



Global Investment Office | July 24, 2025

Fiduciaries in Focus

Endowments and Foundations After the OBBBA

Fiduciaries in Focus is a quarterly report that provides guidance on fiduciary-related and retirement-specific regulations. In this report, we discuss the impact of the One Big Beautiful Bill Act (OBBBA) on endowments and foundations.

The OBBBA extends the existing individual and business tax cuts from the Tax Cuts and Jobs Act (TCJA), while adding new tax cuts and tax revenue raisers. These include increases to the excise tax on investment income for endowments, which could have impacts on investment decisions and fundraising strategies.

The legislation underwent notable changes since its initial stages. The proposed excise tax on investment income of foundations of up to 10% was removed in favor of the current 1.39% rate. Under the new law, a progressive tax structure would be applied only to endowments. The largest private university endowments may be subject to excise taxes as high as 8% for endowment assets per student above \$2 million—up from 1.4% before the OBBBA but below the initially proposed 21% from the version from the House of Representatives. The tax on endowments increases as the asset size per enrolled student grows (see Exhibit 1).

Furthermore, the tax on private college and university endowments applies only to institutions that have endowments with at least \$500,000 per student, have at least 3,000 students enrolled and have student bodies with at least 50% located in the US. The calculation of an institution's student-adjusted endowment excludes international and undocumented students. State colleges and universities are exempt from the excise tax structure, but unlike previous versions of the OBBBA, religious institutions and certain operating foundations are not exempt from the tax.

Monica Guerra

Investment Strategist
Monica.Guerra@morganstanley.com

Suzanne Lindquist

Senior Investment Strategist

Daniel Kohen

Associate
Daniel.Kohen@morganstanley.com

Cate Glackin

Associate

Exhibit 1: Progressive Structure of the Private University Endowments Excise Tax

Endowment Assets Per Student	TCJA NII Excise Tax Rate (Prior)	OBBBA NII Excise Tax Rate
Below \$500,000 or Student Exemption*	Exempt	Exempt
\$500,000 to \$750,000	1.4%	1.4%
\$750,000 to \$2,000,000	1.4%	4%
Over \$2,000,000	1.4%	8%

Note: NII refers to net investment income. *2017 student exemption was less than 500 full-time students. OBBBA exemption has been raised to 3,000 full-time students.

Source: US Congress, Joint Committee on Taxation, Morgan Stanley Wealth Management Global Investment Office as of July 22, 2025

Implications of OBBBA on Charitable Giving Incentives

The OBBBA includes provisions that alter the incentive structure for charitable contributions from its predecessor, the TCJA. The Tax Policy Center notes that as a result of the TCJA, the number of filers claiming itemized deductions fell from 31% in 2017 to 9% in 2020. The decrease has likely resulted from taxpayers favoring the use of the larger standard deduction allowance included in the TCJA. To

address some of the negative effects of the TCJA's changes on charitable giving, the OBBBA's provisions have implications for both individual and corporate charitable giving incentives. For example, a new deduction in the bill allows for a \$1,000 charitable gift deduction for nonitemized individuals, potentially increasing participation and driving smaller donors to give more (see Exhibit 2). It is estimated that this provision will cost more than \$70 billion over 10 years. The law introduces a floor of 0.5% of adjusted gross income (AGI) for individual itemizers, so individuals can now deduct charitable giving above 0.5% of AGI, which could also disincentivize giving below this floor. It also caps the tax benefits for charitable deductions for taxpayers in the 37% bracket at 35%, from 37% previously. Together, these two provisions could raise almost \$310 billion over 10 years. While this could reduce the incentive for gift-giving from high-capacity donors after 2025, it could also accelerate gift-giving in 2025 ahead of this provision taking effect in 2026.

Similarly, corporations will only be permitted to deduct charitable contributions that exceed 1% of taxable income. We encourage key stakeholders in the nonprofit space to consider how these tax changes could impact their donor base and potentially shift fundraising tactics to account for these new rules.

Exhibit 2: Impacts of OBBBA on Charitable Giving

Charitable Giving Changes	Current	OBBBA Language	Giving Impact	Giving Impact (\$)	10-Year Deficit Impact
Individual Nonitemized Deduction Increase	No deduction if a taxpayer does not itemize	Deduction for nonitemizers. Cap of \$1,000 (\$2,000 for joint returns)	Smaller donors incentivized to give more	Slightly positive	(\$73.5 billion)
Limitation on Tax Benefit of Itemized Deduction	No floor	Creates a 0.5% AGI floor for itemizers	Disincentivizes giving below 0.5% floor	Slightly negative	\$63.1 billion
	Value is 37%, the marginal tax rate avoided by giving	For taxpayers in the 37% bracket, caps the value of charitable deduction at 35%	Reduces incentive for major gifts from high-capacity donors in the long term, but incentivize pull-forward in 2025	\$4.1b to \$6.1b per year	\$255.5 billion
Corporate Itemized Deduction Floor	Corporations can deduct donations up to 10% of taxable income, no floor	1% taxable income floor	Disincentivizes smaller corporate donations	\$4.2b to \$4.8b per year	\$16.6 billion

Source: US Congress, Joint Committee on Taxation, Morgan Stanley Wealth Management Global Investment Office as of July 22, 2025

Implications of OBBBA on Portfolio Positioning

No two institutions respond in exactly the same way to policy changes, and internal institutional decision-making involves numerous stakeholders. However, there are still some leading considerations that could drive an institution's response to the expansion of the graduated endowment excise tax on net investment income. With the changes to tax thresholds and rates, institutions face new trade-offs between maintaining or growing the corpus and sustaining near-term financial commitments. Tax-mitigation strategies will vary depending on the institution's size, flexibility and liquidity needs.

The impact of changes to net investment income taxation compounds over time, reducing the effective return on portfolio assets and pressuring operating budgets. If long-term replacement funding is not feasible, institutions may revisit spending and payout policies—potentially drawing more from unrestricted funds and/or decreasing student aid or grant programs. Colleges near the asset threshold may also consider growing their student body to lower the endowment-per-student ratio and avoid falling within the taxable range. Additionally, another strategy may be to adjust spending policies to better align with after-tax return expectations. Institutions will need to gain a thorough understanding of their donor base and how their giving may be impacted. Liquidity management becomes increasingly important in this environment of notable tax policy change.

From a portfolio construction perspective, greater focus will be placed on liquidity management and portfolio flexibility to incorporate tax-efficient strategies (see Exhibits 3 and 4). Tax-mitigation techniques could include rebalancing portfolios toward more tax-efficient structures or products, such as tax alpha index strategies or private investments with deferred gains. Some institutions may consider selling low-cost-basis positions to realize gains within the portfolio prior to the proposed tax changes. Institutions may also consider repositioning a portion of their portfolio away from illiquid investments and toward more-liquid investments, while moving away from high-income-generating assets to minimize realized income. Given the increase in taxes, endowments may need to reconsider the use of certain asset classes, which may impact expected returns.

Exhibit 3: Portfolio Managers May Consider Growth-Oriented Assets

Asset Class	Liquidity	Tax Efficiency	Investment Considerations
Public Equities	High	Low	Tax-management strategies improve tax efficiency while maintaining market exposure.
Buyout Funds	Low to Moderate	High	Tax efficiency remains a question, and liquidity management concerns point to the appeal of co-investments and secondary strategies to take advantage within this sector. These typically return capital faster.
Venture Capital	Low	High	Deferred return improves tax efficiency; however, portfolio liquidity and flexibility must be considered.
Hedge Funds	Moderate	Low	Less attractive at the margin because of lower tax efficiency and liquidity limitations.

Source: Morgan Stanley Wealth Management Global Investment Office as of July 22, 2025

Exhibit 4: Tax Efficiency and Liquidity Are Considerations When Diversifying Assets

Asset Class	Liquidity	Tax Efficiency	Investment Considerations
Private Credit	Low	High	Increases portfolio flexibility, improves liquidity versus private equity and may offer better tax efficiency than traditional, high-yielding fixed income.
Traditional Fixed Income	High	Moderate	Tax-advantaged strategies and tax-managed products may improve tax efficiency while maintaining market exposure.
Hedge Funds	Moderate	Low	Less attractive at the margin because of lower tax efficiency and liquidity limitations.
Real Estate	Low	Moderate	Improves tax efficiency through pass-through and return-of-capital structures, to lower the tax base.
High Yield Bonds	High	Low to Moderate	Lower tax efficiency due to high income but significant liquidity and portfolio flexibility, thus must be sized appropriately.

Source: Morgan Stanley Wealth Management Global Investment Office as of July 22, 2025

The final 2025 budget reconciliation bill includes provisions that increase the excise tax on investment income for endowments to a maximum of 8%. Based on the new law, we emphasize the importance of asset allocation, liquidity management and product selection to improve after-tax investment performance and provide ample capital to meet spending requirements.

Disclosure Section

Risk Considerations

Equity securities may fluctuate in response to news on companies, industries, market conditions and general economic environment.

Bonds are subject to interest rate risk. When interest rates rise, bond prices fall; generally the longer a bond's maturity, the more sensitive it is to this risk. Bonds may also be subject to call risk, which is the risk that the issuer will redeem the debt at its option, fully or partially, before the scheduled maturity date. The market value of debt instruments may fluctuate, and proceeds from sales prior to maturity may be more or less than the amount originally invested or the maturity value due to changes in market conditions or changes in the credit quality of the issuer. Bonds are subject to the credit risk of the issuer. This is the risk that the issuer might be unable to make interest and/or principal payments on a timely basis. Bonds are also subject to reinvestment risk, which is the risk that principal and/or interest payments from a given investment may be reinvested at a lower interest rate.

Bonds rated below investment grade may have speculative characteristics and present significant risks beyond those of other securities, including greater credit risk and price volatility in the secondary market. Investors should be careful to consider these risks alongside their individual circumstances, objectives and risk tolerance before investing in high-yield bonds. High yield bonds should comprise only a limited portion of a balanced portfolio.

Asset allocation and diversification do not assure a profit or protect against loss in declining financial markets.

Rebalancing does not protect against a loss in declining financial markets. There may be a potential tax implication with a rebalancing strategy. Investors should consult with their tax advisor before implementing such a strategy.

Growth investing does not guarantee a profit or eliminate risk. The stocks of these companies can have relatively high valuations. Because of these high valuations, an investment in a growth stock can be more risky than an investment in a company with more modest growth expectations.

Value investing does not guarantee a profit or eliminate risk. Not all companies whose stocks are considered to be value stocks are able to turn their business around or successfully employ corrective strategies which would result in stock prices that do not rise as initially expected.

Because of their narrow focus, **sector investments** tend to be more volatile than investments that diversify across many sectors and companies.

REITs investing risks are similar to those associated with direct investments in real estate: property value fluctuations, lack of liquidity, limited diversification and sensitivity to economic factors such as interest rate changes and market recessions.

Alternative investments may be either traditional alternative investment vehicles, such as hedge funds, fund of hedge funds, private equity, private real estate and managed futures or, non-traditional products such as mutual funds and exchange-traded funds that also seek alternative-like exposure but have significant differences from traditional alternative investments. The risks of traditional alternative investments may include: can be highly illiquid, speculative and not appropriate for all investors, loss of all or a substantial portion of the investment due to leveraging, short-selling, or other speculative practices, volatility of returns, restrictions on transferring interests in a fund, potential lack of diversification and resulting higher risk due to concentration of trading authority when a single advisor is utilized, absence of information regarding valuations and pricing, complex tax structures and delays in tax reporting, less regulation and higher fees than open-end mutual funds, and risks associated with the operations, personnel and processes of the manager. Non-traditional alternative strategy products may employ various investment strategies and techniques for both hedging and more speculative purposes such as short-selling, leverage, derivatives and options, which can increase volatility and the risk of investment loss. These investments are subject to the risks normally associated with debt instruments and also carry substantial additional risks. Investors could lose all or a substantial amount of their investment. These investments typically have higher fees or expenses than traditional investments.

Hedge funds may involve a high degree of risk, often engage in leveraging and other speculative investment practices that may increase the risk of investment loss, can be highly illiquid, are not required to provide periodic pricing or valuation information to investors, may involve complex tax structures and delays in distributing important tax information, are not subject to the same regulatory requirements as mutual funds, often charge high fees which may offset any trading profits, and in many cases the underlying investments are not transparent and are known only to the investment manager.

Venture Capital investments involve a high degree of risk and are not appropriate for all investors. Financial and operating risks confronting startups are significant. While targeted returns should reflect the perceived level of risk in any investment situation, such returns are unrealized and based solely on the startup's own estimate of the current value of its fund investments, are not verified or audited by third party valuation, and do not represent actual return of capital or gain, may never be realized and/or may not be adequate to compensate an investor for risks taken. Loss of an investor's entire investment is possible and can easily occur. Moreover, the timing of any return on investment is highly uncertain given the illiquid nature of venture capital investments. The venture capital market is highly competitive and the percentage of companies that survive and prosper is small. Startup investments often experience unexpected problems in the areas of product development, manufacturing, marketing, financing, and general management, among others, which frequently cannot be solved. In addition, startups may require substantial amounts of financing, which may not be available through institutional private placements, the public markets or otherwise.

Environmental, Social and Governance ("ESG") investments in a portfolio may experience performance that is lower or higher than a portfolio not employing such practices. Portfolios with ESG restrictions and strategies as well as ESG investments may not be able to take advantage of the same opportunities or market trends as portfolios where ESG criteria is not applied. There are inconsistent ESG definitions and criteria within the industry, as well as multiple ESG ratings providers that provide ESG ratings of the same subject companies and/or securities that vary among the providers. Certain issuers of investments may have differing and inconsistent views concerning ESG criteria where the ESG claims made in offering documents or other literature may overstate ESG impact. ESG designations are as of the date of this material, and no assurance is provided that the underlying assets have maintained or will maintain and such designation or any stated ESG compliance. As a result, it is difficult to compare ESG investment products or to evaluate an ESG investment product in comparison to one that does not focus

FIDUCIARIES IN FOCUS

on ESG. Investors should also independently consider whether the ESG investment product meets their own ESG objectives or criteria. There is no assurance that an ESG investing strategy or techniques employed will be successful. Past performance is not a guarantee or a dependable measure of future results.

Certain securities referred to in this material may not have been registered under the U.S. Securities Act of 1933, as amended, and, if not, may not be offered or sold absent an exemption therefrom. Recipients are required to comply with any legal or contractual restrictions on their purchase, holding, and sale, exercise of rights or performance of obligations under any securities/instruments transaction.

Disclosures

Morgan Stanley Wealth Management is the trade name of Morgan Stanley Smith Barney LLC, a registered broker-dealer in the United States. This material has been prepared for informational purposes only and is not an offer to buy or sell or a solicitation of any offer to buy or sell any security or other financial instrument or to participate in any trading strategy. Past performance is not necessarily a guide to future performance.

The author(s) (if any authors are noted) principally responsible for the preparation of this material receive compensation based upon various factors, including quality and accuracy of their work, firm revenues (including trading and capital markets revenues), client feedback and competitive factors. Morgan Stanley Wealth Management is involved in many businesses that may relate to companies, securities or instruments mentioned in this material.

This material has been prepared for informational purposes only and is not an offer to buy or sell or a solicitation of any offer to buy or sell any security/instrument, or to participate in any trading strategy. Any such offer would be made only after a prospective investor had completed its own independent investigation of the securities, instruments or transactions, and received all information it required to make its own investment decision, including, where applicable, a review of any offering circular or memorandum describing such security or instrument. That information would contain material information not contained herein and to which prospective participants are referred. This material is based on public information as of the specified date, and may be stale thereafter. We have no obligation to tell you when information herein may change. We make no representation or warranty with respect to the accuracy or completeness of this material. Morgan Stanley Wealth Management has no obligation to provide updated information on the securities/instruments mentioned herein.

The summary at the beginning of the report may have been generated with the assistance of artificial intelligence (AI).

The securities/instruments discussed in this material may not be appropriate for all investors. The appropriateness of a particular investment or strategy will depend on an investor's individual circumstances and objectives. Morgan Stanley Wealth Management recommends that investors independently evaluate specific investments and strategies, and encourages investors to seek the advice of a financial advisor. The value of and income from investments may vary because of changes in interest rates, foreign exchange rates, default rates, prepayment rates, securities/instruments prices, market indexes, operational or financial conditions of companies and other issuers or other factors. Estimates of future performance are based on assumptions that may not be realized. Actual events may differ from those assumed and changes to any assumptions may have a material impact on any projections or estimates. Other events not taken into account may occur and may significantly affect the projections or estimates. Certain assumptions may have been made for modeling purposes only to simplify the presentation and/or calculation of any projections or estimates, and Morgan Stanley Wealth Management does not represent that any such assumptions will reflect actual future events. Accordingly, there can be no assurance that estimated returns or projections will be realized or that actual returns or performance results will not materially differ from those estimated herein.

This material should not be viewed as advice or recommendations with respect to asset allocation or any particular investment. This information is not intended to, and should not, form a primary basis for any investment decisions that you may make. Morgan Stanley Wealth Management is not acting as a fiduciary under either the Employee Retirement Income Security Act of 1974, as amended or under section 4975 of the Internal Revenue Code of 1986 as amended in providing this material except as otherwise provided in writing by Morgan Stanley and/or as described at www.morganstanley.com/disclosures/dol.

Morgan Stanley Smith Barney LLC, its affiliates and Morgan Stanley Financial Advisors do not provide legal or tax advice. Each client should always consult his/her personal tax and/or legal advisor for information concerning his/her individual situation and to learn about any potential tax or other implications that may result from acting on a particular recommendation.

This material is disseminated in Australia to "retail clients" within the meaning of the Australian Corporations Act by Morgan Stanley Wealth Management Australia Pty Ltd (A.B.N. 19 009 145 555, holder of Australian financial services license No. 240813).

Morgan Stanley Wealth Management is not incorporated under the People's Republic of China ("PRC") law and the material in relation to this report is conducted outside the PRC. This report will be distributed only upon request of a specific recipient. This report does not constitute an offer to sell or the solicitation of an offer to buy any securities in the PRC. PRC investors must have the relevant qualifications to invest in such securities and must be responsible for obtaining all relevant approvals, licenses, verifications and or registrations from PRC's relevant governmental authorities.

If your financial adviser is based in Australia, Switzerland or the United Kingdom, then please be aware that this report is being distributed by the Morgan Stanley entity where your financial adviser is located, as follows: Australia: Morgan Stanley Wealth Management Australia Pty Ltd (ABN 19 009 145 555, AFSL No. 240813); Switzerland: Morgan Stanley (Switzerland) AG regulated by the Swiss Financial Market Supervisory Authority; or United Kingdom: Morgan Stanley Private Wealth Management Ltd, authorized and regulated by the Financial Conduct Authority, approves for the purposes of section 21 of the Financial Services and Markets Act 2000 this material for distribution in the United Kingdom.

Morgan Stanley Wealth Management is not acting as a municipal advisor to any municipal entity or obligated person within the meaning of Section 15B of the Securities Exchange Act (the "Municipal Advisor Rule") and the opinions or views contained herein are not intended to be, and do not constitute, advice within the meaning of the Municipal Advisor Rule.

This material is disseminated in the United States of America by Morgan Stanley Smith Barney LLC.

FIDUCIARIES IN FOCUS

Third-party data providers make no warranties or representations of any kind relating to the accuracy, completeness, or timeliness of the data they provide and shall not have liability for any damages of any kind relating to such data.

This material, or any portion thereof, may not be reprinted, sold or redistributed without the written consent of Morgan Stanley Smith Barney LLC.

© 2025 Morgan Stanley Smith Barney LLC. Member SIPC.

RSI1753372565869 07/2025