Making an impact: how philanthropy is evolving in the private client space

Kevin O'Connell

What does the future hold for private client philanthropy? We have witnessed a marked shift in recent years; one that is increasingly becoming a global phenomenon. Ultra-high-net-worth (UHNW) individuals and their families are increasingly moving away from simple charitable donations, where the recipient would spend the money as they see fit, and towards a much more dynamic, innovative and hands-on approach. The lines between philanthropy and business are blurring as wealthy donors seek active involvement in the management of their charitable funds, applying the same principles of control and accountability as they would for their regular investments.

Philanthropic financial vehicles are now becoming more sophisticated than the traditional charitable trust or foundation and more central to clients' wealth management and business strategies. In particular, we are seeing a trend towards impact investing, ie, investments made into a company, organisation or fund with the intention of making a positive social or environmental impact alongside a financial return.

Sustainable, high-impact philanthropy is an emerging scene in the private client space and of increasing importance to our clients at a global level. While historically we have found US clients to be more philanthropically focused than those in Europe and Asia, we are now seeing an increased emphasis on philanthropy overall. There is ample opportunity for significant global growth in philanthropy, noting that the global ultra-wealthy population (ie, those with a net worth of at least US$30 million) is expected to increase by 40% in the next five years, according to the Knight Frank 2018 Wealth Report. Furthermore, Asia's number of UHNW individuals is predicted to shoot ahead of Europe's, with China's ultra-wealthy population set to more than double during this period.

So, with this anticipated global growth in the number of UHNW individuals and families, how is philanthropy in the private client space evolving in different parts of the world? In this article we have examined the situation in a number of key regions: the Middle East, which is still in an evolutionary phase of development; Asia, which is already seeing the impact of millennials towards an impact investing approach; Europe, which is demonstrating 'hands on' investing in action; and, finally, the United States, which is at the forefront of driving innovative solutions for the next generation.

Middle East: starting on the path to sophistication in philanthropic solutions

The culture of giving is deeply ingrained in the Middle East, and Zakat ('that which purifies') is a religious obligation for those who meet a certain criteria of wealth. Based on income and the value of all of a person's possessions, it normally represents 2.5% of a Muslim's total wealth and savings over and above a specific threshold. Zakat contributions are voluntary in most countries with a Muslim majority, although there are a few countries (including Malaysia, Saudi Arabia, Libya and others) where Zakat is mandated and collected by the state.

In the light of this well-established tradition, the sums spent on philanthropy in the Middle East can be vast, and there is a strong desire to create a positive and lasting social impact. The United Arab Emirates is the leader when it comes to giving in the region, where it has been estimated that the wealthiest philanthropists donate an average US$10.2 million per person over the course of their lifetime, according to the Philanthropy Report 2015 published by Wealth-X and Arton Capital. Saudi Arabia is considered to be close behind. A recent report by the Belfer Center for Science and International Affairs showed that in 2018 there are over 40 formal foundations in the UAE, of which nearly two-thirds are linked to the government.

From our experience of dealing with clients in the Middle East, we see that the philanthropic sector is still in a nascent and evolutionary phase in this region. Our clients have a natural tendency to opt for the 'foundation' approach, modelled along the lines of well-known US private family foundations such as the Bill and Melinda Gates Foundation, or the Obama Foundation. Despite the Middle Eastern philanthropist's best intentions and preferences, however, unyielding local laws in their home jurisdiction can mean they are unable to find a suitable local structure. We are therefore seeing Middle Eastern clients looking further afield to set up an offshore foundation. Taking this approach not only offers greater flexibility but provides donors with a robust, tax neutral structure within which assets can be consolidated. At the same time, in order to maintain a local link, the offshore foundation might sit alongside a local entity that also holds shares in a holding company, and the two structures – the offshore and onshore entities – would then interact with each other.

We have seen that the objectives of philanthropy can be very broad, even for a single foundation, ranging from education to health, to arts and culture, to promoting entrepreneurship or environmental protection. We have also seen in the UAE, for example, that philanthropy for religious purposes is considered important, with philanthropists building mosques where their own domestic staff and community might attend for prayers.

Since there are large sums involved in Middle Eastern philanthropy, the donors of foundations are very keen to exercise strong influence over how funds are invested and distributed, and will also wish to ensure that any money invested is done so in a Sharia-compliant manner. There are examples of philanthropists who have started an activity, which then becomes a business, and where the profit is then reinvested, providing for further charitable ends to be met. Foundations may decide on specific priority areas, to be designated by the founder and possibly a board of directors. In terms of evolution, some market commentators have noted that philanthropists in the Gulf region have tended to operate on annual budgets, with a short-term focus, but there is now more discussion around the sector becoming more strategic and sustainable, and so in future years there could be an increase in the number of foundations with endowments and possibly multi-year funding commitments.

The fact that philanthropic organisations in the Middle East are relatively new means that there is likely to be room for greater development and sophistication in processes, and also in areas of monitoring and evaluation, where there will be more to learn regarding international best practices and procedures. We have seen from our experience with private clients that even very wealthy families who have given a lot might not always be well 'joined up' in terms of their approach.

When it comes to partnerships, most foundations in the Middle East tend to cooperate or collaborate with national governments, in view of a range of legal, financial and practical conditions, in a way that is not so commonly seen in the West. Due diligence regarding partner organisations is also taken very seriously. Keen to guard against any potential reputational risk, Gulf foundations are ambitious on the one hand and discriminating on the other, and this combination drives them in the direction of 'blue chip' companies and non-profit organisations.

Furthermore, the wider regulatory landscape, and in particular strict laws to combat terrorist financing, can place some constraints on the options available to Middle Eastern private clients, since American and European banks may be wary of accepting regional charities as their clients or processing significant sums through their accounts. This has led some foundations to set up branches or to register in foreign jurisdictions in order to facilitate international activities.

Asia: millennials driving move from charitable giving to impact investing

Personal wealth in Asia is considered to be at an all-time high, with more billionaires in the region than anywhere else in the world, and there are signs of change in the approach to philanthropy that will affect the preferences of private clients in the future. Euromoney has highlighted that with increasing wealth and a desire to create sustainable social and environmental impacts, Asia is overtaking the United States as the driver of innovation in philanthropy. A new approach is being driven by younger UHNWIs in parts of the region, who are moving away from the cheque-writing style of the past generation and towards a 'profits with purpose' form of investing, while there is potential for the growth of philanthropic support mechanisms for private clients in the region overall.

In the light of changing client demand, Singapore's largest bank, DBS, has recently boosted its socially-responsible product offerings and is now seeking to develop a pan-Asian ecosystem to help 'next gen' wealth clients to meet their new philanthropic concerns, and this trend is also being seen by other leading wealth managers. While the bank got off to a slow start with its first Women's Livelihood Bonds in 2017, the instrument has since been performing well,

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and a second tranche of the programme was launched in September 2018 in partnership with Impact Investment Exchange (IIX), targeting a total of US$100 million. The bond impacts the livelihoods of over 385,000 women in Southeast Asia through micro-loans, and further demand for impact investment products is anticipated. This trend would appear to be corroborated by a survey of Asian high-net-worth individuals, conducted by Credit Suisse and Campden Research, which revealed that 95% of them said that their main objective around philanthropy was to deliver social impact.

Despite this apparent enthusiasm for philanthropy, Asian philanthropists are capable of giving around 11 times more than they are currently, according to an index launched by the Centre for Asian Philanthropy and Society (CAPS) in January 2018. It was suggested by that organisation that if governments in Asia created the right incentives, regulations and tax policies, it would create a 'magic recipe' for philanthropy in the region to 'leap ahead' of its current status. It was highlighted that in recent years Official Development Assistance for the entire Asia continent stands at US$45.5 billion, where it could be US$500 billion, if this figure is compared with that of their philanthropic peers in the West. US$500 billion is equivalent to 2% of Asia's combined GDP, with 2% of GDP being the US giving benchmark.

The CAPS report examined 15 Asian economies' tax incentives, regulatory regimes, procurement procedures, and cultural conditions, and considered how well these economies are catalysing philanthropic giving, if at all, based on responses from social delivery organisations and sector experts, based on numerous interactions and previous work with philanthropists across the region. It was found that Japan, Singapore and Taiwan all scored higher than the Asian average, but that all economies could improve. India and China, both starting from a low base, were seen as slowly improving in the light of new laws adopted in recent years focused on international and local private social investment. The report highlighted that many economies in Asia are rethinking the policies affecting the sector including Indonesia, Cambodia, Myanmar, Thailand and Pakistan.

Furthermore, the CAPS report highlighted that there was also a 'trust deficit' impeding philanthropic giving in Asia, which could be attributed to a fluctuating regulatory environment, ambiguity around the goals of NGOs, front-page financial scandals, the inability of many organisations to be transparent and accountable, combined with a historical tendency for the best and the brightest to go to other sectors. It concluded that there is unprecedented space and opportunity for Asia to leapfrog ahead and be on a par with donors in the West but that, in order for this to happen, Asian governments need to lay the right regulatory, institutional, and even cultural and social foundations for private social investments to thrive.

Opportunities for private clients may be impacted by regulatory challenges posed to philanthropic organisations in Asia, as noted by a number of commentators. Professor Mark Sidel of the University of Wisconsin-Madison and Consultant (Asia), and International Center for Not-for-Profit Law (ICNL), has highlighted that there are increasing restrictions across the region, coupled with more wholesale state discretion over when and how legal sanctions will be used to mould and restrict the work of civil society groups, including philanthropic organisations. They include restrictions on formation and burdensome registration requirements for organisations, limitations on permissible purposes (such as broad and vague ideas of national security or political activities), restrictive membership criteria, prohibitions and even criminal sanctions on unregistered groups.

Professor Sidel notes that laws in a number of Asian countries, from China to Nepal to Vietnam, have introduced a multi-step registration process for non-profit and philanthropic organisations, with approvals required from several government actors. In addition, sub-national (provincial and state) governments exercise an increasing degree of oversight in registration and governance processes, often in restrictive ways. Furthermore, in many countries of the region, including China, India, Pakistan, Bangladesh and Hong Kong, an increasing role of security agencies in the registration process and in monitoring and enforcing rules on the non-profit community has been identified. Opportunities for philanthropy are also being skewed where tax incentives for giving are discriminatory towards government-favoured charitable organisations.

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improvement in terms of philanthropic support mechanisms in Asia that could benefit private clients, with Professor Sidel concluding that the growth of giving in Asia far outpaces the development of the support and services required to facilitate it. It is noted that in China, for example, where thousands of foundations have been formed after the introduction of a new charity law, there may not be enough lawyers to deal with increasing government requirements and pressure, and it is also seen that there is room for legal, accounting and other support services to be further developed across the region.

Europe: The growth of 'hands-on' philanthropy

Philanthropy in Europe has a rich history and takes a number of different forms, in view of different cultural practices, legal systems, tax rules, economic and political conditions, as well as varying national traditions regarding state provision, the role of the church in charity provision and volunteering, among other factors. European philanthropy stands out for the concentrated nature of its capital, which arises as a result of very large corporate foundations. German foundations account for approximately one-third of total foundation spending in Europe (with the Bosch Foundation alone estimated as holding assets worth €5 billion), while in Italy savings bank foundations, which were created in the 1990s, are estimated to hold half of all Italian philanthropic assets, representing over a fifth of the European total. The role of private philanthropy is recognised by European states, with almost universal presence of tax relief across countries, although there can be some legal and fiscal obstacles to cross-border philanthropy which remain to be addressed.

In Europe, we are actively supporting a wide range of private clients with their philanthropic activities, and we are witnessing an increasing marked focus among UHNW families and family offices who are taking a much more 'hands-on' approach than seen in the past.

To provide an example from our client base, a wealthy European entrepreneur who made money in commercial real estate deals created a family-run private equity/venture capital fund, valued at approximately US$500 million, within a charitable foundation. The fact that this is a fund that will strategically invest in companies and business opportunities, with family members providing investment advice, demonstrates a more long-term and hands-on approach to philanthropic giving.

There is also a trend in private client philanthropy in Europe that brings the personal passions and luxury assets of the philanthropist to the fore, to be shared with a wider audience. The UBS Billionaires Insights 2017 report highlights the rising interest in art collecting and establishing private museums for the public to enjoy. It also notes that public museums are receiving more funding than ever before. It has similarly been predicted by Fine Art Wealth Management that art will play an important role in philanthropic gifting strategies led by UHNWIs. Family art foundations and private museums opened by wealthy individuals will increase in both size and number globally.

If we look at the financial products available to private client philanthropists, Europe has led the way with the creation of social impact bonds. The first social impact bond was launched in Peterborough, England, in 2010 after Social Finance raised £5 million from trusts and foundations. It funded the One Service, an umbrella organisation designed to respond to the complex needs of offenders to help them break the cycle of reoffending. The programme reduced reoffending by 9% overall, compared to a national control group, exceeding the target of 7.5% set by the Ministry of Justice. The 17 investors in the scheme were therefore entitled to receive a single payment representing their initial capital plus an amount representing a return of just over 3% per annum for the period of investment.

Social impact bonds (SIBs) are now playing an important role on the philanthropic landscape in the UK and beyond, with the UK Government announcing in September 2018 almost £200 million of funding for 22 programmes backed by SIBs via the Life Chances Fund. This concept has now taken hold in a number of countries, with well over 100 SIBs commissioned with a range of purposes, from helping migrants find work in Belgium, to supporting micro-enterprises in Kenya, to improving education for girls in India and preventing diabetes in Israel. While there are different models used in different countries, they are all based around an outcomes contract – whereby a social enterprise or non-profit organisation agrees to deliver on a 'pay for success' basis and so the funder (often the government) only pays if some pre-specified outcomes are achieved by the service – and the necessary working capital and management support are provided by an impact investor.

Another variant on government-supported philanthropy can be seen in Ireland, where the government created the Social Innovation Fund Ireland (SIFI) in 2013. The SIFI is the venture capital fund of the social innovation sector, and its purpose is to find and back innovative solutions that address critical social issues in Ireland. Every euro that is donated in private philanthropy is matched by a euro from the Department of Rural Affairs and Community Development from the Dormant Accounts Funds. This is therefore a good example of both the state and the non-profit sector working together to create an enabling environment for social innovation, and one which is likely to encourage private clients to pursue philanthropy in the country.

United States: champion of strategic, outcome-driven philanthropy

If we turn to the United States, seen by many as the natural home of philanthropy, how is philanthropy evolving to meet client demand?

The Epic Foundation, a global non-profit start-up headquartered in New York, offers an approach that is likely to hold increasing appeal with private clients. Epic has noted that philanthropy is evolving because society is evolving, particularly in terms of the profound influence of the millennial generation. It observes that today's 18–35-year-olds have a value-based set of expectations and are looking for purpose and social impact.

Epic has identified the main reasons why people do not give and why they do not give more: a lack of trust in social organisations, a lack of understanding of their impact and a lack of time to find out more. To address these issues, Epic came up with a strict selection and monitoring process to build a portfolio of high-impact social organisations around the world. It also provides donors with the opportunity to experience their philanthropy through a web app, so they can stay connected and engaged with the social organisations they support. Donors can also view a collection of VR films on every portfolio organisation, transporting them 'to the field' in an instant.

In addition, Epic offers a range of giving solutions to individuals and corporations so that they can donate more by leveraging innovative and efficient systems such as payroll giving for employers and employees, transactional giving for businesses and Sharing Pledges for investors, entrepreneurs and corporate leaders. Notably, here at SGG we have already started working closely with Epic to deliver our new employee fundraising programme, under which all donations made by our employees to selected charities will be matched by the Group.

The approach of the Epic Foundation is very much in line with that identified by the Johnson Center at Grand Valley State University, Michigan, in its report on "11 Trends for Philanthropy in 2018". It has highlighted that the current wave of 'next gen' donors will have unprecedented financial resources to give, both from the new fast fortunes being created by young techies, hedge funders, and others, and from the extraordinary transfer of wealth underway within some of the United States' wealthiest families. The Johnson Center anticipates that these donors will also be historically significant because of their zeal for revolutionising philanthropy through new strategies and innovations that are already starting to shake up the field. Furthermore, 'next gen' donors will want to transform giving in ways that they hope will finally 'move the needle' on long-standing social challenges. It is noted that these donors want to be more focused, more metric-driven and more experimental – all in the hope of expanding the impact of big giving. It is underlined that these donors wish to 'do good' through impact investing and other new tools, not just through traditional grant-making.

One example highlighted by the Johnson Center, which might provide a model for private clients in the future in the United States and beyond, is that of the famous 'next gen' donors Mark Zuckerberg and Priscilla Chan. Rather than setting up a traditional foundation, they decided to establish a 'charitable LLC' – known as the Chan Zuckerberg Initiative – as

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the primary vehicle for their giving and investments for social good. This allows them to make philanthropic gifts as well as to invest in socially responsible businesses, political initiatives and other ventures. Such donors will seek to engage in a much more 'hands-on' way with the organisations they support, bringing their time and talent to projects, to develop real relationships with their partners.

In terms of wider trends, from our own base of US private clients, we are also continuing to see philanthropy in the form of more traditional giving, driven by the individual's passions and personal beliefs. For example, one trust has been settled by a US citizen living in Europe, which has real estate and quoted portfolios earmarked for charitable giving to animal species preservation, with around US$10 million allocated for this purpose.

When it comes to innovative philanthropic financial products, the United States has pioneered the development of donor-advised funds (DAFs), which have been reshaping the landscape of US philanthropy. DAFs are accounts set up within a charitable organisation, such as a community foundation. Some DAFs can be set up as charitable gift trusts and are managed by financial institutions. With a DAF, the donor contributes personal assets to an account, where the contribution can be invested, and it then grows tax-free until a grant is made to a qualified charity.

While DAFs are not new, the National Philanthropic Trust has identified that they are the fastest-growing vehicle in philanthropy, with assets in DAFs nearly doubling between 2012 and 2016, growing from just under US$45 billion to more than US$85 billion in five years. According to a 2017 Foundation Source survey, the average family foundation manages US$5 million in assets, while the average DAF account size is US$292,000, making DAFs accessible to a larger donor base. Any asset that can be accepted by the managing charity may be accepted by the DAF, which helps donors receive the best possible income tax deduction opportunities. The one downside of DAFs, however, relates to a lack of control. While a donor may indicate an investment objective or strategy or recommend charities to receive grants, the donor does not reserve the right to direct distributions, and the managing charity has the authority to approve or deny any donor recommendations.

The social impact bond, pioneered in Europe, has also become very popular in the United States, and will continue to play a role in private client philanthropic strategies. It was noted in the *New York Times* in March 2018 that the United States already had 20 social impact bonds in place, leveraging US$211 million in investment capital, and that at least 50 more were on the way. These bonds were already funding programmes to reduce Oklahoma's population of women in prison, to help low-income mothers have healthy pregnancies in South Carolina, teach refugees and immigrants English and job skills in Boston, house the homeless in Denver, and reduce storm water runoff in the District of Columbia, while a Forest Resilience Bond was underway that would seek to finance wildfire prevention.

The trend towards impact investing and socially responsible investment (SRI) shows no sign of abating, with the Global Impact Investing Network (GIIN), based in New York, estimating that there was US$228 billion invested in impact, as at June 2018, which was double the prior year estimate. Some commentators have also highlighted that in the past investors did not mind sacrificing some return to invest in socially responsible investments but that this is shifting to the expectation that SRI should keep up with, or even outperform, the broader market. In the future, therefore, private client philanthropists may look to achieve the optimal balance along the spectrum of traditional giving and impact investing, with an increasing array of options available, with varying levels of control.

Conclusion

Our own experience with our private clients across the globe is very much reflected in the Wealth-X report from earlier this year, which revealed philanthropy as the top interest (36.3%) pursued by ultra-wealthy individuals across the globe in 2017. The report attributes this trend to a "growing sense of social engagement and motivation for personal fulfilment"; likely driven by the more socially and environmentally minded younger generation, recent high-profile charitable endeavours (such as the Giving Pledge initiated by Bill and Melinda Gates and Warren Buffett), and the strong growth of first-generation wealth in emerging economies where religious beliefs and family/social ties instil a desire to give back.

Overall, we can anticipate a much more innovative and business-like approach to philanthropy at a global level than seen in the past, with the Wealth-X research further observing that "there will be a rising demand to cater for the increasingly sophisticated channels of philanthropic engagement". It is also interesting to note from the Third Annual Philanthropy Index Report by BNP Paribas Wealth Management and Forbes Insights that more than two-thirds of the 400 surveyed individuals worldwide, with at least US$5 million in investable assets, believe advisers are necessary to effectively navigate the giving sector. At SGG Group, we are well aware that with this evolution comes a greater need for private client practitioners to demonstrate expertise in philanthropic solutions as well as good governance procedures. What I can say for sure is that, as trustees, we must keep adding value for our clients, and a deep understanding of philanthropy in its evolving forms is becoming an increasingly important aspect of the trustee's role.

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