COMMITTEE REPORT:
HIGH-NET-WORTH FAMILIES & FAMILY OFFICES

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Philanthropy in a Pandemic

Have the giving strategies of family offices changed?

The year 2020 has ushered in unexpected and unprecedented challenges across a myriad of dimensions, from health to wealth to family and philanthropy. The onset of the COVID-19 pandemic—and the ensuing turbulent markets and global economic shutdown—have spurred many family offices to revisit their philanthropic strategies. Civil unrest in the pursuit of racial equality and justice have added further impetus, compelling many to consider, and at times enact, meaningful change.

Over the past few months, we've undertaken countless consultations with philanthropic families regarding today's landscape and its potential impact on their giving strategy. For this article, we supplemented those discussions with extensive interviews with philanthropically minded family offices. In particular, we sought out large family foundations and family offices with long-standing charitable track records. In doing so, we explored a range of subjects including:

- What concerns rank top of mind?
- How do you expect giving strategies to change, if at all?
- Are there tensions among the family's stakeholders?
- What changes sparked by the pandemic and wider racial justice movement might be woven into the fabric of the family's long-term philanthropy?

We asked family stewards to consider their philanthropic missions and visions and the underlying values that informed these principles. Ultimately, we know that values represent the inspirational underpinnings that tend to drive individuals towards altruism. See "Values Inform Philanthropy," p. 50. Unsurprisingly, many interviewees returned to those values—whether shared across a family or unique to individual members—as the key drivers for any change.

Five key themes emerged across our discussions:

Responsiveness

Donors across the board expressed a desire to heed the calls coming from their communities, the causes they feel passionate about and the organizations with which they've formed deep relationships. As a result, several foundations have accelerated grants originally scheduled for later in the year, allowing for their immediate use while the need remains greatest. Others manifested their sense of urgency by increasing the size of budgeted grants. However, the responses varied with grantmaking patterns. For instance, one foundation that distributes a few very large gifts spread out over several years noted they hadn't received requests for additional funds or frontloading of existing commitments.

Without exception, all donors had proactively checked in with the organizations they support and continue to monitor the situation closely. When it comes to ongoing diligence, key considerations include

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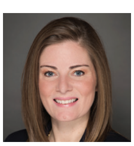
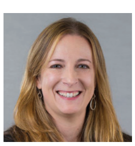
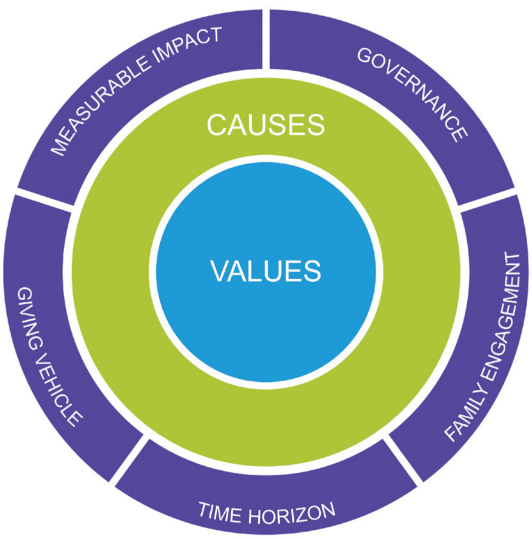



Values Inform Philanthropy

Key drivers for change



— Bernstein

the current and projected health of the nonprofit, an overview of current challenges and exploration of innovative initiatives. For instance, under normal circumstances, foundations seek to make an impact through gifts to non-profit organizations. But, during national emergencies,[1] private nonoperating foundations can establish funds to provide support directly to individuals without advance Internal Revenue Service approval. One private nonoperating foundation offering college scholarships in its community decided to give supporting funds directly to the scholars. These students lived off campus or had sheltered in place at home and found their hardships compounded by loss of employment as restaurants and businesses shut down. This marked the first time that the foundation established such an emergency fund, and it was pleased to have one more tool in its repertoire should it need to adopt a similar approach in the future.

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In some cases, donors' desire for responsiveness has come into direct conflict with long-standing practices, such as adding giving restrictions. Many donors understandably add stipulations to their gifts, requesting that the funds be deployed for a specific purpose, with certain recipients, or distributed in a unique way. But, such restrictions often increase the amount of time, effort and expertise required to process the gift, delaying its use. Nonprofits need resources now, and open-ended and nonrestrictive donations go a long way towards providing immediate relief. The donors on our panel are proactively working to reduce such restrictions to ease the burden on their grantees.

One thing remains clear: Donors are spending time conducting outreach to understand the changing dynamics and constraints of the communities, causes and organizations important to them. The pandemic has created extraordinary needs that can't be ignored.

Partnerships

Many donors appear to recognize that there's strength in numbers. Leaning into and leveraging one's social network to uncover individuals, philanthropic vehicles (that is, other family foundations) and companies that share the same or complementary fields of interest continuously emerge as a theme. Several donors mentioned planned alliances including:

- COVID relief funds
- public/private partnerships[2]
- corporate donors giving in partnership with private giving

One donor remarked that historically, the same 10 individuals in his network championed his philanthropic mission, which aims to reduce inequality through access to education. In response to recent events, he decided to get creative and partner with a local nonprofit providing support to underserved communities. He launched an Income Share Agreement to appeal to those in his network who want to put their money to work for a good cause but also desire a return on their investment. The for-profit circle and the nonprofit joined forces, raising over $750,000 in just four days.

A number of philanthropists demonstrated newfound creativity by tapping a range of strategies to foster meaningful change—often leveraging public/private partnerships in the process. For instance, one family office with a focus on supporting aging seniors recently established a non-profit pharmaceutical company to manufacture drugs designed for seniors in the United States. The move proved timely. Recent turmoil in the health care markets helped the nonprofit secure a major contract from a U.S. government agency.

But, partnerships don't always take the form of a new venture. Often, they arise from revisiting existing ties. In fact, many donors regard today's challenging environment as a potential catalyst to secure additional funds. One donor confided that he's proactively reached out to large corporations for support for his mission over the past several years—with minimal success. He's now finding a more receptive audience. Today's protests and intense media focus have prompted many corporations to funnel their giving to established solutions led by private donors.

Strategic alliances between non-profit and for-profit entities can be mutually beneficial while providing tremendous opportunities for their communities. However, the structure of such arrangements can be complex. It's critical for tax and corporate counsel to match the structure to the mission of the alliance.

Governance

Today's unsettled environment has also impacted governance policies. To provide the best chance for success, clear and effective governance policies should carefully document a donor's vision and mission. Such a governance structure often includes crafting a formal giving policy and process—and communicating it to family members and other stakeholders. Defining the rules and expectations for family remains equally important.

Many of our interviewees represent first generation (G1) wealth creators and philanthropists. We found that when this is the case, giving tends to come with fewer constraints and less rigid governance. In effect, giving centers on the change that G1 wants to affect in the world. To put it more plainly, many G1 members serve as Class A trustees and therefore have the final say—while considering support, feedback and recommendations from other board members.

Often, both foundation assets and personal balance sheets serve as giving sources. One family noted that it currently gives more from its personal portfolio than from the family foundation because the personal side remains more liquid. As such, it's imperative to consider the sourcing of gifts. Will a large unexpected gift cause significant portfolio disruption within the family philanthropic vehicle? Is the family open to contributing more to philanthropic endeavors over time and are thus prepared to add funds today from personal reserves? Many family offices with active G1 members operate their philanthropic efforts with a tacit understanding of how much additional wealth, if any, will move into the foundation on G1's passing. Their actions and giving today align with a very long-term plan.

But, even long-term plans must adapt to changing times. For example, one foundation noted that quarterly board meetings—previously conducted in-person—had shifted to a virtual format. The move allowed them to invite all members of the family as observers (in contrast to two to three at a time in the past). While virtual meetings offer operational and tangible benefits (reduced travel expenses, time savings and ease of logistics), they also dramatically increase the sense of knowledge and connection among family members. As a result, the board plans to continue holding virtual meetings in some capacity, perhaps once per year, so all members can participate.

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From a governance perspective, investment policy statements (IPS) have also come into focus. Drafting, monitoring and adhering to an IPS helps families protect their philanthropic assets. That's because an IPS establishes and documents guidelines for prudent investment of philanthropic assets and ensures that the resources are being used to further the mission. Clearly documenting and defining key components of the investment strategy fosters a transparent, shared

understanding of the approach. A well-designed IPS can typically withstand day-to-day market distractions without revision for up to five years—barring significant changes to mission, time horizon or funding. Yet, with the capital markets in turmoil and volatility elevated, many donors (and the organizations they support) are revisiting their current investment strategies.

At a minimum, an IPS should include:

- Anticipated duration
- Investment goals
- Roles and responsibilities for board members and investment managers
- Target asset allocation
- Constraints
- Performance and risk guidelines

Senior generations with a long-established approach to philanthropy might have concerns about the direction younger generations might take once they assume greater control.

Perpetuity or Spend Down?

Most interviewees represent foundations designed to last for many years or even perpetuity (versus sunset). However, this construct doesn't necessarily correlate to whether a foundation only distributes its required minimum of 5%. Take the case of foundations with G1 philanthropists at the helm—many regularly exceed the 5% distribution threshold each year, arguably on a path to deplete assets. However, the donors still retain meaningful personal wealth, and a number intend to transfer significant additional funds into the foundation on their death. Therefore, a strict adherence to a sustainable spending level from a perpetuity perspective isn't relevant today but remains on the radar for the future.

Sometimes a foundation's intended time horizon can change, especially when a generational transition occurs. Consider one family foundation in the midst of implementing changes as the second generation (G2) assumed leadership after G1 passed. G2 prolonged the foundation's time horizon from sunsetting over G2's lifetime to maintaining the foundation into perpetuity. This shift requires creative solutions, including a re-examination of all costs and expenses incurred today to determine how best to minimize them in the future.

Ultimately, spending policies should align with a donor's philanthropic mission. They're also inextricably linked to how foundation assets are invested. Unfortunately, investment policies that address both longevity and stability often conflict. Typically, a foundation must balance these goals. For instance, foundations aiming for perpetuity require a significant exposure to return-seeking assets such as stocks (typically 70% or more) to deliver the necessary growth to sustain 5% annual distributions and stay ahead of inflation. This exposure tends to result in greater volatility in both annual returns and distributions. But, foundations that plan to spend down their assets have greater flexibility when it comes to investment policies and can take measures to stabilize distributions, if that would serve their charitable goals.

In any case, today's upheaval may prompt donors to review the duration of their giving and ensure that their IPS properly reflects it. If changes result, consider whether they should be evergreen or specific to the current environment.

Engaging the Next Generation

As those at the helm age, it's prudent to begin envisioning how the next generation's involvement might take shape. If engagement seems desirable, family leaders can prepare the next generation by explaining the past and encouraging participation in the present—but always with an eye towards the future. Heirs need to understand how the family's circumstances and expectations might evolve as generational leadership shifts. Some of that understanding comes in the form of educating the next generation about current charitable giving. But, allowing heirs to express their interests and goals for philanthropy, and how their objectives may impact the current charitable plan, remains equally important. For example, a family foundation that expects to expand on a donor's death will need to

decide whether to increase the size of current grants or fund new ones with the additional assets.

Consider a family we consulted in early 2019 about what lay on the horizon for their family office. Currently in the fifth generation (G5), the family expressed the need for a next generation engagement program. Among the options considered, the family explored the establishment of a "junior board," in which the eldest of G5 could participate in the foundation's philanthropic decisions. However, with children sheltering at home and distance learning, G5 felt "zoomed out." Because the program—originally slated to roll out this summer—aims to go beyond education and inject some fun, the family pushed back the launch to the summer of 2021 due to the pandemic. It's considered too important of an initiative to sacrifice key components of the program, and the family considered a 12-month delay an acceptable trade-off.

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What are other ways families maximize participation, interest and cohesion? In our experience, values can serve as unifying principles—or focal points—to engage not just the next generation, but all generations. Identifying personal tenets is critical, but uncovering the principles of other family members and those involved in the philanthropic mission matters just as much. Once identified, families must communicate their values to other members, surfacing both shared ideals and distinct divisions. In doing so, they can learn to appreciate commonalities among members while respecting unique differences. For example, G1 may feel compelled to redirect resources to support COVID-19 efforts, such as frontline healthcare workers. G2, on the other hand, sees a greater need to address the disproportionate burden on underserved communities. Reconciling these viewpoints can help shed light on the values each party holds dear: G1 obligation and community; G2 equality and freedom. Senior generations with a long-established approach to philanthropy might have concerns about the direction younger generations might take once they assume greater control. In our experience, communication and governance hold the keys to a successful transition.

Role of Philanthropy

Today's environment has laid bare the vital contributions many organizations make in addressing today's greatest social, economic and health concerns. It's also highlighted the corresponding need for funding. As one interviewee so eloquently stated, "Philanthropy plays an important role during 'tinder box' times, and now is the perfect time for foundations to step up." While today's challenges seem vast, we've seen them inspire and ignite the passion of family offices and foundations. Across the board, donors are demonstrating thoughtfulness and creativity in maximizing their philanthropic impact—rising to the occasion in new and different ways. Ultimately, philanthropy remains deeply rooted in values, whether for a single donor or multiple generations in a family. While each family may define legacy differently, it'll view philanthropy as one of its most important pillars.

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Endnotes

1. Internal Revenue Service Publication 3833 sets forth the circumstances under which a private nonoperating foundation may provide disaster relief assistance to individuals without advance IRS approval. On March 13, 2020, President Trump declared a national emergency in response to the COVID-19 epidemic, which makes COVID-19 a "qualifying disaster" for purposes of such grants.
2. For purposes of this article, "partnership" refers to any joint activity pursued by a nonprofit and a for-profit. These relationships can take many forms, including (but not limited to) joint ventures, licensing agreements and formal partnerships.