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A Donor's Declaration of Independence

Geoffrey Moss for The Chronicle Review

By Sylvia Kronstadt

When my father, an analytical chemist, died last May, my mother and I decided to honor him by endowing a scholarship fund for economically disadvantaged, academically deserving chemistry majors at our state university. Our intent was to provide one full-tuition scholarship annually to a student who had completed no less than a year of college-level course work with at least a 3.0 average and had demonstrated a commitment to a career in the sciences. We assumed that our substantial donation would continue to generate adequate funds for such scholarships in future years despite inflation, since we thought the university's investment professionals were certain to achieve returns that would meet—or more likely beat—inflationary trends.

But the way endowments actually work made a naïve fantasy of that simple, heartfelt dream. The university would provide to our scholarship recipients only a fraction of what our money was expected to earn each year. The rest of it—usually most of it, we eventually discovered—would be plowed back into the endowment "for future generations." Even during the boom years of the stock market, when the endowment was realizing double-digit returns, it had paid out only 4 percent. In 2009 it was reportedly paying just 3 percent but has since returned to the 4-percent rate. This, it turns out, is only slightly less than most endowment-payout rates across the country. Today nearly three-quarters of all colleges and universities set their endowment spending at about 5 percent.

Then we learned that tuition at the university has been rising at the rate of almost 10 percent a year. Thus our "full scholarship" would be "full" for only the first year, and would then decline precipitously as tuition continued to soar and the endowment payout remained a piddling fraction of its real value. It wouldn't be very long before our scholarship would join the hundreds (perhaps thousands) of others at the university that had been established as substantial gifts over the years but had dwindled into inconsequentiality. Meanwhile our initial, sizable donation would forever remain the property of the university—sitting there, earning money for the institution's highly prized, well-tended endowment—a sort of hothouse flower that gives little back except for the scintillating aroma of wealth.

(One dean admitted to me that he was hoping to "cobble together" some old donations that had lost most of their value in order to create several decent-size scholarships. To me, this honorable man's pragmatic and well-intentioned solution is nevertheless a sort of desecration, like consolidating graves to accommodate the needs of the present. It constitutes a breach of faith that I find disheartening.)

We regarded the way in which endowments are managed as an unacceptable betrayal of our intention. We were determined to help students *now,* and to do so in a high-impact way, giving them a year free of financial worries that could truly be transformative—resulting in better grades, priceless research opportunities, and a better chance at subsequent financial aid based on merit.

So, quite brashly, we created our own scholarship program, which we lightheartedly christened an "endearment." The concept is a twist on amortization: We will "spend down" our contribution, but with the benefit of accruing interest. We calculated a worst-case scenario and found that we would be able to provide full scholarships for about 15 years, possibly more. We will continue to offer the opportunity that a full scholarship provides, and the process will unfold while we are around to monitor how the money is spent and to enjoy the reward of aiding truly needy, deserving young people.

Our approach is similar to the one advocated by the Forum for the Future of Higher Education's Master Class in its report, "The Purposes and Uses of Endowment." "The promise of 'in perpetuity' for endowment gifts should be reconsidered," according to the report, which suggests that donors be encouraged "to make their gifts expendable—not in a single year, but perhaps over a 10-year period."

We had donated $100,000 to the university, expecting to endow a scholarship fund, until we learned about the downward trajectory of endowment payouts. When we decided to put into effect our own formula for disbursing the funds, we left them with the institution to hold and invest. But we dictated every aspect of the contract, specifying how and by what criteria the students would be selected, making certain that need and minority status were emphasized. We made provisions to be involved in the selection process to the extent that we wished. My mother and I have enjoyed the experience of helping our three initial Kronstadt Scholars so much that we have decided to augment our original payout with enough money to sponsor two additional students each year, depending upon the quality of the applicants.

This approach seems clean, simple, principled, and rather elegant. The notion that an endowment creates a "gift that keeps on giving" is seductive but disingenuous. Our gift really will "keep on giving," as our students plunge with even greater freedom and enthusiasm into their studies and then enter the work force as well-trained chemists, perhaps someday choosing to create their own scholarships.

It is clear that the traditional endowment model is geared more toward enlarging and perpetuating itself than toward actually assisting students or advancing the institution's overall mission. It feeds insatiably upon generous intentions, but in reality it seems transfixed by the pure grandiosity of being rich. Indeed, a number of state legislatures, as well as Congress, have considered requiring greater payouts by university endowments, which have repeatedly been accused of hoarding their wealth.

"Universities are behaving in a way to grow the endowment rather than using it to support the activities of the university," said Jeffrey R. Brown, a professor of finance at the University of Illinois at Urbana-Champaign, who wrote a working paper on the subject last year for the National Bureau of Economic Research. "The point is that if you think endowments exist to smooth over the shocks in bad times, they're not doing that. ... They're maintaining the value of the endowment for its own sake."

Numerous critics have challenged the validity of the tax-exempt status of endowments, arguing that they produce little societal value relative to the billions of dollars in lost state and federal tax revenue, both from donors' monies and from endowment earnings. Around the country, individual universities are hoarding millions—if not billions—of dollars in endowment assets, even as tuition increases keep many young people from pursuing a higher education and put many students tens of thousands of dollars in debt by the time they graduate.

Even those within academe have criticized endowments' payouts and warned that the public will see universities as "greedy," a view that will lead to reduced giving. Simply hoarding endowment funds for the future is an increasingly suspect strategy. "One of the most important stewardship steps in an endowment is to spend that endowment every year," Edward Schneider, executive director of the University at Buffalo Foundation, said last year. "Don't allow it to accumulate. There's less value in seeing it accumulate than there is in seeing it spent every year in a prudent sort of way consistent with donors' intent."

Indeed, the policy of paying out all earnings, rather than just a percentage, every year was generally practiced until the 1960s, when universities decided to leap into the realm of Wall Street speculation rather than invest their monies in secure, reliable instruments. Payouts have declined ever since, even as rates of return have soared.

The great allure of an endowment, of course, is the vision of perpetuity that it engenders, the promise of a kind of immortality: "The money I donate for scholarships will live on, in my name, from here to eternity." The discrepancy between rising tuition costs and penurious endowment payouts makes a lie out of that implied promise. But even if the discrepancy were not there, I would have a problem with the concept of perpetuity, particularly with regard to higher education. It has erected over the years a superstructure of administrative and ancillary functions, grand buildings and manicured terrain, that looms over the interchange between a teacher and a student that is its purported mission.

This ivory-tower empire cannot endure if we are ever again to offer higher education that is affordable for the average person. Fundamental change is essential. Thus, I do not believe in perpetuity. And so our scholarship will not have eternal life—but it will have a quality of life that the endowment would have denied it.

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