowment fund
3. general economic conditions
4. effect of inflation or deflation
5. the expected total return from income and appreciation of investments
6. other resources of the institution
7. the investment policy of the institution

Visit www.upmifa.org to determine how UPMIFA is implemented in your state.

A good rule of thumb in most cases: no more than 20% of a church's operating budget should be funded by the endowment.

Recordkeeping & Reporting

As with all church business, transparency is essential in all aspects of endowment management and reporting.

- Who will manage the accounting for contributions, investment results, and distributions?
- How will the records be maintained?
- Where will the founding documents be safeguarded? United Church Funds will keep a copy of all founding documents and gift records forwarded by United Church Funds investors.
- What reports will be provided to the congregation, and at what intervals: investment results? distributions and spending? original gifts received?
- How will donors be recognized?
- How often will officers and committee members be elected? How many terms may they serve before they must stand down?
- What policies are in place to ensure regular turnover of individuals serving in financial capacities?

Other Legal Particulars

- How often, and by whom, will the endowment be audited? An audit ensures transparency and encourages continuing donations to the endowment. Like management fees, audit fees are paid from the endowment. NOTE: Unless the endowment is established as a separate legal entity, an audit of the church's financial records will include the endowment.

- How may policies be amended or modified, including fund designations?

- How will funds be distributed if the church merges or closes?

- What committee and officer responsibilities still need to be addressed?

- How will we define the fiduciary responsibility of managers, officers and committees?

- How will we protect trustees from liability when they are acting in good faith?

- Will we require bonding of all people handling money and accounts?

- What conflict of interest policies do we need to include?

Reconsidering the Endowment Spending Policy

A spending policy based on Total Return means more money for ministry

For generations, investors were taught to "invest the principal, spend only the income." And back in the old days, that advice made sense. But times have changed, and the standards for prudent investment management have changed as well. In recent years, many corporations have shifted their focus away from paying shareholder dividends, focusing instead on increasing the value of the stock itself.

Investing for total return
As a result, today's diversified investors look for overall portfolio growth rather than concentrating on income potential — a concept known as investing for Total Return. Rather than withdrawing the dividend income from their portfolios, institutional investors — from the Ford Foundation to Harvard University to historic churches — reinvest their dividends and evaluate performance by considering the overall growth in the value of their portfolio from both reinvested earnings and capital gains.

Technology company Microsoft offers a good example of the wisdom of the Total Return approach. Microsoft made its initial public offering in 1986, but didn't begin paying dividends until 2003. If you had purchased 100 shares of Microsoft 10 years ago when the market opened on June 1, 1998 ($20.97/share), and sold those shares (which had now grown to 400 shares thanks to stock splits) at the same time five years later ($24.98/share), you would have gained $7,895 or an average annual return of 75% — but you would have enjoyed no cash benefit until you sold your shares. Had you held your shares, you would have achieved an average annual total return of 44% from your initial investment of $2,097.

An individual investing for retirement might not have minded receiving no income over those years. But church endowments generally have different requirements. Donors to endowments intend for their gifts to be used continuously to advance the mission and ministry of the church over generations. Consequently, endowment funds need to be invested so that the long-term power of the financial markets can grow the portfolio, protect its value from the eroding effect of inflation, and generate an income stream to fund mission and ministry programs.

Spending Policy Based on Total Return
With the shift to investing for Total Return, institutional investors have established spending policies that ignore the distinctions between principal and income. Instead, a modest percentage of the portfolio's value is "cashed in" each year to create the revenue used for the organization's mission.

For many who are new to the idea of a spending policy based on Total Return, the notion of selling part of the portfolio sounds a lot like 'dipping into principal.' But investing for Total Return requires a new way of thinking about the portfolio: instead defining principal instead defining principal (or the corpus), the portfolio is seen as an integrated whole from which both income and capital gains become available to support the organization.

Take the Microsoft example above. Prior to the company's distribution of dividends, no cash was available even though the portfolio was growing rapidly. Even after Microsoft began paying dividends, income totaled only $1,800 from 2003 to 2008; but a spending policy based on Total Return would have provided over $3,600 for ministry — twice as much — while the portfolio value still realized a 10-year gain of $8,500 or an average annual return of over 40%.

For most institutions and local churches, a spending policy based on total return is determined in a way that permits adjustment as circumstances require —

1. *The value of the portfolio is determined at a given point in each of the last three to five years.*
   A three-year range is typical, while a five-year range is more conservative. Because the range considers values from prior years, church budget managers know in advance how much money will be available from the endowment.
2. *An average value is calculated from the values in the range.*
   This value is known as a rolling average, as the three- to five year range shifts by one year each year.
3. *A percentage of the resulting average portfolio value is sold.*
   Most spending policies establish 3-6% spending range, with most organizations spending in the 4-5% range.
4. *The proceeds are spent as permitted by the terms of the endowment or organizational policy.*
   Although the overall value of the portfolio is reduced by a small percentage each year, the value of a well diversified portfolio should continue to grow over the long term. The chart below illustrates the performance of a $10,000 church endowment invested on January 1, 1978 in the United Church Foundation's Moderate Balanced Fund, which offers a prudent mix of both stocks and bonds. Even with a policy permitting a 5% spending rate each year, the value of this $10,000 investment grew by an average of 20.3% each year for 30 years, to a total value of $70,924. Even more exciting, however, is the fact that a spending policy based on total return would have permitted this church to invest more than $57,000 in ministry over the last 27 years — funds earned from the total return on the initial $10,000 investment!

When faithful members and donors entrust future generations with legacies and gifts intended to serve the church for decades to come, each group of trustees bears a sacred responsibility to manage both the investment and expenditure of those funds in a wise manner — faithful both to the intent of the donor and informed by an understanding of the financial markets and prudent investment management.

The United Church Funds stands ready to assist churches and UCC-related organizations with guidance in developing updated investment and spending policies, offering professional investment management services, and helping build endowments that provide more money for ministry.

Year	Total Return	$10,000 Investment	3-Yr Rolling Average	5% Spending Policy	CPI	Inflation-adjusted value
1978	4.52%	$10,452.00			7.6%	$9,657.65
1979	13.21%	$11,832.71			11.3%	$10,495.61
1980	15.60%	$13,678.61			13.5%	$11,832.00
1981	4.96%	$14,357.07	$11,987.77	$599.39	10.3%	$12,878.29
1982	21.32%	$16,818.61	$13,289.46	$664.47	6.2%	$15,775.86
1983	14.64%	$18,616.38	$14,951.43	$747.57	3.2%	$18,020.66
1984	5.33%	$18,861.06	$16,597.35	$829.87	4.3%	$18,050.04
1985	30.72%	$23,825.31	$18,098.68	$904.93	3.6%	$22,967.60
1986	12.80%	$25,970.02	$20,434.25	$1,021.71	1.9%	$25,476.59
1987	0.39%	$25,049.59	$22,885.47	$1,144.27	3.6%	$24,147.80
1988	13.87%	$27,379.69	$24,948.31	$1,247.42	4.1%	$26,257.13
1989	25.08%	$32,999.11	$26,133.10	$1,306.66	4.8%	$31,415.15
1990	-0.07%	$31,669.35	$28,476.13	$1,423.81	5.4%	$29,959.21
1991	26.27%	$38,565.08	$30,682.72	$1,534.14	4.2%	$36,945.35
1992	10.83%	$41,207.55	$34,411.18	$1,720.56	3.0%	$39,971.32
1993	10.90%	$43,978.61	$37,147.33	$1,857.37	3.0%	$42,659.25
1994	-3.48%	$40,590.79	$41,250.41	$2,062.52	2.6%	$39,535.43
1995	26.99%	$49,483.72	$41,925.65	$2,096.28	2.8%	$48,098.18
1996	13.76%	$54,196.40	$44,684.37	$2,234.22	3.0%	$52,570.51
1997	21.79%	$63,771.58	$48,090.30	$2,404.52	2.3%	$62,304.83
1998	19.64%	$73,891.80	$55,817.23	$2,790.86	1.6%	$72,709.53
1999	11.36%	$79,495.05	$63,953.26	$3,197.66	2.2%	$77,746.15
2000	-0.22%	$76,122.49	$72,386.14	$3,619.31	3.4%	$73,534.33
2001	-5.91%	$68,004.35	$76,503.11	$3,825.16	2.8%	$66,100.23
2002	-11.22%	$56,549.10	$74,540.63	$3,727.03	1.6%	$55,644.32
2003	19.08%	$63,611.64	$66,891.98	$3,344.60	2.3%	$62,148.57
2004	8.42%	$65,623.14	$62,721.70	$3,136.08	2.7%	$63,851.32
2005	4.66%	$65,545.10	$61,927.96	$3,096.40	3.4%	$63,316.56
2006	10.59%	$69,389.92	$64,926.63	$3,246.33	3.2%	$67,169.45
2007	6.89%	$70,924.56	$66,852.72	$3,342.64	2.8%	$68,938.67
				$57,125.76	4.2%	

This table illustrates a $10,000 investment in the Moderate Balanced Fund, adjusted for inflation as represented by the Consumer Price Index (CPI), which offsets the actual total return each year. Past performance is not indicative of future performance, and an investment made in this fund today may gain or lose value in the future.

FINAL Steps

Present the Draft

4

Once your committee(s) have created a draft of recommended policies, present the draft to your council or consistory — or smaller churches may choose to test the document broadly in the congregation. Plan time for discussion of points that have generated a lot of input or conversation, and help church leaders (or members) understand the choices you made. Give everyone involved time to read and consider the draft before reconvening to resolve any lingering issues.

Then present the draft to the congregation in a manner appropriate for your church. Remind people that the document is still a draft, and create opportunities where the policy development teams can respond to questions and explain their decisions.

Listen carefully to the questions that are asked — and even to those that are not asked. Work to understand the concerns that different members raise as they seek to move forward in the process. Depending on the level of interest and involvement in your church, the policy development committees may need to return to the previous step to reconsider and even re-draft some of their statements before moving forward.

Seek legal review

With input from church members and leaders considered and outstanding issues resolved, submit your refined policy to legal counsel for a review that considers the law in your state. Be sure to select an attorney with experience in a relevant area of the law, and consider asking a CPA and investment professional to review the document as well. If you're considering using United Church Funds as your investment manager, submit your draft policy for a free review to ensure no conflicts exist with UCF's guidelines and policies. Once the reviews are complete, refine your policy to a final document.

5 Refine the Final Document

Considering the feedback from church leadership and interested members, edit and refine your policy. If conflicts persist that could pose a problem in a congregational meeting, draw the concerned parties together to discuss and resolve significant differences.

Once your policy is finalized, be sure to proofread the final document carefully before its final presentation to the congregation.

6 Vote on the Policy

Present the final policy to the congregation for a vote. Use the occasion to thank the members and professionals who shared their time and skill, to celebrate the moment as a milestone in the church's growth, and to gain widespread ownership of the endowment and its objectives. Take the opportunity to educate the congregation about the endowment and its value to the church's future, reminding members to include a gift to the endowment in their wills.

The Challenge to Leadership

by Robert F. R. Peters, Jr.

The endowment planning committee of Main Street United Church of Christ was deep in discussion. The issue: whether the endowment fund they were developing would have a negative impact on annual support for the church. Martin was worried. "I think we may see a decline in giving if our endowment gets too big. Maybe we should limit its size." Maria, on the other hand, wasn't worried. "It seems to me that a person's financial commitment is based on love of God. I give based on my faith, not on whether the church needs funds."

Both research and experience with church endowments shed light on this discussion. In one study, when asked whether the presence of an endowment fund would have a negative effect on annual giving, 60% of those surveyed agreed that an endowment would cause giving to decline. However, 80% of the same study's participants, when asked if they would reduce their own giving because of an endowment, said they would not.

One key to successful use of an endowment: to ensure that a congregation's operating budget does not rely heavily on endowment income. Some observers suggest that the level of operating support from an endowment should not exceed 20%. Evidence suggests that increasing the percentage of annual support from the endowment may be a factor that correlates with reduced commitment to stewardship and annual giving.

A large endowment does not necessarily depress annual giving. Research indicates that some churches with large endowments experience little negative impact on annual giving, while others with small endowments do encounter a decline in annual giving. In this writer's research among 20 UCC congregations with endowments exceeding $1 million, the six congregations that reflected the least negative relationship between endowment and annual support agreed strongly that 'the leaders of the congregation showed strong commitment to stewardship through their personal giving'.

The level of annual giving in congregations with endowments is most directly influenced by the following actions —

1. Ensure the congregation understands the church's mission and vision. Two researchers have noted that leaders responsible for oversight of the endowment should spend time in the study of Biblical material related to wealth and faith to gain new perspectives related to decision-making.
2. Develop a dynamic program of stewardship development The pastor and leaders of the congregation must be committed to a meaningful, ongoing stewardship emphasis, of which endowment development is part.
3. Develop and distribute well-defined, written endowment and gift acceptance policies
4. Control the percentage of the operating budget supported by endowment income

In a study prepared in 1985, Loren Mead of the Alban Institute declared, "If a congregation's leaders, beginning with the pastor, believe in the importance of stewardship and practice it themselves, there is no need to worry that an endowment will cripple the congregation's ability to present the challenge of personal stewardship as part of a person's response to his or her understanding of their faith."

7 Promote the Endowment

While some endowments are built from a significant founding gift, many develop over time as church members make intentional contributions to an established endowment fund. Even if a handsome endowment is presently just a dream, creating an endowment policy and seeding the fund with a small contribution can get the ball rolling and launch the church on a path to building a legacy.

Educate the congregation

The process of developing an endowment policy does more than just create a document — the process begins to educate church members about the value of an endowment and their part in helping it grow. Continue to keep the endowment in front of members with regular educational efforts: include articles in the church newsletter, host programs about wills and their importance for every adult, distribute brochures and other information about planned giving.

Promote planned giving

Planned giving offers church members a way to strengthen the church not only through a bequest identified in a will that is paid upon the donor's death, but through gifts made in the present. A variety of planned giving vehicles allows donors to meet their own current needs while supporting the church in the future.

Many charitable gifts arranged through the UCC's Financial Development Ministry are managed by United Church Funds, offering donors the assurance of proven, professional management that seeks to maximize the value both to the donor and the ultimate recipient.

Launch a capital campaign

While most churches begin capital campaigns for building projects, a multi-year campaign can also build the financial "structure" of an endowment. A capital campaign to create an endowment seeks gifts over-and-above regular giving, generally paid over a three-year period. The resulting fund becomes the foundation on which the church can continue to build through ongoing educational and planned giving programs.

Getting Started with a Wills Emphasis

One of the best ways for a church to build its endowment: begin a wills emphasis in your congregation.

Writing and maintaining an updated will remains an important issue and act of stewardship — ensuring your family and loved ones are protected in the event of your death, and helping to ensure that the organizations you value receive the gifts you intend.

Your will should reflect the current circumstances of your life and be updated upon a change in —

- family status (ie, marriage, birth, divorce)
- the nature or value of your estate
- laws affecting estate planning
- your place of residence from one state to another

Consider offering a will-writing seminar or program for your church or organization that includes legal assistance to ensure compliance with state and other laws.

Endowment Building with Planned Giving

The UCC's Financial Development Ministry helps donors arrange a variety of planned gifts to support their local church endowment, ministries and organizations related to the United Church of Christ, and even non-UCC organizations. Potential donors can consider the following options, consult with their financial professional, then contact the Financial Development Ministry at 800-846-6822 or giving@ucc.org.

Life Income Gifts
These gifts pay a donor income for life, with the remaining principal paid to the designated church (or other UCC-related organization). The donor receives a tax deduction for the charitable portion of the gift in the year the gift is made. Life-income gifts may significantly increase a donor's spendable income, and may also be established in a will for the benefit of heirs and the ultimate benefit of the church.

Charitable Gift Annuity
Annuities may be funded with cash or appreciated securities, and provide fixed income payments for life to the donor and/or another person (successively). A gift annuity's rate of return is based solely on the donor's age at the time of the gift, and a significant portion of the income may be tax-free. Donors may defer income payments to a later date, such as retirement age, which may produce a substantial increase in the rate of return.
Minimum gift: $1,000

Charitable Remainder Trusts
These irrevocable trusts may be funded with cash, securities or real estate, with the donor enjoying fixed or flexible income payments during their lifetime. The most common type, the unitrust, is valued annually with the donor paid a fixed percentage of the value over the following year.
Minimum gift: $50,000

Pooled Income Fund
Working much like a mutual fund, this fund accepts and manages gifts from many donors, then distributes each gift's portion of the earnings to the designated life-income beneficiary(ies).
Minimum gift: $2,000

Life Insurance
The church can be named as the beneficiary of a life insurance policy, or the policy itself may be donated to the church. If the policy is paid, the donor's tax deduction will generally be the replacement cost of the policy at the time of the donation.

Retirement Assets
Retirement assets may be expensive for heirs to inherit, yet naming the church as a beneficiary of a retirement fund may provide significant estate tax savings.

Charitable Lead Trust
This gift provides current income to the church during the donor's lifetime or for a specified term of years, after which the remaining principal is returned to the donor or his/her heirs. Payments to the church may be fixed or variable, depending on the terms of the trust.
Minimum gift: $100,000

Regularly Review the Policy 8

Because cultures, communities and churches change over time, be sure to review your endowment policy every few years. While frequent changes are not recommended and alterations should require a "super-majority" vote, the church will want to consider whether the choices made during the policy's development still make sense for the church in its current configuration. Is the policy helping the endowment fund meet the church's objectives? Are some elements proving too cumbersome for effective management? Do any revisions or adjustments need to be considered? A regular review ensures your endowment policy remains an effective guideline for church and ministry leaders.

FAQ & Glossary

Frequently Asked Questions

Is our church really big enough for an endowment policy?
If your church is big enough to receive a lasting gift, it's big enough for an endowment policy. Often, churches find that the people they least suspect are the people who leave substantial gifts to the church in their wills. A policy needs to be in place before a gift is made to guide the church when happy surprises come its way. Even if a church has only a small "reserve" account that's used for special projects, gift and investment policies help ensure fewer conflicts and better management of the funds.

Doesn't the church need to depend on its current members to support its ministry?
Absolutely! An endowment is not a replacement for regular giving and a church community that encourages stewardship. An endowment makes funds available for creative new ministries, for the maintenance of ministry through changing and challenging times, and for special projects or programs. An endowment makes new life possible for a church's mission and ministry.

Don't endowments make people think they can stop giving?
Giving is about far more than money — it's about receiving and sharing the gifts of God. Giving is a spiritual discipline and a personal expression of God's generosity in the world. A good church leader helps members understand that an endowment supplements — rather than supplants — the funding of the church's ministry.

Shouldn't we spend all the money we have on ministry — not hoard it in an endowment?
While God surely blesses an active and relevant ministry, God expects us to make an effort to multiply our gifts. Just look at the parable of the talents! An endowment allows a church to put the gifts of its members past and present to work in perpetuity — using those gifts not just for the short-term, but investing them so that the church has the ability to impact its community, even the world, for years to come.

Why should the entire congregation be involved in the endowment policy?
An endowment belongs to the whole church, and just as transparency is important in the day-to-day use of the church's funds, transparency is critical in the use of funds entrusted over generations. The entire church determines how the budget will be spent each year —the investment and distribution of the endowment deserves equal consideration.

Essential Terms

Like every area of specialty, endowments and related policies have a vocabulary of their own. A good investment "dictionary" can be found at investorwords.com.

Asset
Cash, property or other goods owned by an individual or organization. Assets may include investments, buildings, art, furnishings or other items of value.

Bequest
A gift designated in a will, which is typically paid upon the donor's death. The will might read as follows: "I give, devise, and bequeath to NAME OF CHURCH/ORGANIZATION, the sum of AMOUNT [or a percentage of assets, other specifically described personal or real property, or even the residual of an estate after other bequests have been paid] for its general uses and purposes."

Distribution
An endowment can only benefit an organization when the money is put to use for more ministry. An endowment policy outlines the timing, amount and recipient of distributions — or monies paid out — from the endowment. Where investors once sought to "preserve the principal, spend the interest," modern endowments establish a certain percentage (usually 3-6%) of the total value of the endowment to be paid out on a regular basis.

Endowment
A pool of money — which may contain several different gifts, funds or accounts — that is set apart by a church or organization to accomplish specific and stated objectives. Some endowments are "restricted" to very particular purposes, while "unrestricted" endowments may be used for any purpose that meets endowment policy guidelines.

Income
Traditionally the "spendable" return on investments, like interest or dividends. Under current laws in most states, income includes not only interest and dividends, but also a portion of appreciation — both realized and unrealized — on investments.

Investment
The money in an endowment must be invested in some way to maintain and ideally grow the value of the pool of funds. Investment options vary widely, so an investment policy is needed to specify the parameters under which money is invested.

Principal
Traditionally understood to be the original gift, usually adjusted to represent the historic value as given by the donor. For modern investment managers, however, the notion of "principal" that is never touched no longer applies; instead, managers use a policy of investment for Total Return.

Rolling Average
A spending policy based on Total Return must set a point at which the value of the portfolio is established so that a pre-determined percentage of the portfolio may be sold. Rather than spending based on just one year's value, however, a prudent investor will consider the value of the portfolio at the same point for the last three to five years, then calculate their distribution based on an average of those different portfolio value figures.

Total Return
Total Return includes both current yield (interest and dividends) and accumulated changes in the value of the investment. Corporate and investment managers once focused their attention on the dividends to be paid to shareholders; but today, the focus has shifted to appreciation in stock price or value. Investors seek stocks that will increase in value, whether or not dividends are ever paid, because the real cash benefit of stock ownership accrues to investors when stock is sold at a profit. A policy of Total Return assumes dividends and income will be reinvested, and the investor will seek an overall increase in value of the portfolio. With a spending policy based on Total Return, an investor simply sells a small percentage of the portfolio when he or she decides to spend part of the accrued wealth.

UPMIFA
The Uniform Prudent Management of Institutional Funds Act, which can be found at upmifa.org.