

 SECTIONS COMMENTARY: ENDOWMENTS ARE FINANCIAL PILLARS, NOT PIGGY BANKS

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Endowments Are Financial Pillars, Not Piggy Banks



Michael Morgenstern for The Chronicle

By *David Oxtoby* | SEPTEMBER 21, 2015

Like many other college presidents, I've seen good financial times and bad. And I've experienced the tremendous benefit, in any economy, of having endowment resources that guarantee, first, that our college will

have a future, and second, that we can continue to enhance our value and service to our students, faculty, community, and nation.

Yet these essential tools for fiscal management in higher education are once again under fire as our nation grapples with the growing cost of a college education. There is renewed pressure to force colleges with sizable endowments to spend more, and increased talk about revoking their tax-exempt status. These attacks on endowments reveal both an extremely short-term outlook, and a fundamental misunderstanding of what they do and how they work.

Endowment funds provide scholarship dollars for students and allow colleges to expand student access and diversity. They help ensure that support for faculty teaching and research remains a long-term institutional priority. They support libraries and other facilities, public service, and student success and retention programs. At my institution, Pomona College, our endowment provides funds to commit to need-blind admissions by meeting 100 percent of a student's demonstrated need. It has enabled us — and our peers — to enroll incredible young men and women who will do great things.

So why are our endowments getting such a bad rap? They have been attacked by higher-education critics, politicians of all stripes, and others who are just plain frustrated by rising college costs. The bigger the endowment, the bigger the target, and the easier it is to make comparisons and draw conclusions that spark outrage but contribute nothing to understanding and reasonable discussion. For example, putting aside part of an endowment to grow for the future becomes "hoarding" — even if it actually means that we will be able to provide tuition benefits to greater numbers of students.

Political scrutiny of endowment structures and spending first surfaced in 2008 when the Republican and Democratic leaders of the Senate Finance Committee at the time, Sen. Chuck Grassley of Iowa and then-Sen. Max Baucus of Montana, wrote to the 136 colleges with endowments of \$500 million or more asking questions about endowment growth and student aid. Rising college tuition was the impetus, along with a concern expressed in the letter that tuition relief should be growing as fast as endowments. Fast forward seven years, and some old ideas have re-emerged, such as taxing college endowments and/or requiring all colleges with endowments to spend at least 8 percent of the total annually, as Victor Fleischer recently suggested in *The New York Times*. The big targets are the big universities with big endowments, but the proposed solutions betray a lack of understanding of actions and consequences.

College endowments may be simple in concept and structure, but they are often complicated in the details. A review of some of the basics of endowments — whether at Pomona, with an endowment of \$2.1 billion, at Harvard and Yale, with endowments topping \$20 billion, or at the great majority of private colleges and universities in this country, with a median endowment of \$7.9 million — can offer some clarity and common sense.

First, endowments are not one fund but multiple funds — generally contributions, large and small, from donors that may include alumni, corporations, and foundations. Most of these gifts come with very specific donor-directed purposes and restrictions on how they can be spent. A recent survey from the Council for Aid to Education shows that 73 percent of endowment income goes to restricted purposes. A recent NACUBO-Commonfund Study of Endowments reports that 90 percent of new gifts are restricted for a specific purpose by the donor.

Second, some share of the investment returns must be reinvested to cover the future costs of programs created by endowment funds. Mandating increased payments would put the long-term support for these programs at risk. Prudent use of investment returns allows these individual endowment funds to support the donors' wishes on an annual basis while protecting and increasing the principal value of the gifts to support future students and faculty. Forced payouts could actually drive tuition up, not down (as mandated-payment advocates contend).

As we learned in the 2007-8 recession, and as recent worldwide economic volatility reminds us, markets go up — and down. Colleges need the freedom to spend a smaller percentage in good times so that we can build up the value of the endowment to be able to support long-term programs in bad times. When markets drop, we need, if anything, the flexibility to spend even more to provide aid to students and their families. Mandating specific payment rates will hold annual institutional budgets hostage to serious market volatility.

Third, rising investment returns are a good thing for colleges, students, and parents. They create more immediately available support for numerous projects, as well as for controlling tuition costs and raising financial aid. In fact, private four-year colleges and universities dropped net tuition prices over the past decade by 13 percent. Grant aid per full-time equivalent student at private four-year colleges increased 5.9 percent between 2012-13 and 2013-14 (data for 2014-15 will be available in January) — more than the inflation rate of 1.47 percent for 2013 and 1.62 for 2014.

Fourth, undermining the tax-exempt status of endowments, either by limiting the deductibility of contributions for donors or changing the status of endowments, would reduce — in some cases, drastically — charitable contributions to higher education. At a time of steadily declining financial support from states for higher education, this is an especially frightening prospect. It's also worth noting that universities in countries without the American endowment model rely heavily on government appropriations. With less state support, would the federal government be prepared or willing to fill the gap? And, if so, with what consequences?

Endowments succeed when they are able to do what they are supposed to do: support the full mission of the institution, today and far into the future. Weakening them to meet immediate needs, with no regard for tomorrow's,

is a threat to higher education in this country, and, consequently, to our nation's future.

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