PERSONALIZED PHILANTHROPY

Fixing the Flaw in Your Business Model

By Steven L. Meyers, PhD

The gift design strategy embodied in personalized philanthropy is a holy grail for charities and fundraisers. Yet it should also motivate financial and estate advisors, for several reasons. Personalized gift design awakens the possibility that donors’ philanthropic impact and recognition can begin now, allowing “giving while living,” which clients may find more satisfying than gifts that must be deferred until death. Such a strategy also can be tailored so that it poses little risk to and may even increase assets under management.

Many wealthy donors cannot make the larger gifts they would like to establish during their lives. Even (or especially) if they have the capacity, they would insist on a lever to build on that advantage. The “killer apps” of personalized philanthropy accomplish this alchemy by leveraging the concept of endowment spending rate and creating a radical rethinking of endowment. Killer apps are game-changers because they are individually tailored gift designs that can mesh donors’ compelling interests with charities’ most compelling needs. They serve the donors’ passions ahead of fundraisers’ narrow campaign silos by drawing on the full spectrum of philanthropic building blocks and encouraging donors to target their gifts for greatest impact. This article describes how this leveraging technique works, suggests its implications, and reveals how personalized philanthropy can fix inherent flaws in the financial and investment manager’s business plan that might otherwise make charitable giving a nonstarter.

“Often investment advisors are held back in serving the client’s philanthropy by fear, partly justified, that the gifts to charity, if significant, will come at the expense of assets under management,” said Phil Cubeta, the Sallie B. and William B. Wallace Chair in Philanthropy at the American College of Financial Services.1

This observation exposes a basic but rarely acknowledged truth: The deck is stacked against a financial advisor whose clients want to be philanthropic—especially during their lifetimes. Advisors must balance serving a client’s desire to be charitable and retaining their assets under management (AUM).

Helping clients part with significant assets to favor their charitable causes may be the basis of a good values-based practice, but giving away AUM is just bad business. This article examines ways that both client and advisor can accomplish their goals.

Confronting AUM Fears

It’s common for advisors to fear the loss of AUM to charity, even if those assets go to a foundation that might be managed by the same advisor. Another well-founded fear is that the descendants of the wealth-creator also will depart the advisor. Indeed, a Google search on “Studies show that more than 95% of heirs change advisors after they inherit assets” returns more than 50,000 hits.

So the parting of ways looms with assets under management and with clients under management. The standard business model can only do so much to defer, if not entirely prevent, the exodus.

Fundraisers and financial advisors share these concerns, which are like a sword of Damocles hanging precariously over both (see figure 1). For financial advisors, the concern is labeled and familiar as AUM. For fundraisers, it’s labeled and familiar as “financial resource development”—also known familiarly to fundraisers as FRD—the one-number metric that translates as “How much did you raise?”

Many advisors are taking up client-focused specialized practices and collaborating with other professionals to serve client families and wealth creators. Under this approach, wealth is more than money. Clients and their families are considered with a more holistic and multidimensional approach. A trusted advisor (and there may be more than one) may lead a team in a purposeful fusion practice, gathering around the table with a lawyer, banker, money shrink, and philanthropic gift officer, all in the interest...
of serving a client’s interests. But even this enlightened practice shares the common flaw of the original business model: Divesting client assets, even for charitable giving-while-living, is not consistent with advisor prosperity.

Personalized Philanthropy and the Leading-Edge Business Model

A different model may be better-suited for advancing philanthropy while supporting a philanthropic client’s advisor. “We are on the cusp of a major historical opportunity to help boomer business owners in transition from success to significance, and also greatly increase and retain assets under management,” Cubeta said.

Under the conventional model, financial planners tend to discourage the divesting of assets to be managed by charity. Under the personalized philanthropy model, planners themselves have the opportunity to manage and control vehicles from which charitable funds are dispensed. Using personalized philanthropy’s killer apps, the charitable funds are delivered to the charity in a staged and intentional manner.

The goal is to connect the social capital of the client, which comes from good planning, with the societal impact that comes from the client’s connection with engines of philanthropy—the causes that work on the issues the client cares about most deeply. The staging and distribution strategy makes the difference.

Killer Apps

The vehicles of personalized philanthropy are sometimes described as killer apps. They dramatically shift the focus from the institution to the donor, with respect both to how gifts are created and how donors are engaged. The impact of the resulting gifts—which begin “now”—make conventional gift planning appear hobbled and dated.

These personally designed gift applications or killer apps allow donors greater impact and recognition during their lifetimes than would otherwise be possible. The killer apps are actually flexible endowments variously named “virtual endowments,” “philanthropic mortgages,” and “step-up gifts” (see table 1). They use familiar building blocks of philanthropy staged over time and combine current and future gifts in novel ways. Each strategy leverages the power of spending rate to accomplish the gift.

Three Personalized Gift Designs—From the Advisor’s Perspective

Discussion of the full impact of personalized philanthropy is beyond the scope of this article. Cubeta, however, is convinced that it can make a difference in the practices of financial and investment managers.

“Instead of making a huge gift, for an endowed program, and having the charity hold the principal and spend the income (“the spend rate”) on the program, the newer idea is for you—the advisor—to hold the money and dole it out in stages and installments, as the work is performed,” Cubeta said. “Rather than give the charity the whole lump and trust it in perpetuity, we pay it as they go along.”

Three Personalized Gift Designs (or Killer Apps)

Virtual endowment. In a virtual endowment, a donor chains together a series of current gifts to maintain a program with a future gift such as a bequest, providing what might be called a “ballot payment” in the financial-services industry, is made to fully fund the endowment.

Philanthropic mortgage. In a philanthropic mortgage, a donor’s annual gift commitment covers the endowed program but includes additional money to gradually build “equity” in an endowment or legacy fund until it’s fully established.

Step-up Gift. Donor establishes a gift at a starting level, then adds to it (usually through a bequest or other balloon payment) to increase the impact.

Table 1: Three Personalized Gift Designs

<table>
<thead>
<tr>
<th>Killer App</th>
<th>Description</th>
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<tr>
<td>Virtual Endowment</td>
<td>Donor commits to a series of gifts that covers the annual spending of an endowed program or chair. A future gift such as a bequest, providing what might be called a “ballot payment” in the financial-services industry, is made to fully fund the endowment.</td>
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The following are two examples of personalized philanthropy that have benefited the Weizmann Institute, the donors, and their advisors. Each uses a killer app to allow the donor to initiate the gift (and its impact) at once and then endow it for posterity.

A Virtual Chair for the Chair Emeritus—Funding the Future of Science Today

This longtime leader and financial supporter of the Weizmann Institute, a financial advisor himself, had been a mentor to the rising generation. He had strategically directed his philanthropy to support creative individuals pursuing art, science, and business, even before they received public acclaim. Now this donor and his wife wanted to bring this same passion and creativity to crafting their philanthropic legacy.

The donor had known for years that his individual retirement account (IRA) would be an ideal funding source for a lasting legacy. He had chosen to create a career development chair because it would help the institute recruit the most talented new scientists and provide them with a substantial start-up package for equipping their laboratories until they were established and able to apply for competitive grants. Career development is a core and continuing need for Weizmann, and a compelling interest for the donor and his family.

The donor couple was assured that the bequest from the IRA would endow the career development chair in the future but wanted to find a way for the science to go forward now, rather than after their demise. By providing gifts to cover the annual spending that the endowment would provide later, the chair could begin now. The annual gifts would be the virtual equivalent of what eventually would be supplied by the endowment. The donors decided to direct that their annual gifts be used to advance science research now. This was an ideal solution, because they were able to execute gifts they already had in mind and have greater impact, starting at once.

During its early years, this career development chair will be supported by annual gifts in the donors’ names; during future years, it will be supported by spending from the endowed bequest. The donors will enjoy enhanced impact of their philanthropy now and know that the future estate gift will assure their meaningful and lasting legacy.

Note: Under the new permanent charitable rollover, IRAs are more versatile than ever. Donors may designate their required minimum distributions as the annual/expendable component for a virtual endowment; they also may direct that the remaining assets in the IRA be used to establish the corpus of the endowment. In this way, a virtual endowment becomes a true endowment.

The Power of Personalized Philanthropy for Having It Your Way

This donor’s story highlights the power of personalized philanthropy. He is an engineer and computer scientist and likes to do things his own way. He enjoys the creative fashioning of numerous “iterations” that is inherent in any kind of design process. Each iteration brought him closer to achieving his goal, his way.

At religious services one holiday, he realized it was now or never for him to plan his legacy. “As someone who loved science and Israel, the Weizmann Institute was a natural for me,” he told me. He found us on the web, including our personalized philanthropy page. He then researched ways to give, what to give for, and how to shape his plan.

He sent us an e-mail asking us to call him about a gift, but at that point he was still exploring. He was retired, but his income was still increasing, and he had amassed an estate that he had no plan to spend.

He became enthusiastic about an ambitious goal: the idea of supporting the entire arc of a scientist’s career. His task then became to create an estate plan that would provide for a doctoral scholarship, a postdoctoral fellowship, a new scientist career development chair, and finally the capstone, a professorial chair. This took 10 months.

That was just the beginning. This donor was not done. He had read about the customized personalized approaches to giving that we call “killer apps”—approaches such as virtual endowments and philanthropic mortgages. He explored these ways of starting his gift now, and realized he could begin by creating a postdoc in memory of his parents.

To fund the postdoc with an outright contribution would cost $350,000. That was out of the question. The alternative he settled on was a philanthropic mortgage. In this arrangement, as an alternative to an outright contribution to pay for the project, the donor makes payments over a number of years. In most pledge agreements, the program (in this case a postdoc) would not commence until the gift was fully paid for, or nearly so. However, with this mortgage-like arrangement, each payment covers both the annual costs needed to operate the program and an additional amount, which builds equity in an endowment until it is fully funded.

Our donor decided on five payments over five years. As noted, the first four payments covered the annual maintenance of the postdoc plus an extra amount that goes to build equity until the postdoc’s cost is fully paid.

The fifth and final payment was a larger amount, a balloon payment. It happens that in the final year, the donor will need to begin taking a required minimum distribution (RMD) on his IRA savings. The annual RMD will be a big lump sum he won’t need. He decided to apply it to the postdoc. So in five years, the postdoc will be fully funded and sustainable for the future.

With the postdoc just about up and running, our donor is now taking about funding the professorial chair with an amount set aside in his will. By the time he finishes paying the five-year philanthropic mortgage on the postdoc, he may be ready to keep the contributions coming and start the chair during his lifetime. In fact, to be sure the chair is established one way or the other, he already has made a pledge commitment to fund the chair through his estate plans.

Our benefactor recently shared with us his thoughts about his gift: “I was able to formulate a strategy that meets my goals optimally and coincidentally matches well with your description of personalized philanthropy,” he wrote. “I am not young enough to have time to slowly build up equity and not old enough to depend solely on bequest pledges. So I am very satisfied with the donation structure that we have chosen. Now, I cannot wait to hear from the first Fellowship recipient.”
than that needed for maintenance of the program. The surplus amount is used to build equity in an endowment or a legacy fund until it is fully established and able to sustain the program. This is the same idea as building equity in your home.

**Step-up gifts.** With step-up gifts, a donor establishes a gift at a starting level then steps it up. The impact begins now and scales up over time (e.g., grows your support from a master’s scholarship to a doctoral scholarship to a professorial chair).

**Endowment and Spending Rate**

Endowments generally are funds in which the principal is expected to remain intact and the investment income is used for charitable efforts. Donors can express specific preferences for the use of the funds, leaving ultimate discretion to the organization. Charities usually designate a spending rate as a certain percentage of the assets to be used each year, which also may include interest and principal as necessary to fulfill that purpose.

A donor can support a mission by making contributions that are to be expended immediately, making a major gift outright during a special campaign, or making a planned gift through an estate plan. But often an institution’s most highly valued source of future support comes from endowment or endowment-like gifts. Indeed, an endowment is like a machine for producing annual support. Endowments are not established through planned gifts such as bequests or charitable trusts, but they also can be funded with outright or major gifts.

In the conventional fundraising and development office, the link between current and future fundraising doesn’t exist. Donors are divided into channels for annual, major, and planned gifts. The connection between current dollars and future dollars often is never established.

**The Personalized Philanthropy Breakthrough**

Personalized philanthropy is a rethinking of endowment, which leads to a rethinking of capacity—the donor’s ability to provide a charitable contribution. In the philanthropic and financial planning context, “capacity” usually means the donor’s ability to transact a complete gift at a given moment in time. When you think of capacity as the lifetime value of a donor, you effectively reformulate the traditional value chain of philanthropy. The value chain no longer has to be thought of exclusively as a one-way pipeline, with the value all coming out at the end. Gifts can be designed and planned to access the value, intentionally, at a time of a donor’s choosing.

Personalized philanthropy is a cascade of strategies that establish or restore the connection between current and future giving. A donor’s greatest impact no longer must occur only at the end of the chain, the donor’s death. Rethinking endowment results in a clear view of the donor’s big picture over a lifetime of giving. It allows us—as both gift advisors and financial advisors, or perhaps a fusion of both—to access the entirety of a donor’s capacity and devise new kinds of gifts that can bridge the gap between current and future dollars. That means we can target and design gifts that can meet an organization’s needs.

**The Underestimated Power of Spending Rate**

Each killer app leverages the power of the spending rate, which is the percent of the corpus of a gift that can be expended annually to support a program.

The goal is to create a stream of annual revenue to sustain a program. It may not be possible to obtain the corpus initially; it may be easier to provide a stream of annual gifts in a decisive and intentional way.

**The Grail of Fundraising**

By focusing on the stream of annual gifts first, programs can be established that otherwise would never see the light of day. These gifts can start having impact right away and scale up over time. You can stage a gift over time that can be transformational for both donor and institution—one that would not be possible to even imagine if approached as a single or unconnected transaction. That’s the grail of fundraising.

For example, a traditional endowment of $100,000 with a 5-percent spending rate produces $5,000 of spending annually. Many more donors can give $5,000 per year than can give $100,000 as a lump sum. Thus even modest annual gifts, in the context of lifetime and estate giving, can have all the impact and power of major gifts.

**Conclusion**

The benefits of personalized philanthropy as a discipline of fusion and collaboration cannot be overstated. Virtual endowments, philanthropic mortgages—the innovative game-changing killer apps of personalized philanthropy—already are building a bridge that spans and unites the practices of philanthropic and financial planners.

Finally, here’s a way to more fully align our advising practice with the philanthropic aims of our donors and clients. Not only for the benefit of our business models but for the benefit of humanity.

If the annual spending commitment precedes the formal establishment of the endowment, then who is to say that is not just as valuable as having the endowment itself? Take a look at personalized philanthropy, and then take another look at your business model.

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**Endnote**