Frequently Asked Questions: Agency Funds

TFEC and our regional foundations hold a number of endowments for charitable organizations. These endowments offer nonprofit agencies the benefits of marketing, development and legal services, professional investment oversight, an excellent investment performance record, and a spending policy that assures a stable annual flow of grant dollars to the organization. The questions below are frequently asked about Agency Funds at TFEC.

FAQ1. What are the types of funds that can benefit an Agency?
Answer: There are three possible types of funds held on behalf of an agency, and the answers to all of the questions noted below may be different, depending upon the type of fund. All FAQ answers when appropriate use the breakdown of A, B, C where answers are different based on the type of fund.

(A) **The agency's own endowment fund transferred to TFEC:** An Agency Fund is a fund established by a nonprofit organization to assure its long-term fiscal health. Generally, these funds are established using assets under the control of the governing body of the organization. Individuals, corporations, or other donors may also contribute to such funds.

(B) **Donor established restricted fund that benefits the agency:** A Restricted Fund established by a donor provides ongoing, permanent support to one or more donor-selected agencies. In essence, this fund enables donors to endow their annual gifts to their favorite charity(s).

(C) **A planned giving vehicle such as a CRT or CLT established by a donor to benefit the agency: CRT –** Donors transfer cash or property *irrevocably* to the Trust, which then invests the assets and creates two interests. The <u>income interest</u> is given to non-charitable beneficiaries (usually the donor, but sometimes other designees). Upon the death of the income beneficiaries, or after a specified period of years, the <u>remainder interest</u> is then distributed to TFEC for creation of a named endowment fund, or contributed to an existing endowment fund. **CLT –** The <u>income interest</u> is given to a TFEC charitable fund, which receives payments during the life of the donor, or for a specified term. The income is used to establish a named endowment fund, or is added to an existing endowment fund. Upon the termination of the trust (i.e., the death of the donor or after a specified period of years), the <u>remainder interest</u> is paid to the donors or to other non-charitable beneficiaries (typically heirs).

FAQ2. Who controls the use of the income from the fund?
Answer: Unless a specific use is identified in the documents that establish the fund, the governing body of the agency may use the income for any purpose. Sometimes, funds are established with specific purposes stated such as building maintenance or continuing education for employees. In such instances, the income must be used in accordance with the specific designation and the organization will be required to certify the use of the funds to TFEC.

FAQ3. TFEC's materials indicate that an Agency Fund should be considered a permanent endowment. Is this correct?
Answer: Yes. A fund established by an agency, which is also the recipient of distributions of that fund, must be a permanent endowment. Otherwise, the fund could be considered as a vehicle for short-term investments and TFEC is not permitted to act as solely an investment advisor or portfolio manager for the donor organization.

FAQ4. Is it possible for the agency to retain ownership of the assets held in the fund(s) at TFEC? If so, are there certain provisions that must be followed to allow this ownership?
Answer: Because the donor (e.g. agency) is also the beneficiary of the fund, the legal ownership of the funds must belong to TFEC. However, please refer to FASB 136 explanation (below in FAQ 7) regarding financial reporting options.

FAQ5. What, if any, are the circumstances in which an agency would not maintain ownership of an asset gift?
Answer: In order to operate as a part of TFEC and avoid private foundation status, the legal owner must remain TFEC.

FAQ6. If, at some future date, the board of the agency wished to transfer the assets from the agency fund to another financial institution, is that possible?
Answer: TFEC has established an investment policy based on low-cost index funds and enhanced index funds. When assets are transferred in kind, the Investment Advisory Committee develops a plan to gradually adapt the fund to TFEC's policy. If an outside financial institution is preferred as custodian, then the institution is expected to adopt TFEC's specific asset allocation model.

If the question refers to removal of TFEC as owner of the assets by way of a distribution to another endowment/investment manager, the answer depends on the type of fund.

(A) It is not our policy or intent to distribute grants from the principal of a fund. Principal may only be distributed upon proof of dire need. TFEC's by-laws allow its Board of Directors to distribute principal, up to the entire fund balance, upon proof of dire need by request. Recommendations for distributions of the fund's principal shall be in writing to the Board of Directors of TFEC and shall contain a copy of the agency's board authorization indicating that the request is made with the approval of the then board of directors of the agency. The Bylaws of TFEC state that if circumstances have so changed as to render it unnecessary, undesirable, impractical or impossible to comply with the terms of the fund agreement, then TFEC's Board of Directors may authorize grants from principal. Such an authorization requires a request in writing from the agency, and an affirmative vote of two-thirds of the members of TFEC's Board of Directors. The request must contain a description of how and for what the grant will be used within the TFEC general grantmaking guidelines. Second, the request needs to provide sufficient information and detail to show that the need for the principal grant is extraordinary and not expected to occur on an ongoing basis. Third, the request needs to be accompanied by a history of fiscal responsibility which indicates that grants from principal will not be needed on an ongoing basis.

(B) A donor established restricted fund's assets remain the assets of TFEC.
(C) CRT's and CLT's remain the assets of TFEC.

FAQ7. How does my agency report the assets held at the TFEC (i.e., what is reported in our financial statements vs. TFEC's financial statements)?
Answer: Accounting rule FASB 136 requires that any funds contributed by the agency itself to the fund shall be reported as an asset on the agency's balance sheet and a liability on TFEC's balance sheet, although they remain the legal asset of TFEC. Any funds contributed by any donor to the fund to benefit the agency shall be reported only as an asset of TFEC. TFEC maintains two separate funds within each Agency Fund to permit accurate accounting practices to meet the aforementioned stipulations of FASB 136.

FAQ8. What flexibility does an agency have with investment choices (e.g., can more than one of the TFEC investment models be chosen to achieve an overall investment strategy of 60/40 equity/fixed income)?
Answer: There are four different investment funds offered by TFEC. Assets may be invested in one or a combination of the four funds as desired. They include:

- Model E 100% Equities
- Model A 70% Equities, 30 % Fixed Income
- Model F 100% Fixed Income
- Model M 100% Money Market

FAQ9. If this flexibility exists, how often can the selected option(s) be changed?
Answer: Upon request, typically once per year. Funds are valued at market monthly.

FAQ10. Can an Agency have more than one "fund" within the fund account? For example, could there be a general fund for unrestricted gifts, and one or more special interest funds for donors who wish to direct their gift for a specific use (e.g., to cover operating expenses, to endow a gift for the annual campaign, etc.)?
Answer: Yes, an Agency Fund may have as many sub-funds as requested. Not all special interest sub-funds need be established at the fund's inception, additional sub-funds may be added at any time.

FAQ11. Can TFEC assist an agency to accept and manage complex gift vehicles such as Charitable Remainder Trusts, Charitable Lead Trusts, real estate, etc.?
Answer: Yes. TFEC currently administers and invests more than forty CRT's and CLT's. TFEC accepts nontraditional assets of stock, closely held business stock, real estate, antiques, fine art, and collections – any asset that may be appraised in value. TFEC serves as the Trustee of the CRT or CLT. The donor receives the income of the CRT and upon maturity; the proceeds would be added to the specific fund designated by the donor. For a CLT, the organization would receive the annual income and upon maturity, the remaining principal would be returned to the donor.

FAQ12. What are the fees related to these choices and how are they determined?
Answer:
(A) **Agency Fund:** TFEC's annual fees are 0.4% for investment management and 1.45% for administration.

(B) **Restricted Fund:** TFEC's annual fees are 0.4% for investment management and 1.45% for administration.
(C) **CRTs or CLTs:** TFEC's annual fees total 1.0% (0.4% for investment management and 0.6% for administration); fees are reduced for trusts over $500,000.

FAQ13. How will my agency receive its annual income distributions? How will the annual distributions be determined? What flexibility does an Agency have in determining the annual percentage?
Answer: Usually on an annual basis, but can also request quarterly or semi-annual payments, depending on the desire of the agency.

(A) The agency determines the investment model or combination of investment models for its Agency funds. The distributions are determined by the spending policy associated with each type of investment model chosen:
   a. Model E 6.20% less 1.45% administration fee
   b. Model A 5.20% less 1.45% administration fee
   c. Model F 3.00% less 1.45% administration fee

   The spending rates are applied to a five-year blended fund balance to avoid excessive year-to-year fluctuation. If the agency has both general funds and special interest funds, TFEC would indicate how much of the annual distribution was attributable to each area.
(B) The same policies apply to donor established funds, except that Nonpermanent Funds have no required spending policy.
(C) Income payments are determined in the specific terms of the trust.

FAQ14. Will the agency have any restrictions on the use of those funds, other than those imposed by the donor (e.g., special interest fund distributions)?
Answer: No, none at all.

FAQ15. Are these distributions considered "grants" from TFEC? If so, what are the annual reporting requirements?
Answer: Yes, they are considered grants and would be reported as any other grant from a 501(c)(3) nonprofit organization.