



## COUNCIL ON FOUNDATIONS

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# Council on Foundations Fact Sheet on the NCRP Report “Helping Charities, Sustaining Foundations”

Fact Sheet Date: June 2003

From the National Committee for Responsive Philanthropy (NCRP) report:

Foundations counted \$2 billion of their administrative costs toward their 5 percent charitable spending requirement in 1999, according to IRS data the NCRP uncovered. More recent data suggest that foundations may be counting up to \$4.3 billion of their administrative and operating expenses toward their charitable spending requirement, according to 2001 data from the National Center for Charitable Statistics (NCCS) at the Urban Institute that NCRP included in its assessment.

Council on Foundations Response:

**According to NCCS, the \$4.3 billion figure cited in the NCRP study as 2001 administrative and operating costs includes both expenditures by independent foundations (grantmakers that aid charitable activities) and expenditures by private operating foundations (those that conduct research or provide a direct service, making few grants). However, the IRS study cited for the "more than \$2 billion" in administrative costs in 1999 excluded operating foundation expenditures. There are more than 6,300 operating foundations, according to the Foundation Center.**

**Under current IRS reporting rules, most of the expenditures of these operating foundations are for direct charitable activities. Including them in the claimed administrative expense total for 2001, when they are excluded from the 1999 figure, is not an appropriate comparison and creates the apparent substantial increase in administrative expenses.**

**Another problem with the \$4.3 billion figure is that the tax returns in the NCCS data set used by NCRP include multiple years. This happened because the NCCS data includes all returns filed during 2001, so many returns covered calendar-year 2000 (which were due in 2001), fiscal year 1999 (many of which also were due during 2001) and returns for any other years for which foundations happened to file during 2001. In contrast, the IRS study covered only tax returns filed for the 1999 tax year.**

From the NCRP report:

The Council on Foundations and its members have long claimed that strict government oversight of the foundations community's administrative and operating expenditures is unnecessary, citing the seemingly high ethical standards within the community and its leadership.

Council Response:

**In fact, the opposite is true. The Council has asked, time and again, for an increase in IRS funds to conduct oversight.**



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### From the NCRP report:

Regarding perpetuity, NCRP cites our study by DeMarche Associates concluding foundations could have paid out 6.5 percent from 1950 to 1998.

### Council Response:

**The study only goes to 1998 -- the height of the bull market. In light of the recent and significant economic decline, the 6.5 percent number just wouldn't hold up.**

**That study, however, also shows that from the same period, 1950 to 1998, a foundation spending 5.5 percent (the .5 percent represents asset management expenses which do not count toward the charitable distribution) every year distributes \$1.3 million more than it would have if it had been spending 6.5 percent annually. This analysis confirms a study published by the IRS suggesting that in the long term, lower initial spending results in higher aggregate spending over time.**

### From the NCRP report:

Regarding perpetuity, a June 2001 study by Akash Deep and Peter Frumkin found that "as a group, the foundations in our sample have returned 7.62 percent annually on their assets."

### Council Response:

**According to the DeMarche study, since 1950 inflation has averaged about 4 percent a year. In addition to countering the effect of inflation on their assets, foundations also incur investment costs, which do not count toward the foundation's required distribution for charitable purposes. On average, these investment management expenses equal about 0.5% of assets each year. Accordingly, a foundation must earn an average return of 9.5 percent return on its investments to sustain the purchasing power of its corpus, pay its investment management costs, and distribute 5 percent of its assets annually for charitable purposes.**

**Even assuming that inflation never again goes above its current low average rate of 2.5 percent (CPI for the last 10 years), foundations still must obtain an average 8 percent return on their investments to support a charitable distribution of 5 percent. Foundations that achieve only a 7.62 rate of return will eventually spend themselves out of existence even at the 5 percent level.**