Commonfund
Benchmarks Study
of Healthcare
Organizations

CSHO

RETURNS AND INVESTMENT OBJECTIVES
ASSET ALLOCATION | INVESTMENT POLICIES
SOCIAL INVESTING | DEBT | FUND FLOWS
RESOURCES MANAGEMENT GOVERNANCE

2016–2017

2016–2017 **Commonfund Benchmarks Study®** of Healthcare Organizations

Commonfund Institute report on healthcare organization performance and management practices.

Commonfund Benchmarks Study of Healthcare Organizations

CSHO

WELCOME

September 2018

Commonfund Institute is committed to providing industry-leading research and promoting best practices in institutional investment and financial management. The intent of the 2016–2017 Commonfund Benchmarks Study® of Healthcare Organizations is to provide an in-depth analysis of the investment and governance policies and practices of nonprofit healthcare organizations across the United States. Our hope is that you find the Report informative and useful.

The Study of Healthcare Organizations, first published in 2003, was conducted on an annual basis until 2013 with the exception of calendar year 2012. In 2016 we published a report that combined data for 2014 and 2015 and in this year's report we combine the next two years—2016 and 2017.

There have been several editorial changes made since the 2014–2015 Report. First, the executive summary that follows still contains highlights from each chapter, but also an introductory section focused on the major changes indicated by the data since the last Study. Second, each chapter opens with actionable questions that readers may want to keep top of mind as they relate the data to their own institution's challenges and opportunities. Third, recognizing the distinct roles and objectives differentiating investable asset pools and defined benefit (DB) plan assets, we are separating DB plan data into a single section of its own.

A deep expression of gratitude goes to the participating U.S. hospitals and operating health systems. We thank you for taking the time to provide the data that is the heart of this Report.

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Executive Summary
2016–2017 Commonfund Benchmarks Study® of Healthcare Organizations

Summary of Major Findings

- The 13.2 percent 2017 return on investable assets was the highest return since 13.3 percent reported for 2013. (Returns are reported net of fees.)
- Long-term (the trailing 10-year period) average annual returns remain below 5.0 percent (4.6 percent for 2008 to 2017).
- The 2017 investable assets allocation to alternative strategies declined to 25 percent from 28 percent in 2015, continuing the reversal of a trend that reached its high point with an allocation of 31 percent in 2013.
- Allocations in 2017 to U.S. equities and fixed income were moderately higher than they were in 2015 but remain well below the upper 30 percent/lower 40 percent level reported when the Study commenced (for 2002).
- Professional staff devoted to managing the investment function showed an increase among organizations with assets under $501 million, where the average number of full-time equivalent employees (FTEs) more than doubled to 1.1 in 2017 versus 0.4 FTE in 2015.
- Returns on defined benefit (DB) plan assets were higher than those earned by investable asset pools. This may be attributed, in part, to a larger allocation to non-U.S. equities, which performed strongly over the two-year period, and a smaller allocation to short-term securities/cash/other.
- At year-end 2017, 57 percent of participating organizations' U.S. equities allocation was actively managed and 43 percent was passively managed—a clear change since 2014 when the active/passive split was 65/35. This may reinforce observations in earlier Studies concerning the shift to passive management of highly efficient asset classes, such as U.S. equities. The allocation to actively managed non-U.S. equities also declined.

Additional Highlights

Returns

Investable Assets

Returns on investable assets for the 56 nonprofit healthcare organizations participating in the 2016–2017 Commonfund Benchmarks Study of Healthcare Organizations averaged 6.2 percent for 2016 and 13.2 percent for 2017. Returns for both years were higher than those reported by healthcare organizations participating in the previous Study, conducted for 2014 and 2015. Returns for those years were 4.4 percent for 2014 and -1.6 percent for 2015.

All returns in the Study are reported net of fees. "Investable assets" include endowment/foundation funds, funded depreciation, working capital and other separately treated assets.

The double-digit gains reported for 2017 benefited healthcare organizations by improving mission-critical long-term results. For the trailing three-, five- and 10-year periods, reported average annual returns on investable assets were 5.9 percent, 6.9 percent and 4.6 percent, respectively, for 2017. For 2016, comparable returns were lower, at 3.1 percent, 6.5 percent and 4.2 percent, respectively.

DB Plan Assets

The 32 participating organizations that have DB plans realized better returns in 2016-2017 than were reported for all participants' investable asset pools. DB plan returns averaged 7.2 percent for 2016 and 14.9 percent for 2017. For 2016, DB plan returns for the trailing three-, five- and 10-year periods averaged 3.9 percent, 7.3 percent and 4.8 percent, respectively. For 2017, DB plan returns for the same periods averaged 6.6 percent, 7.8 percent and 5.4 percent, respectively.

Asset Allocation

Notwithstanding their different purposes, the asset allocations for participating organizations' investable assets and DB plans showed only modest differences, as reflected in the following table:

	2016		2017	
numbers in percent (%)	Investable assets	DB Plan	Investable assets	DB Plan
U.S. equities	19	22	21	20
Fixed income	31	31	31	32
Non-U.S. equities	19	22	20	24
Alternative strategies	26	24	25	23
Short-term securities/cash/other	5	1	3	1

Alternative Strategies Detail

At both year-end 2016 and 2017, participating organizations' largest alternative strategies allocation among their investable assets was to marketable alternative strategies (hedge funds, absolute return, market neutral, long/short, 130/30, event-driven and derivatives). For 2016, the allocation was 55 percent of participants' overall alternatives allocation; for 2017 it was 53 percent. After that, the largest allocation was to private equity (LBOs, mezzanine, M&A funds and international private equity), at 16 percent and 19 percent for 2016 and 2017, respectively. Private equity real estate accounted for 11 percent of the alternative strategies allocation for both years. All other alternative strategy allocations were 3 percent or less.

A similar pattern held for participating organizations' DB plan assets, with the marketable alternatives allocation standing at 49 percent of the overall alternatives allocation at year-end 2016 and 2017. Private equity followed at 23 percent for 2016 and 31 percent for 2017.

Investment Return Budgeting, Long-Term Return Objectives and Operating Margin

Participating healthcare organizations budgeted, on average, an investment return of 5.1 percent for 2016 and 5.0 percent for 2017. The 2017 long-term investment objectives for Study participants' operating assets was 6.0 percent. Organizations' average operating margin for 2017 was 3.5 percent.

Debt

Thirty-seven percent of Study participants reported having the highest or high investment-grade rating for their bonds; 55 percent reported other investment grade ratings; no organization reported non-investment-grade ratings; and 8 percent gave no answer or were uncertain.

Resources, Management and Governance

Participating healthcare organizations reported employing an average of 2.1 full-time equivalent (FTE) professionals to manage the investment function in 2017. The median figure was 1.8 FTEs. The latter was up sharply from 0.9 FTE in 2015, suggesting increased staff among smaller organizations. The data showed that was, in fact, the case: Whereas organizations with assets under $501 million reported an average of 0.4 FTE and a median of 0.3 FTE in 2015, those figures more than doubled to 1.1 FTEs and 1.0 FTE, respectively, in 2017.

Participants reported using an average of 4.4 investment managers each to oversee their U.S. equity allocation, and an average of 4.5 investment managers to oversee their fixed income and non-U.S. equity allocations. They retained an average of 16.0 managers for their alternative strategies (direct) allocation and an average of 2.6 managers for their alternative strategies (fund of funds) allocation. Compared to the Study for 2015, there was a decline in the number of alternatives (direct) managers used by the largest organizations and those in the mid-sized cohort, but an increase for organizations in the smaller size category.

Twenty-seven percent of all participants said they had substantially outsourced their investment function in 2017, a two-percentage-point decline from 2015. Nearly half of the organizations with assets below $501 million reported outsourcing.

Ninety percent of participants said that they used a consultant in 2017, up from 85 percent in 2015. Asset allocation/rebalancing, manager selection, performance attribution and measurement, and ongoing due diligence were cited as the most frequently-used services.

The average number of voting members on investment committees stood at 7.9 for 2017, up from 7.4 in 2015. An average of 4.3 committee members were investment professionals; an average of 2.7 member had alternative strategies experience; and an average of 2.5 were non-trustee voting members.

Profile of the Study Universe

The 56 organizations participating in the 2016–2017 Study reported an average investable asset pool of $2.1 billion as of December 31, 2017, and median investable assets of $987.0 million as of the same date. For the 32 organizations reporting DB plan market value, the average plan value was $2.0 billion as of year-end 2017, while the median market value as of the same date was $481.0 million. The Study separates data from the 56 participants into three size cohorts: organizations with investable assets over $1 billion; those with investable assets between $501 million and $1 billion; and those with investable assets under $501 million.

HOW TO READ THIS REPORT

Data in the main body of the report are presented for all responding organizations as a whole. In many cases, the data are then broken down and segmented into three size cohorts based on total assets. Those size categories are organizations with total assets:

Over $1 Billion

Between $501 Million and $1Billion

Under $501 Million

All data related to defined benefit (DB) plan assets are shown for the 32 participating organizations with DB plans and are not broken into the three size segments.

TABLES

The tables in the report generally display data in two primary ways. The first is the total number of organizations responding to a particular question. The second breaks this total number of respondents in to three cohorts, segmented according to the size of their assets, as described above. In the tables, each size cohort has its own color coding, which remains consistent throughout the report. The purpose of this approach is to assist readers in locating the size category relevant to their own institution and finding the appropriate benchmark data.

RESEARCH PROCESS AND METHODOLOGY

The design of the 2016–2017 Commonfund Benchmarks Study took place in the fall and winter of 2016–2017. Data-gathering took place in the first and second quarters of calendar 2018 using an online survey instrument. Our sample universe targeted senior staff at healthcare organizations with investable assets of $100 million and more. Respondents were supported by online documentation and a dedicated help desk.

Comparisons of current data to data reported for 2014–2015 are included in the narrative where meaningful changes have occurred. However, we caution users of the Commonfund Benchmarks data that any trend presented in this report should be interpreted only directionally as an indication of change.

Readers interested in data from other areas of the nonprofit sector—Educational Endowments and Foundations—can order those Reports on our website: www.commonfund.org.

ACCESS AND NAVIGATION

Items in the document's Table of Contents can be reached by clicking on the chapter, subhead or page. This is also true of the figures listed on pages iii and iv. In addition, by opening the "Bookmarks" tab in Acrobat Reader, an internal table of contents is revealed, permitting you to easily navigate back and forth and jump from one section directly to another.

FREQUENTLY ASKED QUESTIONS

How are three-, five- and 10-year investment returns for participating organizations calculated?

Study participants provide their own three-, five- and 10-year returns, and we report average responses. In short, these returns are reported, not derived.

What is "dollar-weighted?"

Dollar-weighted means that individual responses are weighted according to size or asset base when calculating average results—meaning that responses from large participants have a greater impact on average results than those of smaller participants. By contrast, when overall results are calculated on an "equal-weighted" basis, each response has an equal impact on the average, regardless of the size of the respondent. Unless otherwise noted, asset allocation figures in this Study are dollar-weighted. Selected tables showing equal-weighted data may be found in Appendix II.

Why do the bases (or number of respondents) change between Figures?

Charts and tables contain one of two column headers: "Total Organizations" or "Responding Organizations." The "Total Organizations" column header indicates that the figure depicts responses from the full set of 56 Study participants. "Responding Organizations" indicates that the responses come from a sub-set of participants. For example, Figure 4.1, which reports on bond ratings for 2017, carries the "Responding Organizations" column header because 51 participants out of the total 56 organizations participating in the Study responded to this question.

Are all the data reported as averages?

Most, but not all. The majority of the figures and most of the related commentary present data as the average value (the arithmetic mean, calculated by adding all the observations and dividing by the number of observations). However, some commentary and a few figures present median data. As differentiated from the mean or average, the median is the middle value, or data point in the middle. That is, half of the data points are above the median and half below. The median can be useful in presenting data that have extremely high or low points that can skew the average and make it a misleading indicator.

Chapter 1
The Commonfund Benchmarks Study®
of Healthcare Organizations

INTRODUCTION

Fifty-six healthcare organizations participated in the 2016–2017 Commonfund Benchmarks Study® of Healthcare Organizations. These organizations reported an average investable asset pool of $2.1 billion as of December 31, 2017, and median investable assets of $987.0 million as of the same date. (Investable assets include endowment/foundation funds, funded depreciation, working capital and other separately treated assets). Thirty-two participating organizations reported an average DB plan market value of $2.0 billion as of year-end 2017, while the median market value of their DB plans as of the same date was $481.0 million.

Participating healthcare organizations are segmented into three cohorts based on asset size. The size categories and the number of organizations in each are shown in Figure 1.1.

When data are viewed by size of participating institution, the average value of investable assets increased in 2017 for all three size cohorts compared to 2016. For organizations in the two larger size cohorts, the year-over-year increase was 9.3 percent. For organizations with investable assets under $501 million, the increase was slightly smaller, at 8.3 percent.

In the case of DB plan assets, organizations with investable assets over $1 billion and those with assets between $501 million and $1 billion both reported an increase in the median asset size of their DB plans from 2016 to 2017—by 4.4 percent for the former and 13.2 percent for the latter. (Data for organizations with investable assets under $501 million were not available.)

Participants in the Study reported having a short-term investment pool that averaged $206.5 million in 2017. The median size of their short-term investment pool was $109.2 million.

Figure 1.1 **Average Total Investable Assets for Fiscal Years 2016 and 2017**

dollars ($) in millions	Total Organizations		Over $1 Billion		$501 Million-$1 Billion		Under $501 Million	
Responding organizations	56	56	30	34	13	11	13	11
	'16	'17	'16	'17	'16	'17	'16	'17
Investable assets	1,730	2,073	2,818	3,079	636	695	315	341
Market Value of DB Plan Assets	1,668	1,974	2,073	2,225	222	222	N/A	N/A

Figure 1.2 **Average Short-Term Investment Pool for Fiscal Year 2017**

dollars ($) in thousands	Total Organizations	Over $1 Billion	$501 Million-$1 Billion	Under $501 Million
Responding organizations	33	19	8	6
Average	206,456	227,020	219,073	124,513
Median	109,173	109,173	164,885	17,500

Chapter 2
Returns and Investment Objectives

As you read this chapter, consider these questions:

Reflecting on the decade-long bull market in financial assets, how should we position the portfolio going forward?

In a period when real returns from fixed income have been barely positive, what should our healthcare organization do with our allocation to the asset class?

How can we leverage our investable assets to help ensure long-term financial sustainability and make key, mission-critical investments?

INVESTMENT ENVIRONMENT

In large part, the investment environment in 2016 and 2017 was shaped by the events of Tuesday, November 8, 2016—the day Donald Trump was elected president. Essentially, there were two distinct periods: before election day and after election day. Yet, the surprising result of the presidential election was only the capstone to 2016's year of surprise.

- Each of the quarters in 2016 was marked by headlines that would have been hard to anticipate in advance: the worst calendar year start for U.S. equities ever; the U.K. vote to withdraw from the European Union; record highs recorded by the S&P 500 Index, the Dow Jones Industrial Average and the NASDAQ Composite Index on the same day in August; and, finally, Donald Trump's upset win in the presidential election in November. Equally remarkable, perhaps, every time markets were shaken by negative news, investors eventually held the line and sparked a rebound.
- Following the election, markets that had been predicted to retrench as much as 10 percent on a Trump victory rallied instead. Investors saw opportunity in the president-elect's calls for lower corporate taxes, investment in infrastructure, replacing the Affordable Care Act and a lighter approach to government regulation. The other news emerging from the quarter was the Federal Reserve's 25-basis-point increase in the fed funds rate along with indications that it would be more aggressive in raising short-term rates in the future.

Post-election optimism set the stage as 2017 began. From the start, the year was characterized by strong returns globally and historically low levels of volatility.

- Stocks jumped from the very start and rarely looked back. The hospitable investment environment was not a U.S. phenomenon, as developed and emerging markets in most of the world rallied. In fact, non-U.S. equities led the way. The MSCI Emerging Markets Free (Net) Index returned 37.3 percent, while the MSCI World ex U.S. Net Index returned 24.2 percent. Meanwhile, in the U.S., the S&P 500 Index returned 21.8 percent, as nine of the index's 11 sectors generated double-digit returns. With short-term interest rates rising and rates on long-dated issues remaining fairly steady, the Bloomberg Barclays U.S. Aggregate Bond Index produced stronger returns than it did in 2016—3.5 percent versus 2.7 percent the previous year.
- Despite the positive environment, investors seemed to keep their enthusiasm for the U.S. equity market in check. Analysts cited cautionary signs that kept outright euphoria at bay while consistently good news on the economic, financial and business fronts anchored the market's advance.

RETURNS ON INVESTABLE ASSETS

Returns on investable assets for the 56 nonprofit healthcare organizations participating in the Commonfund Benchmarks Study of Healthcare Organizations averaged 6.2 percent for 2016 and 13.2 percent for 2017. These and all returns in the Study are reported net of fees.

Returns on investable assets for 2017 were consistently higher than those reported for 2016. For the trailing three-, five- and 10-year periods, 2016 returns averaged 3.1 percent, 6.5 percent and 4.2 percent, respectively. For similar trailing periods, 2017 returns averaged 5.9 percent, 6.9 percent and 4.6 percent, respectively. The return gap between the one-year return for 2016 and 2017 narrowed over time, a pattern that has been reported in previous Studies. The one-year return difference of 700 basis points narrowed to 280 basis points for three years and to just 40 basis points for the trailing five-and 10-year periods.

When the data are viewed by asset size, 2016 and 2017 returns were very similar across the three size cohorts. The highest return over the two-year period, 13.7 percent posted in 2017, came from organizations with assets between $501 million and $1 billion. The lowest, 6.1 percent registered in 2016, came from two size groupings—organizations with assets over $1 billion and those with assets under $501 million.

Returns were fairly similar for longer periods as well. The greatest disparity in return was a 70-basis point spread between 10-year returns for organizations with assets under $501 million (5.1 percent) and those with assets between $501 million and $1 billion (4.4 percent). A slightly narrower 60-basis-point gap was found for 2016 trailing three-year returns reported by organizations with assets over $1 billion (3.3 percent) and those with assets under $501 million (2.7 percent). For both years and all three size cohorts, trailing five-year returns were the same or varied by no more than 10 basis points.

The standard deviation of participating organizations' investable asset returns averaged 5.3 percent over the past three years, 5.1 percent for the trailing five-year period and 9.0 percent for the trailing 10 years. This is lower than similar figures in the Report for 2014–2015 (when comparables were 6.2 percent, 7.3 percent and 9.5 percent). This is not surprising, given the relative lack of volatility in financial markets recently, especially during 2017. As noted in the previous Report, this measure of risk and volatility tends to even out or diminish over time, with the trailing 10-year figure remaining high owing to 2008, when markets were heavily impacted by the financial crisis and great recession.

One-, Three-, Five- and 10-year Returns for Periods Ending December 31, 2017

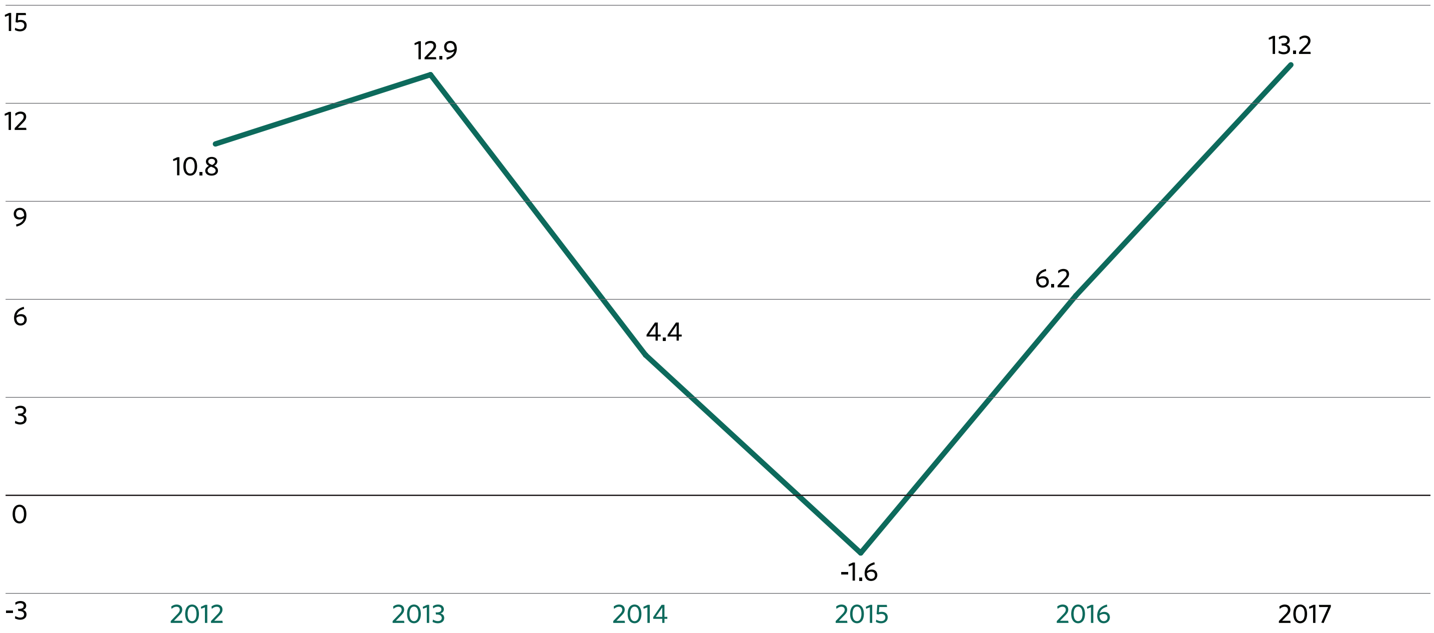
numbers in percent (%)

Index	1-Year	3-Year	5-Year	10-Year
S&P 500	1.4	15.1	12.6	7.3
Russell 3000	0.5	14.7	12.2	7.4
MSCI ACWI	-2.4	7.7	6.1	4.8
MSCI World ex-U.S.	-3.0	3.9	2.8	2.9
MSCI Europe*	4.9	10.1	6.9	3.9
MSCI Emerging Markets Free Net	-14.9	-6.8	-4.8	3.6
Burgiss Private IQ**	8.3	13.7	12.0	10.5
Bloomberg Barclays US Aggregate Bond	3.5	2.2	2.1	4.0
HFRI Distressed Debt	-8.1	1.1	2.2	3.9
HFRI Funds of Funds Composite	-0.4	3.9	2.1	2.3
NCREIF	13.3	12.0	12.2	7.8
Wilshire Real Estate Securities	4.8	12.1	12.4	7.3
Bloomberg Commodity	-19.6	-16.9	-14.1	-6.2
3-Month Treasury Bill (Average Yield)	0.1	0.1	0.1	1.2

*local currency
**Venture Capital and Private Equity Point-to-Point pooled IRRs as June 30, 2016. Returns calculated through Burgiss Private IQ.
Sources: Bloomberg, Burgiss, FactSet, HFR, MSCI, RSM US

Figure 2.1 **Investable Assets | Average Annual Total Net Returns for Total Organizations for Fiscal Years 2012-2017**

numbers in percent (%)



NOTE: Returns based on 73 organizations that provided return data FY2012-FY2015. Return data for FY2012 and FY2013 are estimates based on asset allocation ranges and market returns for participating healthcare organizations in fiscal years 2012 through 2015. While we believe that they are useful in assessing the general trend in investment returns during this period, we make no representation that they are accurate for any

Figure 2.2 **Investable Assets | Average One-, Three-, Five- and 10-Year Net Returns for Fiscal Years 2016 and 2017**

numbers in percent (%)	Total Organizations		Over $1 Billion		$501 Million-$1 Billion		Under $501 Million	
Responding organizations	56	56	30	34	13	11	13	11
	'16	'17	'16	'17	'16	'17	'16	'17
Annual total net return	6.2	13.2	6.1	13.1	6.4	13.7	6.1	12.9
3-year net return	3.1	5.9	3.3	5.9	2.9	6.0	2.7	5.6
5-year net return	6.5	6.9	6.5	6.9	6.4	7.0	6.4	7.0
10-year net return	4.2	4.6	4.1	4.6	4.3	4.4	4.4	5.1

Figure 2.3 **Investable Assets | Average Annualized Quarterly Standard Deviation of Three-, Five- and 10-Year Net Returns for Fiscal Year 2017**

numbers in percent (%)	Total Organizations	Over $1 Billion	$501 Million-$1 Billion	Under $501 Million
Responding organizations	56	34	11	11
3-year net return	5.3	5.2	*	*
5-year net return	5.1	5.2	*	*
10-year net return	9.0	9.2	*	*

*sample size too small too analyze

Chapter 3
Asset Allocation

As you read this chapter, consider these questions:

How can our asset allocation best reflect a balance between our return objectives and an appropriate level of risk?

How does our asset allocation compare to other areas of the nonprofit sector?

How should we assess our tolerance for illiquidity in our portfolios?

Asset allocation showed little change over the 2016–2017 period, as the year-over-year differences among the five primary asset classes/strategies were two percentage points in two allocations, one percentage point in two others and no change in the remaining one.

As seen in Figure 3.1, the allocation to U.S. equities grew by two percentage points while the allocation to short-term securities/cash/other declined by two percentage points. The allocation to non-U.S. equities grew by one percentage point and the allocation to alternative strategies declined by a similar percentage. The fixed income allocation was unchanged.

Greater changes emerge when data are compared with the Study for 2014–2015. Versus 2015, the 2017 allocation to alternative strategies was four percentage points lower, at 25 percent versus 29 percent. The fixed income allocation for 2017, at 31 percent, was three percentage points higher than 2015's 28 percent. The U.S. equities allocation grew from 19 percent in 2015 to 21 percent in 2017, while non-U.S. equities increased from 19 percent to 20 percent. The allocation to short-term securities/cash/other contracted to 3 percent in 2017 from 5 percent in 2015.

When asset allocation is examined by size of institution, organizations with assets over $1 billion reported larger allocations to alternative strategies, smaller allocations to U.S. equities and allocations that were fairly similar to the other size cohorts for the three remaining asset classes. Although the alternative strategies allocation declined for all three asset classes from 2016 to 2017, the largest organizations' 2017 allocation was more than twice that of organizations

Figure 3.1 **Investable Assets | Asset Allocations* for Fiscal Years 2016 and 2017**

numbers in percent (%)	Total Organizations		Over $1 Billion		$501 Million-$1 Billion		Under $501 Million	
Responding organizations	56	56	30	34	13	11	13	11
	'16	'17	'16	'17	'16	'17	'16	'17
U.S. equities	19	21	18	20	27	29	27	26
Fixed income	31	31	31	31	29	27	31	36
Non-U.S. equities	19	20	19	20	18	20	20	21
Alternative strategies	26	25	27	26	22	17	14	11
Short-term securities/cash/other	5	3	5	3	4	7	8	6

*dollar-weighted

in the smallest size cohort. The smallest allocation to fixed income and the largest to U.S. equities were found among organizations with assets between $501 million and $1 billion. Across the size cohorts the allocations to non-U.S. equities were relatively similar but not so the allocation to short-term securities/cash/other. In this instance, organizations with assets under $501 million had the largest allocation in 2016 (8 percent versus 4 percent for organizations with assets between $501 million and $1 billion) while the largest allocation for 2017 was that of organizations with assets between $501 million and $1 billion (7 percent versus 3 percent for organizations with assets over $1 billion).

Examining specific alternative strategies, at year-end 2016 and 2017, participating organizations' largest alternative strategy allocation among their investable assets was to marketable alternative strategies (hedge funds, absolute return, market neutral, long/short, 130/30, event-driven and derivatives). This allocation in 2016 was 14 percent; in 2017, it declined to 13 percent.

No other alternative strategies allocation came close to that of marketable alternatives. The 2017 allocation private equity (LBOs, mezzanine, M&A funds and international private equity) was just over one-third of that to marketable alternatives, while the 2016 allocation was less than one-third. After that, the largest allocations were to private equity real estate and energy and natural resources. Venture capital and commodities and managed futures each accounted for 1 percent.

When the data are viewed by asset size, the pattern remained much the same. The difference in size between the marketable alternatives allocation and the private equity allocation was magnified even more among the smallest organizations. In the case of organizations with assets under $501 million, marketable alternative strategies accounted for nearly 80 percent of the alternative strategies allocation in 2017.

Figure 3.2 **Investable Assets | Detailed Asset Allocations* for Fiscal Years 2016 and 2017**

numbers in percent (%)	Total Organizations		Over $1 Billion		$501 Million-$1 Billion		Under $501 Million	
Responding organizations	56	56	30	34	13	11	13	11
	'16	'17	'16	'17	'16	'17	'16	'17
U.S. equities	19	21	18	20	27	29	27	26
Fixed income	31	31	31	31	29	27	31	36
Non-U.S. equities	19	20	19	20	18	20	20	21
Alternative strategies	26	25	27	26	22	17	14	11
Private equity (LBOs, mezzanine, M&A funds and international private equity)	4	5	4	5	2	3	1	1
Marketable alternative strategies (hedge funds, absolute return, market neutral, long/short, 130/30, event-driven and derivatives)	14	13	14	14	14	10	11	8
Venture capital	1	1	1	1	1	1	0	0
Private equity real estate (non-campus)	3	3	3	3	2	2	1	1
Energy and natural resources	3	2	3	2	2	1	1	1
Commodities and managed futures	1	1	1	1	1	0	0	0
Distressed debt	0	0	1	0	0	0	0	0
Short-term securities/cash/other	5	3	5	3	4	7	8	6
Short-term securities/cash	4	3	4	3	3	4	6	6
Other	1	0	1	0	1	3	2	0

*dollar-weighted

Figure 3.3 **Investable Assets | U.S. Equity Asset Mix* for Fiscal Years 2016 and 2017**

numbers in percent (%)	Total Organizations		Over $1 Billion		$501 Million-$1 Billion		Under $501 Million	
Responding organizations	55	56	29	34	13	11	13	11
	'16	'17	'16	'17	'16	'17	'16	'17
Type of investment strategy								
Active - including REITs	57	57	56	55	56	64	64	65
Indexed (passive/enhanced)	43	43	44	45	44	36	36	35

*dollar-weighted

INVESTMENTS BY ASSET CLASS

At year-end 2016 and 2017, 57 percent of participating organizations' U.S. equities allocation was actively managed while 43 percent was indexed (passive/enhanced). Compared with 2015 in the previous Study, the current Study's active allocation was down only two percentage points. But measured against the allocation for 2014, which was 65 percent active and 35 percent passive, the reduction to active management has been fairly dramatic. As we observed in the previous Study, this may reflect the growing shift to indexation among highly efficient asset classes, such as U.S. equities, where it can be more difficult for an active manager to add value compared to less efficient areas, such as alternative strategies. Of interest, this shift has played out most clearly among organizations with assets over $1 billion; just the opposite was true of organizations with assets under $501 million, where the share of U.S. equities managed actively rose sharply (from 52 percent in 2015 to 65 percent in 2017).

As was true for 2014–2015, respondents in the 2016–2017 Study were much more likely to rely on active management for their fixed income allocation. This is consistent with the widely-accepted belief among institutional investors that fixed income is a much more problematic asset class to index and manage passively. Research supports this belief, as a greater percentage of active fixed income managers consistently outperform the benchmarks. In this case, 75 percent of Study participants' 2016 allocation and 76 percent of their 2017 allocation was to actively managed U.S. investment-grade securities. Seven percent was allocated to the passive equivalent for both years; 4-5 percent was allocated to U.S. non-investment grade (active or passive); 4-5 percent was allocated to non-U.S. investment-grade securities (active or passive); and 8-9 percent was allocated to emerging markets (active or passive).

Figure 3.4 **Investable Assets | Fixed Income Asset Mix* for Fiscal Years 2016 and 2017**

numbers in percent (%)	Total Organizations		Over $1 Billion		$501 Million-$1 Billion		Under $501 Million	
Responding organizations	55	55	29	33	13	11	13	11
	'16	'17	'16	'17	'16	'17	'16	'17
Type of investment strategy								
U.S. investment grade (active)	75	76	75	76	82	79	76	83
U.S. investment grade (passive)	7	7	6	6	11	14	10	5
U.S. non-investment grade (active or passive)	5	4	5	4	4	4	8	6
Non-U.S. investment grade (active or passive)	5	4	5	4	2	3	5	3
Emerging markets (active or passive)	8	9	9	10	1	0	1	3

*dollar-weighted

The data did not vary significantly when examined by asset size. There was a somewhat greater tendency for organizations in the two smaller size cohorts to use active management for their U.S. investment-grade allocation. Organizations with assets over $1 billion had by far the largest allocation to emerging market fixed income (active or passive).

The non-U.S. equities allocation was relatively consistent for all Study respondents and organizations with assets over $1 billion, while greater variability was found among organizations with assets between $501 million and $1 billion and those with assets under $501 million. Sixty-three percent of all respondents' 2017 non-U.S. equities allocation and 65 percent of the largest organizations' allocation were actively managed. However, the proportion of this allocation that was actively managed by the two other size cohorts at year-end 2017 declined to 48 percent each. Compared to the previous Study, the 63 percent of non-U.S. equity asset that were actively managed at year-end 2017 represented a decline from 69 percent at year-end 2015. Eleven percent of assets were passively managed or indexed at year-end in both 2015 and 2017. But the allocation to emerging markets grew to 26 percent at year-end 2017 versus 20 percent at year-end 2015.

Turning to alternative strategies, more than half of healthcare organizations' allocation to alternative strategies was to marketable alternatives in both 2016 and 2017. This allocation was more than two and one-half times larger than that to private equity and almost five times larger than those to private equity real estate and energy and natural resources. Allocations to venture capital, commodities and managed futures, and distressed debt were 3 percent or less.

Figure 3.5 **Investable Assets | Non-U.S. Equity Asset Mix* for Fiscal Years 2016 and 2017**

numbers in percent (%)	Total Organizations		Over $1 Billion		$501 Million-$1 Billion		Under $501 Million	
Responding organizations	55	56	29	34	13	11	13	11
	'16	'17	'16	'17	'16	'17	'16	'17
Type of investment strategy								
Active MSCI EAFE	61	63	62	65	63	48	36	48
Passive/index MSCI EAFE	14	11	12	8	21	34	38	26
Emerging markets	25	26	26	27	16	18	26	26

*dollar-weighted

While remaining the predominant allocation, marketable alternatives accounted for less of participating organizations' alternative strategies allocation compared to the previous Study; in the current Study, the allocation declined to 55 percent for 2016 and 53 percent for 2017 versus 59 percent for 2014 and 56 percent for 2014.

When the data are analyzed by asset size, the 2017 allocation to marketable alternatives among organizations with assets under $501 million accounted for 74 percent of these organizations' alternative asset allocation compared to 52 percent for organizations with assets over $1 billion. That said, organizations with assets over $1 billion committed 19 percent of their 2017 alternative asset allocation to private equity versus just 5 percent for organizations with assets under $501 million. Organizations with assets over $1 billion also had the largest private equity real estate allocation among the three size cohorts.

Figure 3.6 **Investable Assets | Alternative Strategies Asset Mix* for Fiscal Years 2016 and 2017**

numbers in percent (%)	Total Organizations		Over $1 Billion		$501 Million-$1 Billion		Under $501 Million	
Responding organizations	50	52	28	34	11	9	11	9
	'16	'17	'16	'17	'16	'17	'16	'17
Type of investment strategy								
Private equity (LBOs, mezzanine, M&A funds and international private equity)	16	19	17	19	11	18	5	5
Marketable alternative strategies (hedge funds, absolute return, market neutral, long/short, 130/30, event-driven and derivatives)	55	53	53	52	63	56	79	74
Venture capital	3	3	3	3	5	8	0	0
Private equity real estate (non-campus)	11	11	11	11	8	9	4	7
Energy and natural resources	11	10	12	10	7	6	6	10
Commodities and managed futures	2	3	2	3	4	2	4	1
Distressed debt	2	1	2	2	2	1	2	3

In Focus
Defined Benefit Plans

Note: Previous Benchmarks Studies have presented data concerning investable assets and defined benefit (DB) plans together in appropriate chapters, e.g., investment returns and asset allocation. Given the different nature and purpose of DB plans, as distinct from investable assets, this year we are combining all data concerning DB plans into a single, dedicated section.

In the Study for 2016–2017, 32, or 57 percent, of Study respondents said they had a defined benefit plan. Of those with DB plans, 69 percent reported having a traditional-style plan; 16 percent had a cash balance plan; 12 percent had a hybrid or other type of plan; and 3 percent had no answer or were uncertain.

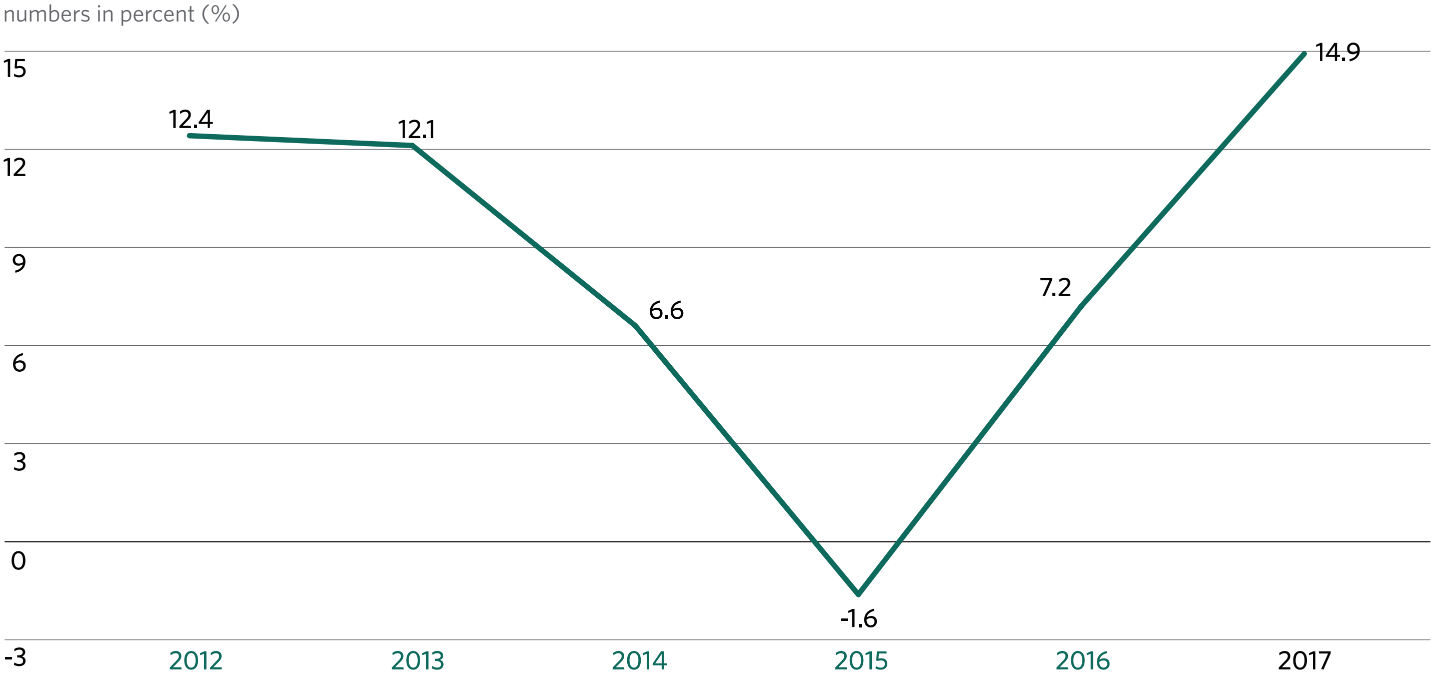
Nineteen percent of Study participants with plans reported that their plans were still open, while 75 percent that their plans had been frozen. Fifty-seven percent of Study respondents overall said that their plans were still accruing benefits, while 31 percent said they were not.

Figure DB.1 Defined Benefit Plans | Status* for Fiscal Year 2017

numbers in percent (%)	Total Organizations
Responding organizations	32
Have DB Plan	57
Traditional	69
Cash balance	16
Hybrid/other	12
No answer/uncertain	3
DB Plan open	19
DB Plan frozen	75
Uncertain	3
No answer	3
DB Plan still accruing benefits	
Yes	57
No	31
Uncertain	9
No answer	3
Do not have DB plan	43
Market Value of DB Plan Assets**	1,974

*multiple responses allowed
**dollars ($) in millions

Figure DB.2 **Defined Benefit Plans | Average Annual Total Net Returns for Fiscal Years 2012-2017**



NOTE: Returns based on 51 organizations that provided return data FY2012-FY2015. Return data for FY2012 and FY2013 are estimates based on asset allocation ranges and market returns for participating healthcare organizations in fiscal years 2012 through 2015. While we believe that they are useful in assessing the general trend in investment returns during this period, we make no representation that they are accurate for any particular healthcare organization or group of healthcare organizations.

Returns on participating healthcare organizations' DB plans averaged 7.2 percent in 2016 and 14.9 percent in 2017. This compares 6.6 percent in 2014 and -1.6 percent in 2015, as reported in the previous Study. (Like investable assets, DB plan returns are net of fees.)

With one minor exception, average DB plan returns for 2016 and 2017 exceeded their respective returns for the trailing three-, five- and 10-year periods. The exception was the 2016 five-year average return, which, at 7.3 percent, was one-tenth of percentage point higher than 2016's 7.2 percent. The greatest spread occurred in 2017's trailing long-term returns; for 2017, DB plan returns ranged from two to almost three times larger than those reported for the three long-term periods.

Of those healthcare organizations with DB plans, 25 percent reported implementing a de-risking strategy in 2017, while 44 percent reported implementing a liability-driven strategy. Another 25 percent reported they had implemented neither strategy and 6 percent gave no answer. Looking ahead, 41

Figure DB.3 **Defined Benefit Plans | Average One-, Three-, Five- and 10-Year Net Returns for Fiscal Years 2016 and 2017**

numbers in percent (%)	Total Organizations	
Responding organizations	32	32
	'16	'17
Annual total net return	7.2	14.9
3-year net return	3.9	6.6
5-year net return	7.3	7.8
10-year net return	4.8	5.4

Figure DB.4 **Defined Benefit Plans | Use of De-Risking and Liability-Driven Investing for Fiscal Year 2017**

numbers in percent (%)	Total Organizations
Responding organizations	32
Implemented	
De-risking strategy	25
Liability-driven investing	44
Neither	25
Uncertain	0
No answer	6
Considering implementing in the next 12 months	
Yes	41
No	31
Uncertain	19
No answer	9

percent said they are considering implementing a de-risking or liability-driven strategy; 31 percent without either strategy said they would not implement an approach in the next 12 months; 19 percent were uncertain; and 9 percent gave no answer.

DB PLAN ASSET ALLOCATION

Fixed income was the largest single allocation for both 2016 and 2017, at 31 percent and 32 percent, respectively. The allocations to non-U.S. equities and alternative strategies were quite similar, with the former increasing two percentage points to 24 percent over the period, while the allocation to alternative strategies declined one percentage point to 23 percent. The allocation to U.S. equities declined to 20 percent from 22 percent, and the allocation to short-term securities/cash/other was unchanged at 1 percent.

Compared with the previous Study for 2014–2015, the greatest change occurred in a five-percentage-point decline in the allocation to alternative strategies—at 23 percent in 2017 versus 28 percent in 2015. Two allocations reflected four-percentage-point increases: the allocation to fixed income—at 32 percent in 2017 versus 28 percent in 2015—and non-U.S. equities—at 24 percent for 2017 compared with 20 percent in 2015. The allocation to short-term securities/cash/other declined by an equal four percentage points, at 1 percent for 2017 versus 5 percent for 2015.

Figure DB.5 **Defined Benefit Plans | Asset Allocations* for Fiscal Years 2016 and 2017**

numbers in percent (%)	Total Organizations	
Responding organizations	32	32
	'16	'17
U.S. equities	22	20
Fixed income	31	32
Non-U.S. equities	22	24
Alternative strategies	24	23
Short-term securities/cash/other	1	1

*dollar-weighted

Figure DB.6 **Defined Benefit Plans | Detailed Asset Allocations* for Fiscal Years 2016 and 2017**

numbers in percent (%)	Total Organizations	
Responding organizations	32	32
	'16	'17
U.S. equities	22	20
Fixed income	31	32
Non-U.S. equities	22	24
Alternative strategies	24	23
Private equity (LBOs, mezzanine, M&A funds and international private equity)	6	7
Marketable alternative strategies (hedge funds, absolute return, market neutral, long/short, 130/30, event-driven and derivatives)	12	11
Venture capital	1	0
Private equity real estate (non-campus)	3	3
Energy and natural resources	1	1
Commodities and managed futures	1	1
Distressed debt	0	0
Short-term securities/cash/other	1	1
Short-term securities/cash	1	1
Other	0	0

*dollar-weighted

Compared with the investable assets allocation in the 2016–2017 Study, the greatest difference was found in non-U.S. equities, which accounted for 24 percent of DB plan assets but 20 percent of investable assets. The allocation to short-term securities/cash/other was higher in the investable assets allocation, at 3 percent, versus DB plans' allocation of 1 percent.

Turning to sub-strategies under the broader alternatives category, marketable alternatives accounted for the largest single allocation, at 11 percent in 2017. This was followed by the allocation to private equity, at 7 percent in 2017. This follows the same pattern seen in investable assets.

DB PLAN ASSET MIX

Organizations with DB plans reported that about three-quarters of their U.S. equity allocation was actively managed in 2016 and 2017, with the remaining quarter indexed or passively/enhanced managed. This was higher than reported for investable assets, where the proportion actively managed was in the 55-56 percent range.

Figure DB.7 **Defined Benefit Plans | U.S. Equity Asset Mix* for Fiscal Years 2016 and 2017**

numbers in percent (%)	Total Organizations	
Responding organizations	31	30
	'16	'17
Type of investment strategy		
Active - including REITs	75	73
Indexed (passive/enhanced)	25	27

*dollar-weighted

Figure DB.8 **Defined Benefit Plans | Fixed Income Asset Mix* for Fiscal Years 2016 and 2017**

numbers in percent (%)	Total Organizations	
Responding organizations	32	32
	'16	'17
Type of investment strategy		
U.S. investment grade (active)	90	86
U.S. investment grade (passive)	2	5
U.S. non-investment grade (active or passive)	1	1
Non-U.S. investment grade (active or passive)	2	4
Emerging markets (active or passive)	5	4

*dollar-weighted

Participating organizations with DB plans reported that 86 percent of their 2017 U.S. investment-grade fixed income allocation was actively managed and 5 percent was passively managed. This compared with 76 percent of the investable assets allocation that was actively managed and 7 percent that was passively managed.

Seventy percent of DB plans' non-U.S. equities allocation was actively managed in 2017 while just 3 percent was passively managed or indexed. Twenty-seven percent was allocated to emerging market equities. Relative to investable assets, somewhat more of the DB plan allocation was actively managed, while the investable assets emerging markets allocation was only one-percentage-point smaller. Looking at the allocations underlying the overall alternative strategies allocation, 49 percent was committed to marketable alternative strategies in both 2016 and 2017. The allocation to private equity, however, showed substantial year-over-year growth, increasing to 31 percent in 2017 from 23 percent in 2016. The allocation to private equity real estate went in the opposite direction, shrinking to 10 percent in 2017 from 15 percent in 2016. The other allocations, all sized in single digits, showed little change.

Relative to DB plans' asset mix, marketable alternative strategies also accounted for the largest single investable asset allocation—but at an even greater 50 percent-plus. Like the DB plan allocation to private equity, that of investable assets also grew, but at three percentage points was not as large as eight percentage points for DB plans. The investable assets allocation to private equity real estate was unchanged over the two-year period, at 11 percent.

Figure DB.9 **Defined Benefit Plans | Non-U.S. Equity Asset Mix* for Fiscal Years 2016 and 2017**

numbers in percent (%)	Total Organizations	
Responding organizations	29	29
	'16	'17
Type of investment strategy		
Active MSCI EAFE	64	70
Passive/index MSCI EAFE	6	3
Emerging markets	30	27

*dollar-weighted

Figure DB.10 **Defined Benefit Plans | Alternative Strategies Asset Mix* for Fiscal Years 2016 and 2017**

numbers in percent (%)	Total Organizations	
Responding organizations	25	26
	'16	'17
Type of investment strategy		
Private equity (LBOs, mezzanine, M&A funds and international private equity)	23	31
Marketable alternative strategies (hedge funds, absolute return, market neutral, long/short, 130/30, event-driven and derivatives)	49	49
Venture capital	3	1
Private equity real estate (non-campus)	15	10
Energy and natural resources	5	5
Commodities and managed futures	3	3
Distressed debt	2	1

*dollar-weighted

Chapter 4
Debt and Fund Flows

As you read this chapter, consider these questions:

How can we optimize the relationship between our asset allocation and our debt rating? What is it costing us in terms of investment return to maintain our debt rating?

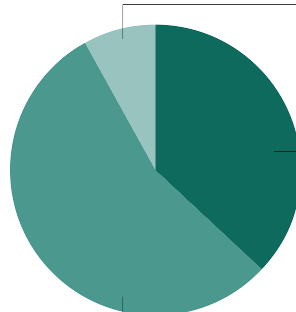
Study respondents say their long-term return objective is 6.0 percent—but data show it's not being achieved. What action should we take to bring our long-term target within reach?

Nonprofit healthcare organizations need to maintain a liquidity level that allows for favorable credit ratings so they can issue bonds to pay for project and capital expenditures and increase their capacity to both sustain and expand. The need to keep high levels of operating cash to maintain their bond ratings impacts their asset allocation strategy, with a heavier weight toward cash and fixed income investments, lessening opportunities to realize higher returns. The tension between the need for liquidity and the desire to maximize endowment fund performance puts an added stress on healthcare organizations that are already experiencing tight margins and an ever evolving operating environment.

DEBT

An organization's debt rating dictates the price at which it can raise long-term capital in the markets. For 2017, 37 percent of respondents' bonds had the equivalent of the highest or high investment-grade ratings by the bond rating agencies, unchanged since 2015. Fifty-five percent reported having some other investment-grade rating—up from 42 percent in 2015—while no organization (zero percent) reported having a non-investment grade rating, down from 3 percent in 2015. Eight percent gave no answer or were uncertain versus 18 percent in 2015.

Figure 4.1 **Bond Ratings* for Fiscal Year 2017**



*used Moody's, S&P and Fitch ratings to determine investment grade for 51 total responding organizations

FUND FLOWS

Participating healthcare organizations budgeted an investment return of 5.1 percent for 2016 and 5.0 percent for 2017. This compares with 4.9 percent for 2014 and 2015.

When data are viewed by size of institution, the three size cohorts were virtually the same for 2016 at just over the 5 percent level. That held for the two larger size cohorts in 2017, but organizations with assets under $501 million lowered their budgeted return on investable assets to 4.5 percent.

In terms of long-term investment objectives for their operating assets, participating organizations' 2017 target was 6.0 percent, up moderately from 5.8 percent in 2015. Organizations with assets over $1 billion had the highest long-term target, at 6.3 percent. The other two size cohorts were lower: organizations with assets between $501 million and $1 billion, at 5.3 percent, and those with assets under $501 million, at 5.5 percent.

OPERATING MARGIN

The median operating margin for 2017 was 3.5 percent. Organizations with assets over $1 billion reported the same margin, 3.5 percent, while organizations with assets between $501 million and $1 billion reported a median of 3.3 percent, and those with assets under $501 million reported the highest median operating margin, at 3.8 percent.

For 2016–2017, major rating agencies and other healthcare industry analysts note that median operating margins for nonprofit healthcare organizations were about 3.4 percent, which corresponds with self-reported operating margins for the healthcare organizations that participated in this Study. While other sectors would find these operating margins alarming, they are a hard reality for healthcare organizations. A changing reimbursement landscape will continue to impact operating revenue for healthcare organizations, making the need for asset allocation strategies that maximize the growth of investable assets that much more important to long-term financial sustainability.

Figure 4.2 **Budgeted Investment Return, Long-Term Return Objectives, Operating Margin and Investment Income**

numbers in percent (%)	Total Organizations	Over $1 Billion	$501 Million-$1 Billion	Under $501 Million
Responding organizations	56	34	11	11
FY2017 Annual budgeted investment return	5.0	5.2	5.0	4.5
FY2016 Annual budgeted investment return	5.1	5.1	5.1	5.2
FY2017 % return objective for long-term investable assets	6.0	6.3	5.3	5.5
Do not have return objective	21	18	27	27
Uncertain return objective	13	15	9	9
FY2017 Median operating margin	3.5	3.5	3.3	3.8
Uncertain operating margin	13	12	18	9
FY2017 Median investment income as a % of net income	58.5	55.7	62.6	50.5
Uncertain investment income	27	21	27	45

Viewpoint
The Long of It

Endowments, like the organizations they support, are generally intended to operate in perpetuity. To accomplish this goal, those responsible for endowments—trustees or directors—make decisions based not on myopic thinking or daily machinations in the financial markets, but on the unique mission, resources and culture of the organization whose interests they represent. The document that usually maps out the intended route to their institution's envisioned future is the investment policy statement, or IPS. Typically, the IPS spells out the institution's philosophy of investment management, its goals and objectives, and its strategies for reaching them: return targets, asset allocation guidelines, portfolio rebalancing, acceptable risk parameters, spending methodology and other considerations.

All of these strategies play a role in the pursuit of a risk-adjusted rate of return sufficient to support the institution's long-term mission. Over the short and intermediate terms, some organizations lean heavily on their endowment to support operations, others less so. For nonprofit healthcare organizations and systems, the endowment is one of multiple sources of support that include operating revenue, reimbursements and philanthropy.

In this year's Commonfund Benchmarks Study® of Healthcare Organizations, respondents told us that, for 2017 at least, the long-term return target for their investable assets is 6.0 percent. It was slightly higher, at 6.3 percent, for organizations with investable assets over $1 billion, but slightly lower for the other two size cohorts: 5.3 percent for organizations with assets between $501 million and $1 billion and 5.5 percent for organizations with assets under $501 million.

Naturally, that leads to a question: How are they doing against their goal? Data in the following tables (from the current and past Benchmarks Studies) give us an indication. The first table shows trailing 10-year returns, a metric that started with the Report for 2013. The second table shows trailing five-year returns, which were the long-term periods used for Reports for 2003 through 2011. (The initial Study, for 2002, reported a one-year return of -4.9 percent.)

10-Year Average Annual Returns on Healthcare Organizations' Investable Assets

	'13	'14	'15	'16	'17
Return	6.2	5.6	4.7	4.2	4.6

numbers in percent (%)

Five-Year Average Annual Returns on Healthcare Organizations' Investable Assets

	'03	'04	'05	'06	'07	'08	'09	'10	'11
Return	3.0	4.0	4.9	7.3	11.1*	1.7	3.5	4.1	1.8

numbers in percent (%)
*This seeming outlier results from 2002's -4.9 percent return rolling off the five-year calculation.

The conclusion is clear: Past performance shows there is a gap between the current long-term target of 6.0 percent and the historic ability of participating healthcare organizations to deliver on it. Only in 2013 did the trailing 10-year return exceed 6.0 percent. And only in two years between 2003 and 2011 did the trailing five-year return exceed that level.

Asset allocation has long been identified as the key factor in investment return. In 1986, what is perhaps the seminal study of asset allocation, the "Determinants of Portfolio Performance," was published by Gary P. Brinson, L. Randolph Hood and Gilbert L. Beebower in The Financial Analysts Journal. The authors' analysis attributed 91.5 percent of the variability of quarterly volatility to asset allocation, while security selection accounted for just 4.6 percent of return and market timing accounted for just 1.8 percent.

On that basis it is useful to look at healthcare organizations' asset allocation and compare how these organizations allocate funds versus other participants in the nonprofit sector.

The high allocation to fixed income investments by healthcare organizations marks a consistent difference between these organizations and others in the nonprofit sector. Healthcare organizations reported a 2017 fixed income allocation of 31 percent among their investable assets, but among other types of nonprofits, fixed income allocations were substantially lower. In the NACUBO-Commonfund Study of Endowments® (NCSE), the fixed income allocation for fiscal year 2017 averaged 8 percent and in the Council on Foundations–Commonfund Study of Investment of Endowments for Private and Community Foundations® (CCSF) for 2017 community foundations reported an average fixed income allocation of 14 percent.

In the following table, we compare healthcare organizations' investable asset allocations as of December 31, 2017, to those of colleges and universities and community foundations participating in the most recent NCSE and CCSF[1].

numbers in percent (%)	Healthcare organizations	Educational endowments	Community foundations
Asset class/strategy			
U.S. equities	21	16	29
Fixed income	31	8	14
Non-U.S. equities	20	20	24
Alternative strategies	25	52	27
Short-term securities/ cash/other	3	4	6

As the table shows, there are major differences in asset allocations among the three organizational types, particularly in fixed income and alternative strategies.

Healthcare organizations have the largest allocation to fixed income—almost four times that of educational endowments and more than twice that of community foundations. Over the course of many Commonfund Studies, it is evident that of the three types of nonprofit organization, colleges and universities have been the most aggressive in their asset allocation. They have a clear equity bias, which is one of the key tenets of the endowment model (the others being a high degree of portfolio diversification, the acceptance of lower liquidity and a perpetual investment horizon). Community foundations[2] tend to fall in the middle between educational endowments and healthcare organizations. Their allocation to alternative strategies is quite similar to that of healthcare organizations, but they have larger allocations to U.S. and non-U.S. equities.

Healthcare organizations' focus on maintaining their bond ratings, and the attendant balance sheet liquidity required by the rating agencies, will likely keep their allocations to fixed income securities high relative to others in the nonprofit sector. In fact, as we have seen, the 2017 allocation to fixed income is higher than it was in 2015 (31 percent versus 28 percent). And while healthcare organizations had been increasing their allocation to alternative strategies in recent years, that trend appears to have paused, if not reversed direction (25 percent in 2017 versus 29 percent in 2015).

Thus, while we opined in the last Study that healthcare organizations appeared to be adopting more of the characteristics of an "endowment model investor," we would no longer hold to that view in light of asset allocation shifts illuminated by the data in the current Study.

As an aside, we note that when healthcare organizations' investable asset allocations are viewed on an equal-weighted basis, for 2017 the allocation to fixed income declines only one percentage point, from 31 percent to 30 percent. The allocation to alternative strategies, however, falls to 21 percent from 25 percent, indicating that only the largest healthcare organizations are participating in this market in any meaningful way. Please refer to Figure 3.2A in Appendix II.

1 College and university returns are not directly comparable with those of other nonprofits, owing to the different fiscal year end observed by these institutions. Healthcare organizations and foundations report on a calendar year ending December 31, while colleges and universities report on a fiscal year that ends June 30.

2 We cite community foundations here instead of private foundations because the latter are funded by a donor (individual, family or institution) and do not pursue additional gifts or donations, as is the case with community foundations (and healthcare organizations).

CONCLUSION

Referring back to the discussion of the IPS, we should acknowledge the importance of the statement of purpose of the investment pool. Different organizations have different purposes for their endowed funds. Endowments are composed of individual funds given by donors over time, usually to support particular activities or missions of the organization. Apart from these restricted funds, donors sometimes give with no restriction as to purpose. In addition, organizations themselves may elect to treat operating surpluses, unrestricted bequests and other similar amounts as "quasi-endowment."

We recognize that healthcare organizations have several factors that make them unique. One is the role of investable funds in supporting the organization's balance sheet. If the endowment is there to support the budget, its role is quite clear. But if it is also meant to support a credit rating, that introduces a new set of considerations. Often, especially with hospitals, the credit rating agencies will have a guideline as to how many days' cash on hand an institution should have and how much underlying capital should be in place. This has to be worked into the institution's risk and return expectations; a growing number of organizations are doing this and are also addressing gifts and debt in their investment policy. So, although this point comes last, it is certainly not least. In fact, it ties back to our earlier discussion point: What is the purpose of the investment pool? There is a strong case to be made for linking the investment policy with the institution's balance sheet as well as its long-term strategic plan.

Chapter 5
Resources, Management and Governance

As you read this chapter, consider these questions:

In managing our assets, what are the appropriate roles for our trustees, managers and consultants?

What is the best size and desired skill set for our investment committee?

Outsourcing has grown. What does this mean for our organization?

In this section, we review the support structure—committee, governance and staff resources— available to guide healthcare organizations into the future after a decade that has gone from the financial crisis/Great Recession to a strong economy and one of the longest U.S. bull markets on record.

PROFESSIONAL STAFFING

Participating healthcare organizations reported employing an average of 2.1 full-time equivalent (FTE) professionals to manage the investment function in 2017. The median figure was 1.8 FTEs. Compared to the same data for 2015, there was little change in the average number of FTEs, standing at 2.0 in 2015, but a sharp increase, from 0.9 FTE, in the median figure. Such a change in the median figure could mean an increase in FTEs on the part of smaller healthcare organizations and indeed, the data support that. Whereas organizations with assets under $501 million reported an average of 0.4 FTE and a median of 0.3 FTE in 2015, those figures rose to 1.1 FTEs and 1.0 FTE, respectively, in 2017.

In the mid-sized cohort, the figures went the opposite way, with the average number of FTEs falling to 0.6 and the median to 0.3 from 1.0 and 0.6, respectively, in 2015. Organizations with assets over $1 billion also reported data that was mixed—an average of 2.8 FTEs in 2017, down from 3.4 FTEs in 2015, but a slightly higher 2017 median of 2.3 versus 2.0 in 2015.

MANAGER USE

Participating healthcare organizations reported using an average of 4.5 investment managers each to oversee their fixed income and non-U.S. equities allocations and 4.4 managers to oversee their U.S. equites allocation. They retained an average of 16.0 managers for their alternative strategies (direct) allocation and an average of 2.6 managers for their alternative strategies (fund of funds) allocation. All data show little change from the previous Study for 2015.

Figure 5.1 **Professional Staffing of Investment Function for Fiscal Year 2017**

number of Full-Time Equivalents (FTEs)	Total Organizations	Over $1 Billion	$501 Million-$1 Billion	Under $501 Million
Responding organizations	56	34	11	11
Average number of FTEs	2.1	2.8	0.6	0.9
Median number of FTEs	1.5	2.3	0.3	1.0

Figure 5.2 **Number of Managers Used by Asset Class for Fiscal Year 2017**

average number	Total Organizations	Over $1 Billion	$501 Million-$1 Billion	Under $501 Million
Responding organizations	56	34	11	11
U.S. equities	4.4	4.8	4.0	3.4
Fixed income	4.5	5.1	3.8	3.4
Non-U.S. equities	4.5	5.2	4.5	2.5
Alternative strategies (direct)	16.0	20.7	13.8	4.2
Alternative strategies (fund of funds)	2.6	3.8	1.3	0.6

When the data are viewed by size of institution, in all cases those with assets over $1 billion employed the most managers. The widest disparity was among alternative strategies (direct) managers, where organizations with assets over $1 billion used an average of 20.7 managers versus 4.2 on average for organizations with assets under $501 million. Compared to the Study for 2015, there was a decline in the number of alternatives (direct) managers used by the largest organizations, as the 20.7 average was lower than 2015's 25.1 average. The number of alternative strategies managers (direct) also declined for organizations with assets between $501 million and $1 billion, but it rose for those with assets under $501 million.

OUTSOURCING OF THE INVESTMENT FUNCTION

Twenty-seven percent of Study participants overall reported substantially outsourcing their investment management function in 2017. Viewed by size cohort, this comprised 21 percent of organizations with assets over $1 billion; 27 percent of those with assets between $501 million and $1 billion; and 45 percent of those with assets under $501 million.

The 27 percent of participating organizations substantially outsourcing in 2017 was two percentage points lower than the 2015 figure. There was no change in the proportion of the largest Study participants that outsourced, remaining at 21 percent, but the share of respondents outsourcing among the mid-sized cohort nearly doubled to 27 percent from 14 percent in 2015. There was a modest change among small organizations, where 45 percent outsourced in 2017, down from 48 percent in 2015.

Figure 5.3 **Outsourcing of Investment Function for Fiscal Year 2017**

numbers in percent (%)	Total Organizations	Over $1 Billion	$501 Million-$1 Billion	Under $501 Million
Responding organizations	56	34	11	11
Have substantially outsourced	27	21	27	45

Figure 5.4 **Consultant Use for Fiscal Year 2017**

numbers in percent (%)	Total Organizations	Over $1 Billion	$501 Million- $1 Billion	Under $501 Million
Responding organizations	56	34	11	11
Use consultant	91	100	91	64
Services used*				
Asset allocation/rebalancing	90	85	100	100
Manager selection	88	88	90	86
Policy review	76	68	90	100
Performance attribution and measurement	86	82	100	86
Outsourced investment management	12	12	10	14
ESG criteria review	22	24	10	29
Ongoing due diligence	84	91	80	57
Other	0	0	0	0

*multiple responses allowed

CONSULTANT USE

Ninety-one percent of total Study respondents said they use a consultant, up from 85 percent in the previous Study. Viewed by size of institution, 100 percent of organizations with assets over $1 billion said that they use a consultant (up from 88 percent); 91 percent of those with assets between $501 million and $1 billion do so (up from 86 percent); and 64 percent of those with assets under $501 million also reported using a consultant (down from 80 percent).

Consultants are most often used for asset allocation and rebalancing, by 90 percent of participants; manager selection, by 88 percent; performance attribution and measurement, by 86 percent; and "other," by 84 percent. Consultants were least likely to be used for outsourced investment management, as just 12 percent of respondents used them for this purpose. This is a significant decline from the 31 percent of Study participants using them for this purpose in 2015. We also observe that while various forms of responsible investing are being implemented at an increasing rate among nonprofit organizations, there appears to be little change among Study participants. In 2015, 21 percent of Study respondents used consultants for ESG (environmental, social, governance) criteria review, a rate that grew to just 22 percent for 2017.

Figure 5.5 **Investment Committee Members and Credentials for Fiscal Year 2017**

average number	Total Organizations	Over $1 Billion	$501 Million-$1 Billion	Under $501 Million
Responding organizations	56	34	11	11
Voting investment committee members	7.9	7.7	11.1	6.3
Investment committee members that are investment professionals	4.3	4.5	5.0	3.2
Investment committee members with alternative strategies experience	2.7	3.1	1.8	1.6
Non-trustee voting members	2.5	2.8	0.6	2.6

INVESTMENT COMMITTEE PROFILES

Turning to investment committee demographics, the average number of voting members on the investment committees of participating healthcare organizations was 7.9. This compares with an average of 7.4 in 2015.

The number of investment committee members who are investment professionals averaged 4.3, up from 4.0 in 2015; the average number of investment committee professionals with experience in alternative strategies was 2.7, down slightly from 2.9; and the number of voting investment committee members who are not trustees averaged 2.5, up from 2015's 2.3.

When the data are viewed by asset size, organizations with assets between $501 million and $1 billion had the largest number of voting members on the investment committee, an average of 11.1. This was substantially ahead of organizations with assets over $1 billion, at an average of 7.7 voting members, and organizations with assets under $501 million, with an average of 6.3 voting members. Organizations with assets between $501 million and $1 billion also had the highest number of investment committee members who are investment professionals but lowest number who are non-trustee voting members.

APPENDICES
Appendix I
About Commonfund Institute

ABOUT COMMONFUND INSTITUTE

Commonfund Institute houses the education and research activities of Commonfund and provides the entire community of long-term investors with investment information and professional development programs. Commonfund Institute is dedicated to the advancement of investment knowledge and the promotion of best practices in financial management. Commonfund Institute pursues its objectives through a wide variety of resources, including conferences, seminars and roundtables on topics such as endowment and treasury management; proprietary and third-party research and publications including the annual Council on Foundations - Commonfund Study of Investment of Endowments for Private and Community Foundations® (CCSF) and Commonfund Benchmarks Studies®, in-depth surveys of investment management practices and policies; the management and distribution of the Commonfund Higher Education Price Index® (HEPI), an inflation index designed specifically for higher education; and Commonfund Forum, the largest investment conference for trustees and senior executives of qualified organizations. The Institute's broad range of programs and services is designed to serve financial practitioners, fiduciaries and scholars.

Commonfund Institute, in addition to conducting and publishing the CCSF and the various Commonfund Benchmarks Studies, conducts the full range of research, education, publication, professional development and best practice initiatives in which Commonfund has been engaged since its founding in 1971. At that time, Commonfund was established with the assistance of a $2.8 million grant from the Ford Foundation; of that total, $500,000 was earmarked specifically for research and publications. Thus, projects such as this Study have been an essential part of Commonfund's mission from the beginning. Over the years, we have published numerous books, white papers and monographs on topics related to endowment and treasury management.

Appendix II
Equal-weighted Tables

Figure 3.2A/EW Investable Assets | Detailed Asset Allocations* for Fiscal Years 2016 and 2017

numbers in percent (%)	Total Organizations		Over $1 Billion		$501 Million-$1 Billion		Under $501 Million	
Responding organizations	56	56	30	34	13	11	13	11
	'16	'17	'16	'17	'16	'17	'16	'17
U.S. equities	25	25	22	22	28	29	28	28
Fixed income	31	30	30	29	31	28	32	35
Non-U.S. equities	17	19	17	20	17	20	18	19
Alternative strategies	22	21	26	25	20	16	14	11
Private equity (LBOs, mezzanine, M&A funds and international private equity)	2	2	3	3	2	3	1	0
Marketable alternative strategies (hedge funds, absolute return, market neutral, long/short, 130/30, event-driven and derivatives)	13	13	15	15	12	9	11	9
Venture capital	1	1	1	1	1	1	0	0
Private equity real estate (non-campus)	2	2	3	3	2	2	1	1
Energy and natural resources	2	1	2	2	2	1	1	1
Commodities and managed futures	1	1	1	1	1	0	0	0
Distressed debt	1	1	1	0	0	0	0	0
Short-term securities/cash/other	5	5	5	4	4	7	8	7
Short-term securities/cash	4	4	4	4	3	4	7	7
Other	1	1	1	0	1	3	1	0

*equal-weighted

Figure 3.6A/EW **Investable Assets | Alternative Strategies Asset Mix* for Fiscal Years 2016 and 2017**

numbers in percent (%)	Total Organizations		Over $1 Billion		$501 Million-$1 Billion		Under $501 Million	
Responding organizations	50	52	28	34	11	9	11	9
	'16	'17	'16	'17	'16	'17	'16	'17
Type of investment strategy								
Private equity (LBOs, mezzanine, M&A funds and international private equity)	10	11	11	11	11	17	4	4
Marketable alternative strategies (hedge funds, absolute return, market neutral, long/short, 130/30, event-driven and derivatives)	62	63	56	60	62	56	78	75
Venture capital	4	4	5	4	6	9	0	0
Private equity real estate (non-campus)	9	9	11	11	8	9	8	9
Energy and natural resources	8	7	9	7	8	6	4	7
Commodities and managed futures	4	4	5	5	4	2	4	2
Distressed debt	3	2	3	2	1	1	2	3

*equal-weighted

Figure DB.6A/EW **Defined Benefit Plans | Detailed Asset Allocations* for Fiscal Years 2016 and 2017**

numbers in percent (%)	Total Organizations	
Responding organizations	32	32
	'16	'17
U.S. equities	25	22
Fixed income	38	40
Non-U.S. equities	18	19
Alternative strategies	17	16
Private equity (LBOs, mezzanine, M&A funds and international private equity)	2	2
Marketable alternative strategies (hedge funds, absolute return, market neutral, long/short, 130/30, event-driven and derivatives)	9	10
Venture capital	0	0
Private equity real estate (non-campus)	3	3
Energy & natural resources	1	1
Commodities and managed futures	1	0
Distressed debt	1	0
Short-term securities/cash/other	2	3
Short-term securities/cash	2	2
Other	0	1

*equal-weighted

Figure DB.10/EW **Defined Benefit Plans | Alternative Strategies Asset Mix* for Fiscal Years 2016 and 2017**

numbers in percent (%)	Total Organizations	
Responding organizations	25	26
	'16	'17
Type of investment strategy		
Private equity (LBOs, mezzanine, M&A funds and international private equity)	10	12
Marketable alternative strategies (hedge funds, absolute return, market neutral, long/short, 130/30, event-driven and derivatives)	60	61
Venture capital	2	1
Private equity real estate (non-campus)	16	15
Energy and natural resources	8	7
Commodities and managed futures	2	2
Distressed debt	2	2

*equal-weighted

Appendix III
Participating Healthcare Organizations

A

Allina Health System, MN

B

Bon Secours Health System, MD

C

CareAlliance Health Services dba Roper St. Francis Healthcare, SC

Carilion Clinic, VA

Catholic Health Initiatives, CO

Children's Health System of Texas, TX

Children's Health System, Inc., VA

Children's Healthcare of Atlanta, GA

Children's Hospital & Medical Center, NE

Children's Hospital and Health System, Inc., WI

Children's Hospital Colorado, CO

Children's Hospital Los Angeles, CA

The Children's Hospital of Philadelphia Foundation, PA

Children's Hospitals and Clinics of Minnesota, MN

The Children's Mercy Hospital, MO

The Children's Mercy Hospital Foundation, MO

Children's of Alabama, AL

CHOC Children's, CA

Community Foundation of Northwest Indiana, Inc., IN

D

Dignity Health, CA

E

East Tennessee Children's Hospital Association, Inc., TN

F

Fairview Health Services, MN

Franciscan Missionaries of Our Lady Health System, LA

G

Greenville Health System, SC

J

Johns Hopkins All Children's Hospital, Inc., FL

K

Kaiser Foundation Health Plan, CA

L

Ann & Robert H. Lurie Children's Hospital of Chicago, IL

M

Mercy Health, OH

MidMichigan Health, MI

Montage Health, CA

N

Nationwide Children's Hospital, OH

Nicklaus Children's Hospital, FL

North Mississippi Health Services, Inc., MS

Norton Healthcare, Inc. , KY

P

Parkview Health, IN

Piedmont Healthcare, Inc., GA

Presbyterian Healthcare System, NM

Providence St. Joseph Health, WA

R

Rady Children's Hospital and Health Center, CA

Rush University Medical Center, IL

S

Scripps Health, CA

Seattle Children's Hospital, WA

Sisters of Charity Health System, OH

Southcoast Health System, MA

Southern Illinois Healthcare, IL

SSM Health, MO

T

Texas Children's Hospital, TX

Texas Scottish Rite Hospital for Children, TX

Trinity Health, MI

U

University Hospitals Health System, Inc., OH

V

Vanderbilt University Medical Center, TN

Vidant Health , NC

W

Wake Forest Baptist Health, NC

West Virginia United Health System, Inc. d/b/a West Virginia University Health System, WV

Y

Yale-New Haven Health System, CT

Appendix IV
Glossary of Terms

501(c)(3) Section of the Internal Revenue Code that designates an organization as charitable and tax-exempt. Organizations qualifying under this section include religious, educational, charitable, amateur athletic, scientific or literary groups, organizations testing for public safety and organizations involved in prevention of cruelty to children or animals. Most organizations seeking foundation or corporate contributions secure a Section 501(c)(3) classification from the Internal Revenue Service (IRS).

absolute return Strategies intended to be market neutral (i.e., not dependent on the overall direction of the markets) which include such underlying strategies as: distressed debt, merger arbitrage, fixed income arbitrage, convertible bond arbitrage and equity market neutral (i.e., offsetting long and short positions).

accumulated benefit obligation (ABO) An approximate measure of a pension plan's liability based on the assumption that the pension plan is to be terminated and thus does not need to consider future increases in compensation.

active management (see passive investing; passive management) The management of a portfolio whose investments may be traded at any time.

active MSCI ex-U.S. (developed) The MSCI World ex-U.S. Index is a capitalization-weighted index of equities in the entire developed world other than the United States. The designation of a country as developed arises primarily as a measurement of GDP per capita. There are 22 countries within this index. Active (long) equity investment strategies in listed stocks of exchanges in developed economies excluding the U.S. Such international investments typically use the Morgan Stanley Capital International World ex-U.S. Index (MSCI World ex-U.S.) or a comparable index as a benchmark.

alternative strategies A broad classification of investments that includes any investment that is considered less traditional or non-traditional (traditional assets include stock instruments and debt instruments, such as direct investments or mutual fund investments in equities, bonds, and money market instruments). Specific examples of alternative strategies include private equity, venture capital, hedge funds, distressed (or private) debt, and "real assets" (such as real estate, oil and natural gas, timber and commodity funds). Alternative investments often have a low or negative correlation to traditional assets, can contribute to lower portfolio risk (as measured by volatility), and can contribute to a higher expected return.

annuity trust A trust that pays an agreed-upon sum of money at agreed-upon intervals, drawing from the trust's principal when income from the trust is insufficient to make the agreed-upon payments.

arbitrage A financial transaction or strategy that seeks to profit from a perceived price differential with respect to related instruments and typically involves the simultaneous purchase and sale of those instruments.

asset allocation Allocating investments among different asset classes (e.g., stocks, bonds, and real estate) to find the optimal risk/reward mix. Tactical asset allocation implies a relatively short-term, and strategic asset allocation a longer-term, approach.

asset mix The proportions of a portfolio invested in various types of investments, such as common stock, bonds, guaranteed investment contracts, real estate and cash equivalents.

asset-backed security A fixed income instrument comprising collateralized assets that pay interest, such as consumer credit cards and automobile loans.

balanced fund manager (balanced manager) A mutual fund manager whose investment policy is to balance the fund's portfolio by investing in more than one asset class—typically stocks, bonds, and cash—to obtain a good return, while minimizing risk.

banded inflation A spending rule pursuant to which the annual dollar amount of spending grows by a designated rate of inflation, subject to upper and lower limits to the total spending rate expressed in percentage terms. For example, the rule may call for last year's spending to be increased by HEPI each year but to be not below 3 percent nor above 6 percent of assets in any given year.

Barclays Aggregate Bond Index An index that covers the U.S. investment grade, fixed-rate bond market with index components for government, corporate, mortgage pass-through and asset-backed securities.

basis point One one-hundredth of a percentage point.

benchmark risk (see risk relative to benchmark)

bequest A type of donation or gift, typically via a decedent's will or estate. Bequests and gifts are awards with few or no conditions specified. Gifts may be provided to establish an endowment or to provide direct support for existing programs. Frequently, gifts are used to support developing programs for which other funding is not available. The unique flexibility, or lack of restrictions, makes gifts attractive sources of support.

block grant A type of mandatory grant where the recipients (normally, states) have substantial authority over the type of activities to support, with minimal federal administrative restrictions. The basic premise is that states should be free to target resources and design administrative mechanisms to provide services to meet the needs of their citizens.

bond Evidence of a debt on which the issuing company usually promises to pay holders a specified amount of interest for a specified length of time and to repay the principal on the maturity date. A bond represents debt and its holder is a creditor of the corporation and not a part owner as is a shareholder. Utility bonds are usually secured by mortgages.

buy-and-hold portfolio A portfolio for which the investment manager buys securities, usually bonds, with the intention of holding them for a long period of time, usually until maturity, in contrast with an actively managed portfolio. The term may also apply to common stocks such as those held by an index fund.

capital gain Profit on the sale of an investment, which may include common stock, corporate and government bonds, real estate and other real assets. There are long- and short-term capital gains, as defined in the Internal Revenue Code. Capital losses may also occur.

capital markets Markets in which capital funds (debt and equity) are issued and traded. Included are private placement sources of debt and equity, as well as organized markets and exchanges.

cash and cash equivalents Assets with maturities of less than one year (e.g., Treasury bills, commercial paper, certificates of deposit and nonconvertible bonds) which are highly liquid and comparatively risk-free.

cash management Bank services designed to help a company manage its cash more efficiently. These services include payable-through drafts, zero-balance accounts, remote disbursement accounts, account reconciliation, lockboxes, depository transfer checks, freight payment plans, wire transfers, concentration accounts, information reporting and cash management consulting.

challenge grant A grant that provides monies in response to monies from other sources, usually according to a formula. A challenge grant may, for example, offer two dollars for every one that is obtained from a fund drive. The grant usually has a fixed upper limit, and may have a challenge minimum below which no grant will be made. This form of grant is fairly common in the arts, humanities, and some other fields, but it is less common in the sciences. A challenge grant differs from a matching grant in at least one important aspect. The amount of money that the recipient organization realizes from a challenge grant may vary widely, depending on how successful that organization is in meeting the challenge. Matching grants usually award a clearly defined amount and require that a specific sum be obtained before any award is made.

charitable gift annuity A contract between the donor and a charity in which the donor transfers assets to the charity. The charity agrees to pay a specified sum of money each year to the donor, for a fixed period (usually life). The assets exceed the present value of the expected payments to the donor, and the charity receives the surplus (mortality tables are used to make this calculation). The donor can claim as a charitable tax deduction the difference between the present value of the expected payments and the value of the assets.

charitable lead trust (also called charitable income trust) A trust in which the donor transfers income-producing assets to a trustee and instructs the trustee to pay a fixed amount or annual percentage to charity for the term of the trust. At the end of the trust term, assets remaining in the trust are conveyed to the donor or his/her beneficiary or beneficiaries. The donor can claim as a charitable tax deduction the present value of the expected payments to charity.

charitable remainder annuity trust A trust that pays the donor or the donor's beneficiary an agreed-upon annual income for the life of the donor or for a specific term. The principal remaining from this type of trust eventually passes to a qualified charity.

charitable remainder trust The assets left in a charitable trust, gift annuity, or pooled income fund that eventually pass to a qualified charity. The present value of the charitable remainder is equal to the charitable tax deduction.

charitable remainder unitrust Under Internal Revenue Code Section 664(d)(2) and the regulations thereunder, there are three variations of the unitrust:

"straight" unitrust Donor irrevocably transfers money, securities or property to a separately invested trust having a charitable remainder. The trust makes payments to named beneficiaries at least annually in an amount equal to a fixed percentage (not less than 5 percent) of the net fair market value of the trust assets, determined once each year. The donor may designate himself and/or other beneficiaries to receive these payments for life, so long as the designated beneficiaries are alive at the time the trust is created. Alternatively, the trust instrument may provide for payment to be made for a term of years, not to exceed 20. At the expiration of all income interests the assets are distributed to the charitable organization(s).

"net income" unitrust The same as a "straight" unitrust except the payments to the beneficiary are limited to the actual income earned by the trust up to, but not exceeding, the fixed percentage stated in the trust agreement.

"net plus markup" unitrust Payments limited to ordinary earned income as in the "net income" unitrust, except that payments may exceed the stated percentage up to, but not exceeding, the amount required to make up any accumulated deficiencies from prior years (years in which the trust earned less than the stated percentage).

charity In its traditional legal meaning, the word "charity" encompasses religion, education, assistance to the government, promotion of health, relief of poverty or distress and other purposes that benefit the community. Nonprofit organizations that are organized and operated primarily to further one of these purposes generally will be recognized as exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code and will be eligible to receive tax-deductible

collateralized mortgage obligation (CMO) A structured mortgage bond, backed by a pool of mortgages that serves as collateral for the bond, that pays interest and principal in maturity succession. The bond is repaid in series from the mortgage proceeds (i.e., principal payments go against the Series A bond {lowest interest and maturity} until it is paid off, at which time all payments go against the next series bond {Series B}). This procedure acts as call protection against a series bond with a higher interest rate and a longer maturity, since it cannot be called until the prior series is paid off.

common stock Securities that represent an ownership interest in a corporation. A common stockholder is not a creditor of the corporation, so he or she assumes greater risk than does a creditor but shares in earnings and growth through dividends and price appreciation.

community foundation A 501(c)(3) organization that makes grants for charitable purposes in a specific community or region. The funds available to a community foundation are usually derived from many donors and held in an endowment that is independently administered; income earned by the endowment is then used to make grants. Although a community foundation may be classified by the IRS as a private foundation, most are public charities and are thus eligible for maximum tax-deductible contributions from the general public.

community fund An organized community program which makes annual appeals to the general public for funds that are usually not retained in an endowment but are instead used for the ongoing operational support of local agencies.

compliance risk The possibility that existing procedures do not adequately ensure that a fund and its managers adhere to the regulations and requirements of governmental and regulatory bodies and industry standards of practice or that the record-keeping of compliance documentation is not sufficient to show that the fund and its managers have been in compliance with those standards.

consortium grant A grant to one institution in support of a project in which any programmatic activity is carried out through a collaborative arrangement between or among the recipient institution and one or more other institutions or organizations which are separate legal entities, administratively independent of the recipient. The involvement of the non-recipient (collaborating) institutions is that of actually performing a portion of the programmatic activity.

convertible arbitrage A strategy that seeks to take advantage of the pricing inefficiencies of the embedded option in a convertible bond. It is generally characterized by a long convertible position and corresponding short position in the underlying stock. Convertible arbitrage may also use leverage.

convertible bond A bond or preferred stock that can be turned into common stock at a predetermined conversion rate, frequently at predetermined times. Conversion is often forced by the issuer by calling the bond or preferred stock prior to its maturity.

corporate foundation A private foundation (company-sponsored) that derives its grant-making funds primarily from the contributions of a profit-making business. The company-sponsored foundation often maintains close ties with the donor company, but it is a separate legal organization, sometimes with its own endowment, and is subject to the same rules and regulations as other private foundations.

corporate giving program A grant-making program (direct giving) established and administered within a profit-making company. Gifts or grants go directly to charitable organizations from the corporation. Corporate foundations/giving programs do not have a separate endowment; their expense is planned as part of the company's annual budgeting process and usually is funded with pre-tax income. Annual grant totals generally are directly related to company profits.

core portfolio A portfolio, closely resembling the structure and risk of the total market, that can be actively or passively managed.

corporate bond A fixed income security issued by a corporation to evidence borrowing, usually with a term in excess of five years.

counterparty A principal to a foreign exchange, swap, or other derivative instrument, as opposed to an agent such as a broker.

credit/counterparty risk (see financial risk) The potential that the issuer of a security may default or fail to honor their financial obligations to the fund or its client. The risk that a counterparty (or participant in a securities transaction) does not meet its financial obligation, thereby resulting in a financial loss for the transaction.

cultural institution A cultural institution is an operating nonprofit (or a foundation that directly supports such an entity) that supports the arts and other cultural endeavors (e.g., museums, art galleries, symphonies, libraries). These are not grant-making organizations; rather, they are typically recipients of grants from private and public foundations.

debt fund (see fixed income portfolio) A portfolio of debt-oriented investments (e.g., real estate mortgages) or fixed income securities (e.g., corporate bonds).

dedicated bond portfolio A portfolio of debt-oriented securities that is structured to meet a specific liability such as the payment of benefits to a group of retirees for the remainder of their life. The portfolio is dedicated to the objective of meeting the identified liability.

default risk (see credit/counterparty risk; financial risk)

deferred payment gift annuity A charitable gift annuity in which payments to the donor are deferred until such time as they can be made at a higher rate (shorter life expectancy) and may be taxable at a lower rate.

derivative A financial instrument whose value depends upon the value of another instrument or asset (typically an index, bond, equity, currency or commodity). Examples are futures, forwards and options.

distressed debt (see event driven strategy) Publicly held and traded debt and equity securities, as well as bank loans, of companies and governments that are in financial "distress." Financial distress is indicated by having filed or being near to filing for protection under Chapter 11 of the U.S. Bankruptcy Code. Distressed public debt and related bank loans trade at risk premiums generally in excess of 10 percentage points to U.S. Treasury securities of comparable duration.

distribution committee The committee responsible for making grant decisions. For community foundations, the distribution committee is intended to be broadly representative of the community served by the foundation.

dollar-weighted return Also called the internal rate of return (IRR); the interest rate that makes the present value of the cash flows from all the subperiods in an evaluation period plus the terminal market value of the portfolio equal to the initial market value of the portfolio.

divestment Divestment of fossil fuels is to actively rid an investment portfolio of holdings in fossil fuel companies. Divestment of fossil fuel companies is a type of exclusionary screening strategy through which investors exclude companies involved in fossil fuels from their portfolio.

donation Transfer of equipment, money, goods, services, and property with or without specifications as to its use. Sometimes donation is used to designate contributions that are made with more specific intent than is usually the case with a gift, but the two terms are often used interchangeably.

donor-advised fund A fund held by a community foundation or other qualified sponsoring organization where the donor, or a committee appointed by the donor, may recommend eligible charitable recipients for grants from the fund. The community foundation's governing body must be free to accept or reject the recommendations.

donor-designated fund A fund held by a community foundation where the donor has specified that the fund's income or assets be used for the benefit of one or more specific public charities. These funds are sometimes established by a transfer of assets by a public charity to a fund designated for its own benefit, in which case they may be known as grantee endowments or agency funds. The community foundation's governing body must have the power to redirect resources in the fund if it determines that the donor's restriction is unnecessary, incapable of fulfillment or inconsistent with the charitable needs of the community or area served.

EAFE The Europe, Australia, and Far East Index from Morgan Stanley Capital International. An unmanaged, market-value weighted index designed to measure the overall condition of overseas markets.

emerging growth fund (see emerging growth stock; emerging markets fund) A fund that consists of the stocks of emerging growth companies, typically higher risk stocks in defined market segments such as high tech and medical technology.

emerging growth stock (see emerging growth fund) The stock of a relatively small company that is growing very rapidly but is not large enough or has not been in business long enough to be of investment quality.

emerging markets fund (see emerging growth fund) A fund that consists of investments in markets of emerging countries, such as some of those in Southeast Asia and Central and South America.

endowment (see quasi-endowment, term endowment, true endowment) The permanent funds of a nonprofit institution, consisting of cash, securities or property. Income from endowment is used to help finance the ongoing operations of the institution. "True" endowment is that portion of the funds that are commonly restricted as to use of principal and/or income. Not all endowments are true endowments, as some may be funds functioning as endowment by vote of the governing board.

endowment (Foundations and Operating Charities) The principal amount of gifts and bequests that are accepted subject to a requirement that the principal be maintained intact and invested to create a source of income for a foundation. Donors may require that the principal remain intact in perpetuity, or for a defined period of time, or until sufficient assets have been accumulated to achieve a designated purpose.

environmental, social and governance (ESG) investing An investment practice that involves integrating the three ESG factors into fundamental investment analysis to the extent that they are material to investment performance.

equity, equities (stock) 1) The total ownership interest in a company of all common and preferred stockholders. 2) Ownership interests in companies, often producing current income paid in the form of quarterly dividends, that can be traded in public equity markets. As an asset class, may include convertible bonds (if held as an opportunistic means of eventually acquiring a company's stock) and warrants, rights, options and futures (if the underlying assets are equities).

equity derivative Any financial instrument, such as options or futures, priced off of individual stocks or groups of stocks.

equity market neutral A strategy designed to exploit equity price inefficiencies. It typically involves using balanced long and short positions in equity markets to insulate the portfolio from overall market risk. Equity market portfolios are often designed to be neutral relative to beta, sector, industry, market capitalization, and style, among other factors. Leverage may be applied to enhance returns.

equity portfolio A portfolio of equity-oriented securities such as common stock or equity real estate.

equity real estate The ownership interest possessed by shareholders in a real estate investment.

environmental, social and governance (ESG) investing, involves integrating ESG factors into fundamental investment analysis to the extent that they are material to investment performance.

event driven strategy Seeks to take advantage of anticipated corporate events and to capture price movement generated by these events. Two of the better known event driven strategies are merger arbitrage and distressed debt.

family foundation An independent private foundation whose funds are derived from members of a single family. Family members often serve as officers or board members of family foundations and have a significant role in their grant-making decisions.

fiduciary A person, committee or institution that holds assets in trust for another. The property may be used or invested for the benefit of the owner, depending on the agreement.

fiduciary risk The potential exposure of fiduciaries to legal and regulatory actions precipitated by a breakdown in controls, or the failure to execute due diligence on behalf of the beneficiaries.

financial risk (see credit/counterparty risk) The possibility that a bond issuer will default, i.e., fail to repay principal and interest in a timely manner. Also called default risk.

fiscal year (FY) Accounting period covering 12 consecutive months, 52 consecutive weeks, 13 four-week periods, or 365 consecutive days at the end of which the books are closed and profit and loss are determined. An institution's fiscal year is often, but not necessarily the same as the calendar year.

fixed income arbitrage A strategy to capture the disparities of pricing across the global fixed income markets and related derivatives. Some of the more common fixed income arbitrage strategies find opportunity in yield curve anomalies, volatility differences and bond futures versus the underlying bonds. Leverage is often used to enhance returns.

fixed income portfolio A portfolio of fixed income securities, such as marketable bonds, private placements, real estate mortgages and guaranteed investment contracts.

Form 990/Form 990-PF The IRS forms filed annually by public charities and private foundations, respectively. The letters PF stand for private foundation. The IRS uses this form to assess compliance with the Internal Revenue Code. Both forms list organization assets, receipts, expenditures and compensation of officers. Form 990-PF includes a list of grants made during the year by the private foundation.

foundation An entity which exists to support a charitable institution and which is funded by an endowment or donations.

fund of funds An approach to investing in which a manager invests in various funds formed by other investment managers. The benefits of this approach include diversification, the expertise of the fund-of-funds manager, access to hedge fund managers who may be otherwise unavailable and a less intense commitment of staff resources by the investor.

general purpose foundation An independent private foundation that awards grants in many different fields of interest.

gift Gifts and bequests are awards given with few or no conditions specified. Gifts may be provided to establish an endowment or to provide direct support for existing programs. Frequently, gifts are used to support developing programs for which other funding is not available. The unique flexibility, or lack of restrictions, makes gifts attractive sources of support.

global macro A global, top-down approach to investing in which managers will take long or short positions in fixed income, equity, currency and commodity markets.

global portfolio (see international portfolio) An investment portfolio (of equities or bonds) that can invest in U.S. and non-U.S. markets. government bond A security issued by a federal, state, or city government to evidence borrowing, with a term usually in excess of 10 years.

government bond A security issued by a federal, state, or city government to evidence borrowing, with a term usually in excess of 10 years.

grant A type of financial assistance awarded to an organization for the conduct of research or other program as specified in an approved proposal. A grant, as opposed to a cooperative agreement, is used whenever the awarding office anticipates no substantial program involvement with the recipient during the performance of the archives.

grantee financial report A report detailing how grant funds were used by an organization. Many corporate grantmakers require this kind of report from grantees. A financial report generally includes a listing of all expenditures from grant funds as well as an overall organizational financial report covering revenue and expenses, assets and liabilities. Some funders may require an audited financial report.

growth stock Stock in a company that has shown better-than-average growth in earnings and is expected to continue to do so. It can pay little or no dividends but is expected to have growth potential over an extended period of time.

hedge fund (see marketable alternative strategies [hedge funds])

HEPI® The Commonfund Higher Education Price IndexTM (HEPI), which reports price information for the goods and services purchased by colleges and universities for their current operations. Colleges and universities use these measures to analyze the impact of inflation on their operations as a starting point for securing additional revenues to meet expected higher costs, so as to preserve their purchasing power.

HR7 A Bill introduced to Congress in 2001, designed to provide incentives for charitable contributions by individuals and businesses, to improve the effectiveness and efficiency of government program delivery to individuals and families in need, and to enhance the ability of low-income Americans to gain financial security by building assets.

high yield bond (junk bond) A lower-quality rated bond, rated BB or lower by Standard & Poor's and Ba or lower by Moody's, is called high yield because the interest rate is higher than average to compensate investors for taking higher-than-average risk.

impact investing Investing in projects, companies, funds or organizations with the express goal of generating and measuring mission-related social or environmental change alongside financial return.

income stabilization reserve A percentage of the total withdrawal set aside in a separate fund to be used to augment spending in a down year. Employed as a smoothing device to lessen any decrease in the transfer to operating budget in a given year.

independent foundation These private foundations are usually founded by one individual, often by bequest. They are occasionally termed "non-operating" because they do not run their own programs. Sometimes individuals or groups of people, such as family members, form a foundation while the donors are still living. Many large independent foundations, such as the Ford Foundation, are no longer governed by members of the original donor's family but are run by boards made up of community, business and academic leaders. Private foundations make grants to other tax-exempt organizations to carry out their charitable purposes. Private foundations must make charitable expenditures of approximately 5 percent of the market value of their assets each year. Although exempt from federal income tax, private foundations must pay a yearly excise tax of 1 or 2 percent of their net investment income.

index fund (see international index fund) A portfolio of stocks structured to replicate the performance of a commonly used index, such as the S&P 500.

indexing (see passive investing; passive management) A passive investment strategy in which a portfolio is designed to mirror the performance of a stock index, such as the S&P 500. Also, tying taxes, wages or other measures to an index.

in-kind contribution (see third-party in-kind contribution) Contributions or assistance in a form other than money. Real property, equipment, materials, or services of recognized value that are offered in lieu of cash. international index fund (see index fund) A portfolio of stocks structured to replicate an index of international securities such as the MSCI World ex-U.S. Index or MSCI EAFE Index.

international index fund (see index fund) A portfolio of stocks structured to replicate an index of international securities such as the MSCI World ex-U.S. Index or MSCI EAFE Index.

international portfolio (see global portfolio) An investment portfolio (of equities or bonds) that can invest only in non-U.S. markets.

investment return The total amount that an investor or an investment fund earns from its investments, including both realized and unrealized capital gains (appreciation/depreciation) and income (dividends and interest).

junk bond (see high yield bond)

laddered cds (certificates of deposit) A cash management practice whereby an institution invests in bank certificates of deposit which mature at regularly spaced intervals thereby ensuring that it has access to ready cash while still being able to protect its capital and earn some current income.

large cap fund A fund that invests in stocks with larger market capitalizations, generally $5 billion or more.

liquidity risk Covers the failure to maintain sufficient funds (cash and marketable securities) to meet short-term obligations. Also, market liquidity risk is the difficulty in liquidating certain investments due to the lack of active markets in these securities.

long/short equity Long/short equity funds take long and short positions in listed equities—generally with a net long position. Managers seek to find (buy) stocks which are "undervalued" by the market and short stocks whose prices are "overvalued" by the market.

macro Macro managers use long and short strategies based on their view of the overall market direction as influenced by major global economic trends and events. Investments can include stocks, bonds, currencies, and commodities in the form of cash or derivatives instruments of both developed and emerging economies. Macro strategies often use moderate amounts of leverage.

manager, investment manager A firm, committee or individual, inside or outside an institution responsible for making decisions to buy, hold or sell assets. May also be called a money manager or investment adviser.

market risk The possibility of loss due to large movements in market prices (e.g., due to changes in interest rates, foreign exchange rates, volatility, correlation between markets, capital flows).

marketable alternative strategies (hedge funds) A fund, usually a limited partnership, used by wealthy individuals and institutions. Hedge funds are allowed to use aggressive strategies including selling short, leverage, program trading, swaps, arbitrage and derivatives. Since most are restricted by law to less than 100 investors, the minimum investment is typically $1 million. The general partner usually receives performance-based compensation and invests significantly in the partnership.

marketable securities Publicly traded securities, such as stocks, bonds or notes, which, as such, are easily bought and sold in the marketplace and readily convertible to cash.

matching grant A grant that requires a specified portion of the cost of the supported item of equipment or project be obtained from other sources. The required match may be more or less than the amount of the grant. Some matching grants require that the additional funds be obtained from sources outside the recipient organization. Many matching grants are paid in installments, the payments coinciding with the attainment of pre-specified levels of additional funding. Matching grants are very common in the sciences, especially for equipment. They are the standard practice in some government agencies.

merger arbitrage (see event driven strategy) Long and short positions are held in both companies that are involved in a merger or acquisition. Merger arbitrageurs are typically long the stock of the company being acquired and short the stock of the acquirer. The principal risk of this strategy is deal risk.

mid-cap fund A fund that specializes in stocks with market capitalizations generally in the range of $2 billion to $10 billion.

modeling risk The potential for loss due to actions taken or to policies implemented based on views of the world, in general, and the investment community, in particular, that are derived from improper models. These views are derived from representation(s) of reality that do not capture all significantly relevant information or are inappropriately applied throughout the investment program.

money market fund (MMF) A fund managed by an investment banking firm, investment manager, or insurance company, in which short-term funds of individuals, institutions, and corporations may be invested. These funds are invested in money market instruments.

money market instrument A short-term debt security, including Treasury bills, bank CDs, commercial paper, Eurodollar CDs, and Yankee CDs, among others. Money market instruments have maturities of a year or less.

mortgage-backed security A security for which investors receive payments out of the interest and principal on the underlying mortgage.

multi-strategy fund A fund providing exposure, in a single investment, to several investment styles and strategies in addition to a disciplined asset allocation process and ongoing rebalancing. A multi-strategy fund seeks to add alpha over a full market cycle, while providing significant risk reduction through diversification of manager and investment styles.

mutual fund An investment company or trust in which a number of investors pool their funds and receive units in the fund that are priced daily. There are many types of mutual funds: stock funds, bond funds, money market funds, and closed- and open-end investment funds. Participants in these funds also cover a wide range of investors (e.g., individuals, pension funds, and trust funds).

operating foundation A 501(c)(3) organization classified by the IRS as a private foundation whose primary purpose is to conduct research, social welfare, or other programs determined by its governing body or establishment charter. An operating foundation may make grants, but the amount of grants awarded generally is small relative to the funds used for the foundation's own programs.

operational risk The potential for discontinuity due to the possibility of a breakdown in operational procedures particularly as they relate to a process breakdown; this is distinct from the design, implementation, and maintenance of computerized information systems, e.g., errors resulting from a lack of reviewer function to catch errors, from incorrect data and/or lack of adequate staffing/backup.

passive account An account of stocks and/or bonds that is not actively managed.

passive/index MSCI ex-U.S. (developed) Equity investment strategies in the Morgan Stanley Capital International World ex-U.S. Index (MSCI World ex-U.S.) or a comparable index. The MSCI World ex-U.S. Index is a capitalization-weighted index of equities in the entire developed world other than the United States. The designation of a country as developed arises primarily as a measurement of GDP per capita. There are 22 countries within this index.

passive investing (see active management; indexing; passive management) A process that creates a portfolio of stock or bonds, not actively traded, that will replicate as closely as possible the performance of standard market indices such as the S&P 500 for stock or the Barclays Aggregate Index for bonds.

passive management (see active management; indexing; passive investing) Assets that are not traded actively but set up and held in an index fund.

performance measurement Various techniques for measuring the total rate of return (income received plus or minus changes in market value between two dates) of a pension or profit-sharing plan and of investment managers, generally in comparison with other plans and managers having similar investment objectives.

philanthropy Philanthropy is defined in different ways. The origin of the word philanthropy is Greek and means love for mankind. Today, philanthropy includes the concept of voluntary giving by an individual or group to promote the common good. Philanthropy also commonly refers to grants of money given by foundations to nonprofit organizations. Philanthropy addresses the contribution of an individual or group to other organizations that in turn work for the causes of poverty or social problems—improving the quality of life for all citizens. Philanthropic giving supports a variety of activities, including research, health, education, arts and culture, as well as alleviating poverty.

policy portfolio A portfolio of investment assets designed to achieve the financial and investment objectives of an institution over the long term. Policy portfolios are typically established by an investment committee which sets target percentages for each asset class and strategy selected for inclusion.

portable alpha The inclusion of a non-correlated strategy (i.e., one whose returns are independent of market performance) within an existing portfolio in order to improve risk-adjusted returns. The word "portable" is used because the strategy can be applied without affecting the style under which a particular portfolio is being managed.

portfolio Combined holdings of multiple stocks, bonds, commodities, real estate investments, cash equivalents or other assets by an individual or institutional investor. The purpose of a portfolio is to reduce risk by diversification.

portfolio diagnostics An analytical performance measurement approach that segregates a manager's investment performance into components such as value added from securities selection and value added from market timing.

portfolio optimization A process whereby an investor's bond portfolio is restructured to match anticipated cash inflow and outflow. Some reinvestment of early cash receipts is allowed.

portfolio restructuring The rebalancing of a large volume of equity in a portfolio at one time by selling baskets of stock and reinvesting the proceeds in other equity, debt, or cash securities.

preferred stock A class of favored stock whose holders have a claim on the company's earnings before payment can be made to common stockholders. Preferred stockholders are usually entitled to dividends at a specified rate, when declared by the board of directors, before payment is made to common stockholders, and they usually have priority if the company is liquidated; however, preferred stockholders generally do not have voting rights.

price/earnings ratio (P/E) The price/earnings ratio of a stock is calculated by dividing the current price of the stock by its trailing 12 months' earnings per share. The P/E ratio relates the price of the stock to the per-share earnings of the company. High P/E generally indicates that the market is paying more to obtain the stock because it has confidence in the company's ability to increase its earnings. Conversely, a low P/E often indicates that the market has less confidence that the company's earnings will increase rapidly or steadily, and therefore will not pay as much for its stock. In most cases, a fund with a high average P/E ratio has paid a premium for stocks that have a high potential for increased earnings. If the fund's average P/E is low, the manager may believe that the stocks have an overlooked or undervalued potential for appreciation. A P/E ratio calculated using a forecast of future earnings is called a forward P/E.

private equity Equity capital invested in a private company.

private foundation A nongovernmental, nonprofit organization with funds (usually from a single source, such as an individual, family, or corporation) and program managed by its own trustees or directors. Private foundations are established to maintain or aid social, educational, religious, or other charitable activities serving the common welfare, primarily through the making of grants.

private operating foundation A private foundation that uses the bulk of its resources to provide charitable services or run charitable programs of its own. It makes few, if any, grants to outside organizations and, like private independent and private family foundations, it generally does not raise funds from the public.

private placement A distribution of securities (including interests in commingled funds) made in a private manner and only to qualified investors. A private placement does not require registration with the SEC and is not offered to the public.

program-related investment (PRI) A loan or other investment (as distinguished from a grant) made by a foundation to another organization for a project related to the foundation's philanthropic purposes and interests.

projected benefit obligation (PBO) The actuarial liability equal to the present value of liabilities earned and the present value of liabilities from future compensation increases, i.e., the amount of money a plan sponsor must pay into a Defined Benefit plan to satisfy all pension entitlements.

proxy voting disclosure In an effort to improve the transparency of proxy voting by mutual funds and other registered investment vehicles, the SEC now requires registered investment management companies to provide disclosure about how they vote proxies relating to portfolio securities they hold. These amendments require registered investment management companies to disclose the policies and procedures that they use to determine how to vote proxies relating to portfolio securities. The amendments also require registered investment management companies to file with the Commission and to make available to shareholders the specific proxy votes that they cast in shareholder meetings of issuers of portfolio securities. The intent of the rule is to encourage funds to become more engaged in corporate governance of issuers held in their portfolio.

proxy voting policy A proxy statement is a document that provides shareholders with information about issues to be discussed and voted upon at a stockholders' meeting. Shareholders may attend the meeting and register their votes in person or vote by sending in proxy ballots on the various matters scheduled to come before the meeting. As investors and shareholders, nonprofits are frequently confronted with the issue of whether they should vote their shares as recommended by the company's management or analyze each issue in light of the institution's mission. Some nonprofits have adopted policies by which they either (i) vote their own proxies, (ii) assign the responsibility to a third party or (iii) have their investment managers vote the proxies, usually in accord with guidelines provided by the institution.

public charity A nonprofit organization that qualifies for tax-exempt status under section 501(c)(3) of the Internal Revenue Code and that derives its support from broad-based public sources. Public charities are the recipients of most foundation and corporate grants. Some public charities also make grants. Religious, educational and medical institutions are deemed to be public charities.

public foundation Legally classified as "public charities," public foundations are publicly supported nonprofit organizations and are predominantly funded by contributions from individuals, corporations, governmental units and private foundations. As distinguished from most public charities, public foundations focus more on grant-making than on providing direct charitable services.

public support test There are two public support tests, both of which are designed to ensure that a charitable organization is responsive to the general public rather than a limited number of persons. One test, sometimes referred to as 509(a) (1) or 170(b)(1)(A)(vi) for the sections of the Internal Revenue Code where it is found, is for charities like community foundations that mainly rely on gifts, grants, and contributions. To be automatically classed as a public charity under this test, organizations must show that they normally receive at least one-third of their support from the general public (including government agencies and foundations). However, an organization that fails the automatic test still may qualify as a public charity if its public support equals at least 10 percent of all support and it also has a variety of other characteristics—such as a broad-based board—that make it sufficiently "public." The second test, sometimes referred to as the section 509(a)(2) test, applies to charities, such as symphony orchestras or theater groups, that get a substantial part of their income from the sale of services that further their mission, such as the sale of tickets to performances. These charities must pass a one-third/one-third test. That is, they must demonstrate that their sales and contributions normally add up to at least one-third of their financial support, but their income from investments and unrelated business activities does not exceed one-third of support.

Q-TIP trust The Economic Recovery Tax Act of 1981 made available a planned giving vehicle which is similar to a qualified charitable remainder trust, but without the stringent technical requirements. A person can establish a "qualified terminal interest property trust" (Q-TIP trust) for the benefit of his/her spouse, with the remainder to the foundation. There is no charitable income tax deduction and the trust is not tax-exempt, because it is not a charitable remainder trust. However, the entire trust qualifies for the marital deduction in the first spouse's estate and for the charitable deduction in the second spouse's estate, and thus generates no tax with respect to either spouse's life interest or the charitable remainder trust. A Q-TIP trust with a charitable remainder is flexible. For example, trust payments to the surviving spouse need not be limited to an annuity or unitrust amount, but may be determined by the needs of the surviving spouse.

qualifying distributions Expenditures of a private foundation made to satisfy its annual payout requirement. These can include grants, reasonable administrative expenses, set-asides, loans and program-related investments, and amounts paid to acquire assets used directly in carrying out tax-exempt purposes.

quantitative portfolio A portfolio management approach using computer-based models or other quantitative methods to select securities and/or structure a portfolio.

quasi-endowment (see endowment, term endowment, true endowment) Endowment that is composed of unrestricted funds functioning as endowment by the vote of the Board of Trustees. These funds are distinct from the operating cash and reserves of the institutions, which has the effect of sheltering them from ad hoc spending. Nevertheless, these funds can be spent, by vote of the Board, for any purpose.

real property Land, including land improvements, structures and appurtenances thereto, but excluding movable machinery and equipment.

religious organization Both operating and grant-making nonprofits that are either directly affiliated with a church or religious order, or are strongly influenced by one.

request for proposal (RFP) The practice of institutional funds that seek to allocate funds to a specific investment style by requesting competing investment management firms and trust and custody banks to submit proposals detailing capabilities, prices and the like.

restricted funds Designated by a donor or board of trustees for a specific purpose, and cannot be used for any other purpose.

return (average, annual, total) Total return measures the annual return on an investment including the appreciation and dividends or interest. Total returns are calculated by taking the change in investment value, assuming the reinvestment of all income and capital gains distributions (plus any other miscellaneous distributions) during the period, and dividing by the initial investment value. These returns are not adjusted for sales charges, but they are adjusted for management, administrative and other costs that are automatically deducted from fund assets.

risk management The procedures necessary to manage exposure to various types of risk associated with transacting business or investments.

risk relative to benchmark (benchmark risk) The potential for losses due to unintended bets or a breakdown in due diligence; the impact of investment initiatives that were not fully understood at the outset and had the potential of unintended consequences; or the monetary impact (to the portfolio and the fund) of managers who violate guidelines, engage in unauthorized transactions, develop excessive concentrations (high trading error), commit fraud, etc.

S&P Standard & Poor's Corporation

S&P 500 A popular stock market index composed of 500 stocks selected by Standard & Poor's Corporation to represent the entire market and used by many funds to compare the investment performance of their equity-oriented managers.

single life gift annuity A charitable gift annuity based and paid on the life of one person.

small cap fund A fund that specializes in stocks with lower market capitalization; small cap stocks are usually $2 billion or less in market capitalization.

social services organization A social services organization is an operating nonprofit (and the category includes foundations that directly support them) that provides social programs to the public or that conducts research to benefit humanity (e.g., Boys and Girls Clubs, Blood Center, various research institutes). These are not grant-making organizations (rather they are typically recipients of grants from private and public foundations).

socially responsible investing A practice wherein investors screen or restrict certain investments based on social, environmental or political criteria. Restrictions can vary broadly depending on the investor's philosophy and may include restrictions based on issues of human rights, environmental impact, gambling, firearms, tobacco, etc.

spending policy or rule The guideline established by the board which determines the amount of the annual transfer of monies from the investable assets to the operating budget. Examples include: a) spend all income; b) spend 5 percent of a three-year moving average market value; c) increase spending by inflation each year.

spending rate The amount of spending specified by the board from the investable assets, usually expressed as an annual percentage of the beginning market value of the fund.

stewardship The management of assistance programs to be exercised by federal officials. Grants management officials oversee the process of evaluating and awarding grants and actively participate in the management of grants to ensure that funding is properly and prudently utilized, that all applicable laws and regulations are followed, and that the mission of the sponsor is furthered.

stock (see equity)

sunset policy A policy that specifies a termination date in the life of a nonprofit institution, such as a foundation or operating charity. The bylaws of many nonprofits do not address a termination date and they are therefore assumed to operate in perpetuity. An operating charity or foundation having a sunset policy would cease operations and distribute all its assets by a specified date. A high-visibility example is the Bill and Melinda Gates Foundation, which has specified that all of the foundation's resources will be spent within 50 years of Bill and Melinda Gates' deaths.

survivorship gift annuity A charitable gift annuity arranged during the donor's lifetime. A payment is made to the donor for life, then to the designated survivor for the rest of his/her life.

sustainability Institutional policies and practices that attempt to meet the material needs of present generations of users, without compromising the ability of future generations to enjoy a similar standard.

systems risk The risk that current system designs or implementations are inappropriate or ineffective to the extent that information obtained from or disseminated through the system environment is incorrect or incorrectly perceived, and the decisions made based on that information are sub-optimal. In addition, this includes the security of information in response to unauthorized access and disaster.

taxing of gifts The process by which all new gifts are assessed their proportionate share of the cost of managing the total endowment pool.

technical analysis Research to identify mispriced securities that focuses on recurrent and predictable stock price patterns and on proxies for buy or sell pressure in the market.

term endowment (see endowment, quasi-endowment, true endowment) Endowment that is restricted for a period of time, after which any remaining unused funds may become unrestricted (or quasi-endowment).

testamentary trust A trust established by the will of its creator for the benefit of survivors. This trust comes into being only after the death of the person whose will creates it. The will must be probated to bring the trust into existence.

third-party in-kind contribution (see in-kind contribution) The value of non-cash contributions directly benefiting a grant-supported project or program that are provided by non-federal third parties to the recipient, the sub-recipient, or a cost-type contractor under the grant or sub-grant without charge. In-kind contributions may be in the form of real property, equipment, supplies and other expendable property, and goods and services directly benefiting and specifically identifiable to the project or program.

true endowment (permanent endowment) (see endowment, quasi-endowment, term endowment) Endowment made up of funds that are restricted (usually by donor mandate) as to the use of principal or income, or both. Funds dedicated to scholarships or faculty support are the most common types of restricted endowments.

trust A legal agreement by which something of value is owned by a person or persons for the benefit of another. In practice, this means that a person transfers assets to a trust, which, for tax purposes, is a separate legal entity (this is not true, however, for revocable trusts).

trustee A foundation board member or officer who helps make decisions about how grant monies are spent. Depending on whether the foundation has paid staff, trustees may take a more or less active role in running its affairs.

UMIFA (see UPMIFA) First promulgated in 1972, the Uniform Management of Institutional Funds Act (UMIFA) has been replaced by the Uniform Prudent Management of Institutional Funds Act (UPMIFA).

underwater fund An individual "true" or restricted fund that has a market value that has decreased below its historic dollar value as defined by the Uniform Management of Institutional Funds Act (UMIFA). Historic dollar value is the aggregate fair value in dollars of (i) an endowment fund at the time established, (ii) subsequent contributions to the fund, and (iii) other additions to the fund required by the donor or law.

unit (see unitized accounting) A division of quantity accepted as a standard measurement of exchange. For example, in the commodities markets a unit of wheat is a bushel; the unit of U.S. currency is the dollar.

unitized accounting A method of managing an investment pool whereby the pool is divided into "units" which are assigned an arbitrary value (e.g., $10 per unit) at a particular point in time. Thereafter, each unit fluctuates in value according to the performance of the fund and the aggregate value of all the units is equal to the fund's current market value. Any new additions to or distributions from the fund are made in units and are assigned a value derived by dividing the total market value of the fund by the number of units.

unrestricted funds Monies with no requirements or restrictions as to their use or disposition.

UPMIFA (Uniform Prudent Management of Institutional Funds Act) This new uniform law, which was approved by the National Conference of Commissioners on Uniform State Laws in 2006 and has now been enacted in virtually all of the states, clarifies previously existing standards for the investment and expenditure of all types of charitable endowment funds. UPMIFA was designed to replace the existing Uniform Management of Institutional Funds Act (UMIFA), which dates from 1972. UMIFA was a pioneering statute, providing uniform and fundamental rules for the investment of funds held by charitable institutions and the expenditure of funds donated as "endowments" to those institutions. Those rules supported two general principles: 1) that assets would be invested prudently in diversified investments that sought growth as well as income, and 2) that appreciation of assets could prudently be spent for the purposes of any endowment fund held by a charitable institution. UPMIFA continues to follow these principles, while clarifying previously existing standards for the investment and expenditure of all types of charitable endowment funds. UMIFA in its original form excluded all trusts, a gap which led to the passage of the subsequent Uniform Prudent Investor Act and Uniform Principal and Income Act in most states. UPMIFA is intended to eliminate the need for multiple statutes by applying consistent investment and spending standards to all forms of charitable funds, whether held by institutions that are incorporated, unincorporated or organized as charitable trusts (i.e., trusts with a beneficial purpose but no named beneficiaries). It strengthens the concept of prudent investing, refining it further by means of specific guidelines for fiduciaries. It applies the rule of prudence to charitable spending, eliminating outmoded concepts such as historic dollar value while providing an optional section to restrain levels of spending that are deemed imprudently high. Finally, it facilitates the release or modification of restrictions on a fund, consistent with the recognition and protection of donor intent. Taken as a whole, UPMIFA establishes a stronger and more unified basis for charitable fund management.

value stock A stock that is considered to be a good stock at a great price, based on its fundamentals, as opposed to a great stock at a good price. Generally, these stocks are contrasted with growth stocks that trade at high multiples to earnings and cash.

venture capital Funds invested in a high-risk enterprise that is not large or mature enough for its shares to be publicly traded.

Yale/Stanford Rule Two types of hybrid spending rule, used by the respective institutions named. There are two parts to the calculation of the Yale rule. The first part, considered the stabilizing factor, takes the previous year's spending dollars and adjusts that figure for inflation (usually CPI or HEPI, but a school may also, like Yale, calculate its own inflation figure). This amount is given a weighting of 80 percent in the calculation. To this is added 20 percent of the figure that results when a targeted long-term spending rate (in Yale's case, 5.25 percent) is applied to a four-quarter market average of the endowment value. The Stanford rule is also a weighted average that uses the previous year's dollar spending, adjusted for inflation, and a targeted spending rate multiplied by the endowment value. The Stanford rule differs from the Yale rule in that it applies a lower weighting to the previous year's spending levels (60 percent), and a higher weighting to the targeted spending value (40 percent). In addition, Stanford's target spending rate is lower, at 5 percent, versus 5.25 percent for the Yale rule, and uses a single fiscal year-end valuation date.

yield The return on a security or portfolio, in the form of cash payments. Most yield comes from dividends on equities, coupons on bonds, or interest on mortgages. In general, yield is defined in terms of the component of return that is taxable as ordinary income. Consequently, since the capital gain on a Treasury bill or other discount note is viewed for tax purposes as a form of interest, it is also included in the definition of yield. Yield is usually described in percent terms (e.g., 7 percent per annum).

yield spread analysis The comparison of yield differential among varying types of fixed income securities. Professional investors watch for changes in normal yield spreads among many types of issues to identify overpriced situations (where they might sell securities they own) and underpriced securities (where they might buy).

yield-to-maturity The rate of return on a bond until its due date, including both interest payments and price changes. It is greater than the current yield when the bond is selling at a discount and less than the current yield when the bond is selling at a premium.

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