This Executive Summary provides highlights from Foundation Source’s 2013 Annual Report on Private Foundations.

The complete report can be downloaded at www.foundationsource.com.

About Foundation Source

Foundation Source is the nation’s largest provider of comprehensive support services for private foundations, bringing unparalleled knowledge and expertise to clients across the country. The company’s administrative services, online foundation management tools, and philanthropic advisory services provide a total outsourced solution for private foundations. The result: better-run, more effective foundations and more enjoyable philanthropy. Our clients supply the funds, the vision, and the philanthropic goals; we provide everything else.

Today, Foundation Source provides its services to nearly 1,200 family, corporate, and professionally staffed foundations coast to coast, ranging in size from $250,000 to over $500 million. The company provides its services directly to philanthropically focused families and institutions as well as in partnership with the nation’s leading private wealth management firms, law firms, and accounting firms. Foundation Source is headquartered in Fairfield, Connecticut, with auxiliary locations in Atlanta, Chicago, Dallas, Denver, Los Angeles, New York City, Philadelphia, San Francisco, South Florida, and Washington, D.C.
Of the more than 86,000 private foundations in the U.S. today, 98% of them have assets of less than $50 million and 60% were created in the last 15 years. Yet what we know about foundations is mostly based on studies of only the largest foundations, many of which have been around for decades. In fact, the most commonly cited studies are based only on the largest 10% of the foundation community. The rest, the supermajority, are little studied even though they contribute significant support for charitable programs domestically and internationally.

Given the paucity of information on this sector, we felt that the philanthropic community, professional advisors, and the media would welcome a different kind of report. After all, in what other field of study is the center of the bell curve defined by the relatively few outliers at the edges of the graph? As the country’s largest provider of administrative and advisory services for private foundations, we are uniquely poised to provide both data and analysis on this understudied foundation sector. Our study sample consists of 732 private foundations, a representative sample of the broader community of U.S. foundations under $50 million. Moreover, our information is timelier than previous reports because our data is based on actual transactions conducted by our private foundation clients as they occur, rather than waiting years to obtain data from previous tax returns.

Our first Annual Report, released last year, spanned the years from 2008, at the beginning of the Great Recession, through the end of 2011. It yielded information that challenged long-held assumptions about “the other 98%” of private foundations in the United States. We learned, for example, that the private foundations in our study gave significantly more than required by law, proving that the so-called “5% payout requirement” is just the starting point for the vast majority of foundations. We also found that foundations did not curtail their giving during 2008 and 2009, despite the pressure on their endowments from diminished or non-existent investment returns. In fact, the total value of their grants increased 4.5% between 2008 and 2011. To continue to meet their philanthropic goals, donors replenished their foundations’ capital, donating 88 cents for every dollar granted to a nonprofit or paid as a charitable expense. They also shifted their investment portfolios. Cash allocations fell; fixed income allocations rose; and the number of mid-sized foundations (assets of between $1 and $10 million) using alternative asset strategies as part of their diversification strategy increased from 41.6% at the end of 2007 to 60.1% at the end of 2011.
From the CEO

Our second Annual Report continues this research with a snapshot of 2012 private foundation behavior. As we gathered data for this report, we asked ourselves whether the above trends would continue. Would the nation’s fragile economic recovery alter the giving behaviors exhibited by our client foundations? Would the rate at which they replenished their foundations’ endowments return to pre-recession levels? How might the renewed vigor in the stock market affect their investment strategies? The answers, contained in the following pages, may surprise you.

To help us contextualize our findings and assess their significance, we submitted our report to a Reviewers Panel, an acknowledged group of private foundation experts. The panel offered constructive feedback and a needed outside perspective. We thank Sharna Goldseker, Tony Mayer, Kathryn Miree, and Phil Shaffer for their investment of time and effort, ensuring the utility and value of this report.

In extending this spirit of thorough and thoughtful external review, I invite all of you to provide feedback and comments either on our website, our Facebook page, or directly to my email address listed below. Your input will help ensure that we’re able to improve upon this report in every subsequent edition.

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At Foundation Source, we are actively engaged in every aspect of our nearly 1,200 private foundation clients’ programs, administration, and governance. This gives us a truly unique opportunity to observe their activities, and to identify and report on aggregate patterns of behavior and emerging trends in near-real time. The following findings are based on our review of the specific transactional details of 732 private foundations throughout the 2012 calendar year.

Last year, we presented our analysis of how foundations with assets below $50 million behaved during the four years of economic distress, 2008 through 2011. Previously, most of the research on private foundations had focused on the billion-dollar “mega” foundations. Our study provided unexpected insights into the vast majority of foundations that make up the foundation community. Many of these findings contradicted commonly held assumptions about all foundations, regardless of size.

While studies of the largest foundations are important because of the tremendous resources and influence such foundations have, they are necessarily imperfect in explaining and predicting how the vast majority of foundations operate. The more we have studied foundations with assets below $50 million, the more we realize that what’s true of the broader sector is not necessarily true of larger foundations, and vice-versa. For example, the headline of a Chronicle of Philanthropy article published on March 18, 2012, warned that, “Big Grant Makers Don’t Expect to Increase Giving in 2012.” In the article, The Chronicle reported that the vast majority (68 of 96 foundations surveyed) predicted that they would give no more in 2012 than they had in 2011. We expect that these predictions will turn out to be accurate. After all, they were made in March, after most foundations had set their grant budgets for the year. However, as you will see from our data below, the foundations in our study behaved quite differently.

With last year’s study, we established that foundations with assets below $50 million do not behave exactly like their larger counterparts. However, because our study tracked their behavior during the four years of the recession, 2008 through 2011, we wondered whether the same trends would persist during a milder economic climate. This year’s report looks at the same general segment of the foundation community, and finds that in 2012, these foundations were strong, growing in size and impact, and contributing even more to their communities than in years past.
What we found is that in the aggregate, these foundations:

- Maintained a consistently high rate of charitable spending, distributing an amount in excess of 10% of the previous year’s average asset balance. This is more than double the amount that foundations are required to distribute by law;
- Increased their grantmaking in 2012, both in terms of the number of grants awarded and the total value of all grants made;
- Continued to receive new contributions from their donors that supplemented their investment gains and helped fuel their charitable work;
- Grew in size, adding roughly 10% to their net endowment balances from the beginning of the year, even after spending on grants, charitable programs, and expenses; and
- Had significantly stronger investment returns in 2012 than they had in the previous year.

In 2012, these foundations fared better in every category that we analyzed relative to the previous year. Grantmaking increased, both in terms of the number of grants given and the total overall value of those grants. Foundation investments produced significantly stronger returns in 2012 than they had in the previous year. Donors also increased their contributions to their foundations, increasing overall endowment balances at the end of the year relative to where they started in January.

To some extent, these findings reflect an improving economy, with the Dow Jones Industrial Average finishing the year up 7.2% from where it began, and the S&P 500 climbing 11.7%. Yet, during the year, when foundations were making decisions about what grants to make, those results would have been hard to predict and were anything but certain. Concerns about the future of the economy and a potential return to recession persisted throughout the year. As the year drew to a close, apprehension about the so-called “fiscal cliff” and what dramatic, across-the-board government spending cuts might portend for the economy created an environment of uncertainty and fiscal restraint in many sectors. The fact that foundations not only increased their giving, but also increased their endowment balances over the course of the year, is a good indication of the health, vitality, and persistence of this sector.
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Major Findings

Finding: Foundations Increased Their Giving
The 732 private foundations in our study group gave 9.2% more in 2012 than the same group awarded in grants in 2011. In 2012, they gave $215.7 million in the aggregate compared with $197.5 million in 2011. Not surprisingly, the total number of grants awarded increased as well, with the foundations in the study group handing out 17,313 grants in 2012 compared to 15,899 the previous year, an 8.9% increase.

Finding: Foundation Endowments Grew
Overall, asset balances increased for foundations in the study group by 10%. In the aggregate, assets held by the 732 foundations in our study grew from $1.9 billion at the end of 2011 to $2.1 billion by the end of 2012. This was a significant improvement over 2011, when aggregate assets for the same group of foundations fell by 1.6%, with market losses and spending outpacing new contributions to foundation endowments. As noted previously, asset growth was not the result of reduced grantmaking, but was fueled by both improved investment performance and a substantial increase in new contributions to the foundations by their donors.

Finding: Distributions Greatly Exceeded Payout Requirements
Distributions, including both grants and expenditures for charitable programs and administration, were more than double the legally mandated 5% of average asset balances. Specifically, foundations in the study group distributed an amount equal to 11.7% of the average value of their assets over the course of 2012—up from a distribution percentage of 11.2% for the same foundations in 2011. In last year’s report, we determined that foundations with assets below $50 million consistently distribute more for charitable purposes than they are legally required to. This year’s report confirms the continuation of this trend.

The trend of exceeding payout requirements is particularly noteworthy in the context of the previously noted 10% increase in assets in 2012. Because the distribution requirement is based on a percentage of each foundation’s endowment, as assets increase, outlays must also increase proportionately to keep pace. The fact that the distribution percentage increased over 2012 means that the relative rise in charitable expenditures not only kept pace with the endowment growth, but actually exceeded endowment growth over the same period.
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Finding: Increased Giving and Asset Growth Fueled by New Contributions
How were the foundations in this report able to increase the amount of grant support they awarded in 2012 and finish the year with more funds then when they began it? The answer is that donors added new funds to their foundations. In 2012, foundations in the study replenished their endowments by adding $1.06 for every dollar of spending (granting and charitable expenses). That’s up from 93 cents contributed to the foundation for every dollar of spending in 2011.

Finding: Asset Allocation Remained Stable in 2012
In last year’s report, we noted that the foundations in our study group appeared to have moved from equities into cash and alternatives at the beginning of the recession, and had slowly begun returning to their traditional asset allocation formulas by 2011. Throughout 2012, asset allocations across the foundations in this study remained almost unchanged, suggesting that the rebalancing of portfolios during the recession normalized in 2011 and remained stable in 2012. The only movement (marginal) was from alternatives (down 1%) to equities (up 1.7%). Allocations to cash were flat, moving only 0.1% from 16% of all assets held by foundations at the beginning of 2012 to 16.1% of total assets by the close of the year. Fixed income holdings were also essentially flat, comprising 23% of all holdings at the beginning of the year and 22.2% by the end. In fact, allocations to different investment classes were so flat that it is impossible to determine whether the minor changes that we observed represent actual, deliberate movement from one class to another, or are simply the product of normal fluctuations in value of the assets held in each class.