Discussion Memorandum from the Vestry of The Church of the Holy Faith regarding the Endowed Reserve Fund

We, the members of The Church of the Holy Faith, are truly blessed with this most wonderful parish family. The Vestry is extremely grateful for everyone's contributions of their time, talents and treasures to the work of our Church. The parish family, all of us, are the body of The Church of the Holy Faith and the Body of Christ. We all want what is best for the continuance and growth of our ministries in the City of Santa Fe and in the world around us.

Your Vestry is concerned that all parishioners have the same complete and accurate information regarding its decision to establish the Endowed Reserve Fund, taken in September 2018. It is important to note that income from the fund will not be available for consideration by future vestries until January 2021, which means that no elected member currently serving will participate in any potential distribution decisions. The rationale for the fund is set out below: -

Donor Direction/Donor Intent There were *requests from parishioners* who wanted to make current gifts to an endowed fund and from *founding members* of the Legacy Society expressing the desire that the endowed income from their gifts and legacies be available to support operating expenses of the church - such as the music program - if the need were to arise in the future. The Vestry wanted to be able to accommodate and honor that legitimate donor intent. The establishment of the fund was driven by the gift instrument executed by the founding donor who directed that the funds be permanently endowed and that the income from those funds be available to future vestries to support capital expenditures, mission & outreach and operating expenses. By establishing the new Endowed Reserve Fund to accommodate that donor direction, the Vestry did *nothing* to close the Endowment Fund to future donations which is, and which will remain open to future gifts, honoring donor intent.

Good Stewardship Holy Faith has enjoyed a balanced budget every year since 2011, thanks to the faithful support of parishioners and the financial discipline of the Vestry and our former and current Rector(s). As a result, we built a cash balance of more than $525,000, roughly five months' worth of operating expenses, as of the end of December 2018. This is the *highest cash balance Holy Faith has had in at least the last twelve years and possibly ever.* Cash on hand as of the end of the first quarter 2019 remained strong at $490,000. Pledged income has increased every year for the last four years. We are so incredibly blessed that current operating income is sufficient to cover current operating expenses and *robust stewardship campaigns will continue*. It is both a canonical obligation for the Parish and more importantly *a spiritual obligation* - we would choose the word "honor" - that we all have in order to be in right relationship with each other and with God. We give *not* because Holy Faith needs money. We give because we are *called* to tithe.

As a Vestry, we also recognize that our economy experiences times of growth and times of contraction. A painful lesson learned during the Great Recession, which was compounded by the misconduct of the Rector before Canon Semon was called to be Rector in 2008, and the resignation of Bishop Steenson in 2007, was that we as a Parish are not immune to external

economic forces. During the years 2008 – 2010, Holy Faith ran deficit budgets rather than cut paid staff positions or pare back on programming sufficiently to balance the budget. During that time, the Vestry, in August 2009, passed a Corporate Resolution authorizing the then Rector, Fr Semon, to borrow on behalf of the Parish up to $100,000 for up to 90 days. By prudent planning and the proper exercise of fiduciary responsibility, it is hoped that such a drastic step can be avoided in the future.

Likewise, we understand that the increase in our pledged income of the last four years is partly due to the growth in our economy. Understanding the vagaries of the business cycle, and knowing that we may need to call upon reserves during the next economic downturn, we are squirreling away surplus today, should we need to call upon it tomorrow.

The question is how best to hold those reserves. *Cash pays virtually no return in today's market.* During the past 10 years, cash has only once been the top performing asset class. On the contrary, it was the worst performing asset class for four of those years, and has returned a Compound Annual Growth Rate of 0.3%, vs an average inflation rate of 1.75% per year. Continuing to add to adequate cash reserves would be akin to burying the talent in the ground, as we read in the *Parable of the Talents* in Matthew's Gospel. By investing cash reserves in excess of current and expected needs in the Endowed Reserve Fund, we are planning for the future of The Church of the Holy Faith. The creation of a *separate fund* assures donors that their intent has been honored and avoids potential legal complications in the future. Your Vestry takes very seriously their responsibility to be good stewards, both for The Church of the Holy Faith and for God as well.

Parish Demographics Based on our Parish's demographics, an unexpected loss of significant pledging unit(s) would have the potential to require an immediate reduction in expenses in payroll or program offerings of our Church. Accordingly, the Vestry desired to be proactive in establishing a fund from which income could be used for operations *on an interim basis* if the need were to arise in the future. It would be incumbent on the Parish to overcome such a drop in pledged income in ensuing years and/or upon a future vestry to reduce operating expenses in line with that income. Holy Faith's Endowment Fund has grown to a level from gifts from many loving parishioners and former parishioners that should allow it to provide adequately for capital expenditures and missions & outreach going forward. Should that not be the case, restrictions on the use of income from the Endowed Reserve Fund would permit use for capital expenditures and missions & outreach, as deemed appropriate by future vestries.

Both the 2017 and the 2018 Vestry voted *unanimously* to approve an endowed reserve fund (and both with the *unanimous consent* of the 2017 and 2018 Finance Committee members). This was a decision not taken lightly, but with much prayerful consideration. It was taken because the Vestry and the Finance Committee deemed it to be in the best interests of Holy Faith for today, tomorrow and the future.

We all are The Church of the Holy Faith. We, as your Vestry, feel that we share the same goals for our beloved church. We all want The Church of the Holy Faith to be alive and vibrant in our

community, doing God's work as long as God would have us to do it. Let us work together, prayerfully, to do our part in helping The Church of the Holy Faith to continue in its current ministries and be open to the Spirit in leading us to develop other ministries that meet the needs of our parish family and our wonderful city of Santa Fe.

Subsequent to the Vestry presentation in January, some members of your Vestry received questions regarding the Endowed Reserve Fund. We would like to address those written concerns directly in an effort to be transparent and give all of our parish family the same complete and accurate information regarding the Endowed Reserve Fund.

Concern 1: "Trust is an important factor in the relationship among the Rector, Vestry, and Parish. The very tenets of our faith tell us to be trustworthy. The trust we have as parishioners has been damaged by the Rector and Vestry taking action specifically not approved by the Parish. The proposal in January 2018 was for a by-law change that required 2/3 of the Parish to approve it. It was tabled by a vote of approximately 86-18."

Response 1: Trust is indeed a paramount factor in our parish family, just as it is in any family. At the 2018 Annual Meeting, the Vestry was asking for a bylaw amendment to Article VI to subject the proposed endowed fund to the same controls and standards that were in place for the Endowment Fund. *The Vestry did not need an amendment to the bylaws to open such a fund*, as is made clear in the *Constitution and Canons for the governance of the Protestant Episcopal Church in the United States of America* in Canon I.14.2: "Except as provided by the law of the State or of the Diocese, the Vestry shall be agents and legal representatives of the Parish *in all matters concerning its corporate property* and the relations of the Parish to its Clergy."

Individuals who supported the concept of a second endowed fund, but who were concerned that the requisite two-thirds majority to amend Article VI might not be achieved, or those who were concerned that the proposed amendment might have been construed to have closed the Endowment Fund to new donations, voted with those opposed to the concept to table the discussion of <u>that amendment only</u> *in order that the legitimate concerns raised about the proposed amendment could be addressed*. The Vestry felt it understood and had addressed the concerns that had been raised at the Annual Meeting and accordingly exercised its authority to open the Endowed Reserve Fund to accommodate donor intent from the founding donor.

Concern 2: "The Vestry's establishment of this "Endowed Reserve Fund" allows for far fewer financial controls of this fund's usage. The "Endowed Reserve Fund" has been established by a simple vote of the vestry, and it can be changed the same way. The current or a future Vestry can change the amount that goes to operating expenses and any other criteria for spending with a simple vote."

Response 2: Subject to honoring donor intent, this is correct and exactly the reason the Vestry was requesting a bylaw change in January 2018 to subject a new endowed fund to

the same controls placed by the bylaws on the Endowment Fund. This Vestry has pledged to operate the Endowed Reserve Fund in the same manner as the Endowment Fund with the same protection of capital as is prescribed in Article VI, and the Investment Advisory Committee (IAC) has directed the fund managers to follow the same asset allocation and risk management guidelines as set out in the Investment Policy Statement (IPS) as described in Article VI. (The Diocesan Investment Board plays no role, nor does it have any oversight of the endowed assets of The Church of the Holy Faith.) The Vestry hopes to come to the Parish to request a new bylaw, *not an amendment to Article VI*, that will *provide in the bylaws* the same protections to the Endowed Reserve Fund that the Endowment Fund has in place. Should the Parish adopt that additional bylaw, it would be filed, as required by Canon, at Diocesan House.

Concern 3: "The purpose served by this "Endowed Reserve Fund" is not clear. Current operating revenues are sufficient to cover current operating expenses."

Response 3: It is true that current operating revenues are sufficient to cover our current operating expenses and we are truly blessed to be in this position. We have also been blessed to have been able to build a substantial cash reserve, and *we are in compliance with the recommendation of The Episcopal Church* that a parish have between 3 – 5 months of operating expenses in a cash reserve before establishing any endowment fund. It is our fiduciary responsibility and obligation not only to live within our means today, but to plan for the future of our Parish. That future is best provided for by endowing funds in the Endowed Reserve Fund (subject to the controls that we are all in favor of), rather than by building further cash reserves.

Concern 4: "The Richdale Bequest of $109,013.82 was deposited into the "Endowed Reserve Fund" when established. Did the donor specifically request these funds to be used for operating expenses?"

Response 4: The Richdale bequest that was given to Holy Faith was to be used as the Vestry saw fit. The bequest was *not* to the Endowment Fund of the Church of the Holy Faith, nor did it stipulate that the money had to be endowed. The funds, under the terms of the will, could have been deposited into the operating account. Because our Parish did not need those funds for current operations, we were not in a position of needing to build additional cash reserves and the corpus of the Endowment Fund as of the end of July already exceeded $7.25 million, the Vestry "saw fit" to endow the bequest in the Endowed Reserve Fund.

Concern 5: "If there is a sudden loss of operating funds or another emergency, the appropriate financial strategy is to establish an operating reserve. Such a reserve is funded out of operating funds, used according to pre-established criteria, and replenished the next year with operating funds."

Response 5: The Church of the Holy Faith does have an operating reserve, by the grace of God and our parish family. The Vestry and the Finance Committee feel that there is a sufficient reserve on hand, nearly five months of operating expenses, to handle a short-term set back. If we were to wait until there is a "sudden loss of operating funds or other emergency" to set up

a reserve fund, endowed or otherwise, we would be reacting to a crisis. In addition, there is *no guarantee that any operating reserve could be replenished in the next operating year*, particularly if the establishment of the fund had been prompted by the "sudden loss of funds or other emergency."

The Vestry, as well as the prior two vestries, is attempting to be proactive so that if confronted with a sudden cash flow need, the Church will be in a position to handle that need *on an interim basis*. The Vestry feels that *it would not be good stewardship on our part to wait until there is a need to plan for that need*. Would those who have expressed a concern about the establishment of the Endowed Reserve Fund find it preferable that a future Vestry be in the position that the Vestry in August 2009 found itself in, facing a cashflow crisis, when Fr Semon was authorized to borrow a short-term loan of up to $100,000?

Concern 6: "The use of endowed funds for operating expenses is not a sound financial practice. It often leads to spending more than the annual revenues each year. Endowed funds are most often given with the understanding that they will be used for capital and other non-operating expenses. The use of endowed funds for operating expense can violate the donors' intent."

Response 6: The assertion that churches or other non-profits do not rely on endowed income to meet operating expenses is simply not true. It is permitted under both civil and canon law. The Episcopal Church for the 2019-2021 triennium is budgeting a 5% draw (1% more than Holy Faith's permitted draw from the Endowment Fund), which represents 23% of the wider church's income. The Diocese of the Rio Grande will fund approximately 18% of its operating budget from investment income in this fiscal year.

According to the National Association of Nonprofits, "Creating an endowment may be an important strategy to set aside funds for the future, and can be a hallmark of *financial sustainability*. Most endowments are designed to keep the principal corpus intact so it can grow over time, but allow the nonprofit to use the annual investment income for *programs, or operations, or purposes specified by the donor(s) to the endowment."* In the case of the Endowment Fund, that income, subject to limitations, can be used to finance capital expenditures and mission & outreach. In the case of the Endowed Reserve Fund, that income, subject to limitations, can be used to finance capital expenditures, mission & outreach and operating expenses. The establishment of the Endowed Reserve Fund has <u>nothing</u> to do with violating donor intent. It has <u>everything to do with honoring donor intent</u>, to honor the requests from current donors and declarations of intent to provide for such a fund. Establishment of the Endowed Reserve Fund was propelled by a pledge, subsequently expressed in a gift instrument, directing that the gift be permanently endowed with the income available to support capital expenditures, mission & outreach and operating expenses.

Concern 7: "The use of endowed funds for operating expenses is also an unsound spiritual practice. Raising the money needed for the church and its activities is the essence of stewardship. Living within our means holds the Parish accountable for both the financial and spiritual health of the church."

Response 7: According to The Episcopal Church "Stewardship is about being grateful, *responsible* stewards of the gifts we receive from God." The Vestry is committed to meeting its obligation both to preach and practice good stewardship in the fullest sense of that word. Good stewardship is necessary for us all to be in right relationship with each other and in right relationship with God. While we recognize God's bounty to us in our current situation, we are working to ensure that we will be able both to continue and to grow the ministries of The Church of the Holy Faith – not just support the bricks and mortar, when and if something happens to current giving levels.

Concern 8: "This church has a recent history of Rector Dale Coleman's misusing church finances and the Vestry failing to exercise sufficient financial oversight. Because the whole Vestry felt they did not live up to their fiduciary responsibility, they resigned. Among the many things the next Rector, Kenneth Semon, did to correct the financial abuses was to support the by-law change that established the Endowment Fund. Because of this history, the Parish is very sensitive to changes in financial strategies and lack of involvement in those changes."

Response 8: There has been financial mismanagement in the past within The Church of the Holy Faith. This is a sad truth and the Vestry realizes that there are still those parishioners who have raw memories of that, but it has now been more than 12 years since Dale Coleman served as Rector. While it is true that the then serving Vestry resigned for failing to meet their fiduciary responsibilities, as the outgoing Senior Warden said in his letter to the Parish "we were deceived and lied to [by the former Rector]." Every Vestry and every Finance Committee since then has worked hard to exercise financial oversight, diligently to implement controls and act at all times as good stewards. Both Canon Semon and Canon Dodge have strongly supported that mission. Third party CPA audits have been conducted for every year since 2007, all of which have been unqualified by the auditors. Any attempt to tar those post-Coleman vestries with that brush is to denigrate the hard work of those intervening vestries.

It is not true that the bylaw establishing the Endowment Fund was brought into force when Canon Semon was Rector. An examination of the 2001 bylaws makes clear that the Endowment Fund was already in existance. The first bylaw amendment to Article VI that was adopted by the Parish in January 2009 changed the definition of income from being "5% of the market value of the unrestricted investments at the end of the calendar year" to "equal to, or less than the three-year rolling average of 5%." Ironically, because the S&P 500 lost 38.49% in 2008, although the Endowment Fund lost only ca. 28%, this bylaw change *increased the amount of money that could be drawn in 2009 which would have invaded the principal under the previous definition.* While the use of income was restricted to outreach and non-operating expenses, the Vestry was given permission *to borrow* from the Endowment Fund up to the amount of the defined income, provided the money was repaid within the fiscal year. It would appear, therefore, that *up to 10% could have been withdrawn* within the course of any calendar year, since the amendment did not appear to preclude an income draw in the event of a loan.

Subsequent vestries, however, did recommend and the Parish did adopt various amendments to the bylaws that strengthened the protection of the principal, such as the controls implemented on the Endowment Fund in 2012, reducing the permitted draw to 4% of the rolling three-year year end average at which time the ability to borrow up to 5% of the three-year rolling average was removed. We do not have a situation of financial mismanagement today and we are working hard to ensure that we have controls in place to prevent financial mismanagement in the future.

Concern 9: "When there are two endowment funds, it is not clear how future bequests will be categorized. The temptation would be to put any money in the endowment with the most flexibility, unless specifically prohibited by the donor. This places an undue burden on the donor to establish guidelines for the placement and use of the gift and means that the Endowment Fund would not receive as much money as it would otherwise."

Response 9: Rather than an "undue burden" being placed on the giver of funds, the creation of the Endowed Reserve Fund allows donors to express more fully their intent to, for example, have the income from their endowed funds go to support the music program. (There is currently *no mechanism* for such a bequest to be accepted, because other than the purchase of sheet music or the replacement or major rebuild of the organ, *all expenses incurred by the music program are considered operating expenses*.) We have parishioners who have expressed a strong interest in *both* of these funds for continuing the work and ministry of The Church of the Holy Faith and parishioners will be able to give to one fund or the other or have the opportunity to split their gifts in any percentage they choose between the two funds by means of a simple form of declaration currently being drafted by the Legacy Society. This does not create an "undue burden" on any giver, and it increases, rather than decreases, the likelihood that legacies will be left, precisely because donor intent can be honored. By honoring that donor intent to include operating expenses, Holy Faith will be better placed to adapt to difficult situations we cannot anticipate right now or possibly consider whole new opportunities – the endowment of a youth minister position, perhaps?

Legacies to the Holy Faith Endowment derived from wills executed before the announcement of the Endowed Reserve Fund (January 20, 2019) will, in the absence of a donor declaration of intent to the contrary, be placed in the Endowment Fund, which, to reiterate, *will remain open to new contributions*.

Concern 10: "There has been some discussion of establishing the "Endowed Reserve Fund" to avoid having to send a portion of the money to the Diocese for the Parish's fair share contribution. Financial strategies to avoid paying our fair share are inconsistent with our spiritual responsibility for outreach and support."

Response 10: The Church of the Holy Faith is the largest Fair Share payer in the Diocese. We do not shrug any responsibility in paying our Fair Share apportionment. It makes no sense to pay Fair Share on endowment contributions received, however, until we know how the proceeds will be used. If the proceeds are to be used for operations, we will

gratefully pay Fair Share on them at the time income is received into the operating budget from the Endowed Reserve Fund. Paying Fair Share up front, on funds the income from which may ultimately be used for capital improvements or missions and outreach, would be *a breach of the Vestry's fiduciary responsibility to parishioners and donors*. It would diminish the amount of reserves available in the future which would ultimately be a disservice to the Diocese if it were to impair Holy Faith's mission and ministry thereby undermining its ability to pay Fair Share in the years to come.

On this topic it should be noted that the Vestry in March 2008 voted to suspend Fair Share payments to the Diocese during its dispute with the Diocese over the Coleman settlement. Although some interim payments were made, the arrears in Fair Share appear to have been caught up finally and fully only in late 2009 following the sale of the St. Simeon property to the City, at which time the outstanding $56,000 balance on the loan from the Endowment Fund was also repaid.

Concern 11: "Lack of trust has resulted in a quiet withdrawal of pledge contributions, consideration of bequests and participation in our ministries."

Response 11: People must give according to their conscience; it is strictly between each individual and God. As it says in Malachi 3:10 "Bring the full tithes to the storehouse, that there may be food in my house; and thereby put me to the test, says the Lord of hosts, see if I will not open the windows of heaven for you and pour down for you an overflowing blessing". The Church of the Holy Faith is blessed by many generous givers, resulting in record amounts pledged for the last four years. The Vestry has acted in good faith and with much thought, prayer, deliberation and debate. We hope that this will be understood and appreciated by the Parish, but we also hope that where trust has been lost it can be rebuilt for the health of our parish family.

Concern 12: "The Vestry would be well served to improve transparency and accountability."

Response 12: The Vestry agrees that it should be transparent and accountable in all of our work except where matters of individual donor privacy or personnel matters dictate otherwise. It is in the interest of transparency that these concerns have been taken seriously and addressed here in this document. We are working to improve transparency by publishing the Vestry minutes in a timely fashion each month. We are open to discussing any ideas that any member of our parish family has on ways we can improve our service to The Church of the Holy Faith.

Concern 13: "The reason we have chosen to speak to the Rector and Vestry in this manner is based on our experience of raising questions in the past. We have been ignored, patronized, and criticized. We trust that we can mutually create an atmosphere in our church that is more conducive to a loving exchange of ideas and resolving of conflict."

Response 13: Where hurt has unintentionally been given, the Vestry offers an unreserved apology. The Vestry welcomes discussion with all members of our parish family and

offered to have this discussion many times and in many ways throughout 2018. That offer was renewed most recently on January 20, 2019 when the Senior Warden invited anyone in the Parish with questions about the new Endowed Reserve Fund - *or any other topic* - to speak directly to the Rector, to him or to any member of the Vestry.