

VIRGINIA STATE UNIVERSITY

Section:	Board of Visitors
Policy Number:	104
Policy Name:	Endowment Investment and Spending Policy
Applicability:	All University Employees
Effective Date:	May 1, 1998
Revision Date:	April 22, 1998- Supersedes all prior University policies on the investment and spending of endowment funds.
Review Date:	September 1, 2000

I. Purpose

The purpose of this policy is to define the University's spending rule, investment objectives, guidelines, and performance standards for endowment funds.

Successful fundraising efforts have provided the University with endowment assets that are critical to the welfare of the University. These critical funds directly influence the quality of the educational environment available to students, faculty and the community. The endowment portfolio provides a significant annual contribution to current operations, such as funding to cover Scholarships, Faculty Merit Awards, the Eminent Scholars Program, etc.

II. Definitions

A. Endowments

The following is the definition of endowments as established by the American Institute of Certified Public Accountants in the Industry Audit Guide for Audits of Colleges and Universities (1993, p. 25).:

Endowment funds are funds with respect to which donors or other outside agencies have stipulated, as a condition of the gift instrument, that the principal is to be maintained inviolate and in perpetuity and invested for the purpose of producing present and future income which may either be expended or added to principal.

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Term endowment funds are similar to endowment funds except that upon the passage of a stated period of time or the happening of a particular event, all or a part of the principal may be expended.

Quasi-endowment funds (funds functioning as endowment) are funds which the governing board of an institution, rather than a donor or other outside agency, has determined are to be retained and invested. Since these funds are internally designated rather than externally restricted, the governing board has the right to decide at any time to expend the principal.

B. Asset Allocation Ranges

Asset allocation ranges are the minimum and maximum levels of investment per asset class per portfolio.

III. Investment Philosophy

The Board of Visitors requires the achievement of optimum long-term total returns within prudent levels of risk. Returns are expected to preserve or enhance the real value of the endowment after funds are released for use. Risk can be reduced with a broadly diversified portfolio of asset classes.

IV. Policy Objectives

The Board of Visitors delegates general authority to the President to achieve the following:

1. To invest and safeguard the corpus of each permanent endowment in order to maintain these funds into perpetuity so they will continuously generate future income.
2. To invest quasi-endowment funds to generate income until the Board authorizes the expenditure of the principal.
3. To optimize returns within prudent levels of risk in order to maximize funds available for the purposes for which each endowment is established.
4. To achieve the desired spending policy for the Eminent Scholars Program, Faculty

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5. To reach the desired spending level, earned income (net of management fees) and realized and unrealized gains (net of realized and unrealized losses) will be included in expendable funds.

V. Investment Policy

1. Minimum Earnings Rate

The Board of Visitors requires that the endowment funds be invested to earn at least 5.5% above the rate of the Higher Education Price Index, which measures university inflation.

2. Asset Allocation

The Board of Visitors authorizes the following asset allocation ranges for investment of the University's endowment funds:

US Large Cap Stocks	45-55%
US Small Cap Stocks	0-15%
International Stocks	0-15%
Fixed Income	20-40%
Cash and Short-term Securities	0-30%

The Board of Visitors delegates to the President the responsibility for monitoring account performance reports to ensure allocations are within the above ranges and ensuring quarterly allocation percentages are reported at Board of Visitors meetings.

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3. Investment Classes and Ratings

The Board of Visitors establishes the following requirements of the investment classes utilized:

- a. Equities Types of Securities Common and preferred stocks, and issues convertible into common stocks, of both domestic and international corporations and American Depository Receipts (ADRs).

Diversification The securities of any one insurer are limited to 5% at market of each portfolio. Broad industry diversification is desirable. For international equities, both industry and country diversification are desirable.

Quality Only equity securities which are broadly classified as institutional quality issues are eligible for inclusion in the portfolio. All securities held in the portfolio should be publicly traded and have sufficient marketability to permit prompt, orderly liquidation under normal circumstances. Stock selection should emphasize quality with due regard to risk.

Exclusions Without prior approval of the Board of Visitors and the express written consent of the President, or his designee, the following investments are prohibited:

- C Short naked call options;
- C Short put options;
- C Commodities including all futures contracts;
- C Swaps; and
- C Other derivatives.

When written consent is given for investment in any of these categories, the University will require the investment manager to adhere to specific safeguards.

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b. Fixed Income

Types of Securities Debt securities of any US entity denominated in US dollars, and not otherwise prohibited, US dollar denominated sovereign and supranational bonds (Yankee bonds), and Collateralized Mortgage Obligations (CMOs) except as prohibited.

Diversification The securities of any one issuer, with the exception of the US Government and its agencies, are limited to 5% at market of each fixed income portfolio.

Quality The average credit quality of the portfolio must be at least A or BBB (investment grade). If any security has a split rating, the lower of the two ratings shall be considered for the purposes of meeting minimum quality standards.

Maturity No one security shall mature longer than 15 years. It is expected that the average duration of the fixed income portfolio will not exceed 7 years. All issues should be readily marketable.

Exclusions Without prior approval of the Board of Visitors and the express written consent of the President, or his designee, the following investments are prohibited:

- C Privately placed debt;
- C Margin buying, short selling;
- C Commodities, options, swap contracts; and
- C Other derivatives.

When written consent is given for any investment in any of these categories, the University will require the investment manager to adhere to specific safeguards.

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c. Cash and Short-term Securities

Types Cash, money markets, and debt securities of any US entity not otherwise prohibited, with a maximum average maturity of one year.

Diversification	<u>Security</u>	<u>Maximum</u>
	Certificates of Deposit (CDS)	10%
	Commercial Paper	35%
	Corporate Bonds	35%
	Single Issuer for Commercial Paper and Corporate Bonds	5%
	US Treasury and Federal Agency Obligations	5%

Quality	<u>Security</u>	<u>Minimum Rating</u>
	Asset Backeds	A
	CDS	A
	Commercial Paper	A1/P1
	Corporate Bonds	AA

Exclusions

Without prior approval of the Board of Visitors and the express written consent of the President, or his designee, the following investments are prohibited:

- Ⓒ Floating rate notes with maturities under two years that have any embedded leverage or option ability (e.g.; caps, floors, multiple reset features, etc.);
- Ⓒ Floating rate notes with maturities over two years;
- Ⓒ Structured notes, including Collateralized Mortgage Obligations (CMOs);
- Ⓒ Swaps; and
- Ⓒ Other derivatives.

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When written consent is given for investment in any of these categories, the University will require the investment manager to adhere to specific safeguards.

d. Real Property

Occasionally, the University accepts gifts of real property. Usually, the University sells all or a portion of the property. There are costs, such as surveys, attorney's fees, etc. associated with these sales. While some of the costs are known at the time of the sale, some are not known. The known costs are paid from the proceeds of the sale.

In order to avoid the use of unrestricted funds to pay for unknown costs, the President shall cause a set aside of 5% of the proceeds of any sale for one year. These reserve funds will be used to pay any unmet expenses of the sale. At the end of the year, the remaining reserve funds will be used as specified by the donor, unless it is known that there are still outstanding expenses. In that case, the remaining money will be transferred after the expenses are met.

4. Investment Pools

Pooled fund investments may be made only with the approval of the Board of Visitors. Investing through a pooled fund vehicle (i.e. the Commonfund and the Local Government Investment Pool) means that the investments will be governed by the fund's own set of guidelines and restrictions. While the intent is to invest in funds which meet these guidelines, there may be instances in which the pooled fund's guidelines differ. In such cases, the pooled fund guidelines and restrictions will supersede those outlined above. Before a pooled fund can be used, the investment manager will provide the University with a prospectus of the fund and will identify, in writing, any guidelines and restrictions that differ from those outlined above. To the extent that pooled funds are implemented, the fees imposed should be at no higher cost than incurred if the securities were separately managed.

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5. Disposal of Securities Received by Gift or Bequest

All securities received by gift or bequest will normally be sold as promptly as possible unless prohibited by the terms of the gift or bequest. The decision to hold securities will be made only after consultation with the investment manager(s).

6. State Match

The Board of Visitors encourages the University's administration to negotiate endowment agreements that include a paragraph stating that, with the expressed intention of the donor, the endowment may qualify for matching funds from the federal or state government. Such governmental support may include the Commonwealth of Virginia Graduate and Undergraduate Assistance Program, the US Department of Education, or Title III Endowment Challenge Grant Program.

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VI. Spending Policy

The Development Committee will review the spending rates at least once every two years. Modifications to the spending policy must be approved by the Board of Visitors.

1. Endowment

The Board of Visitors requires each fiscal year that the spending rate be no more than 5.5% of the averaged market value for the previous three calendar years as measured at December 31st of each year. For the first or second year of a new endowment, the spending rate will be no more than 4.5% of current market value until three calendar years of data are collected.

In keeping with the total return concept, only income in excess of true endowment corpus, in the form of dividends, net realized gains, and capital appreciation can be expended. Quasi-endowment corpus can be utilized after approval by the Board of Visitors. Term endowment corpus can be utilized after the term has expired or a particular event has occurred per the agreement with the approval of the Board of Visitors.

2. Eminent Scholars and Other State Matching Programs

The Board of Visitors requires that earnings generated by endowments restricted by donors for eminent scholars must be used to support named faculty professorships. The Commonwealth of Virginia's programs will match the portion of income earned on the historical principal that is subsequently budgeted for expenditure.

The Board of Visitors requires that each fiscal year the spending rate be no more than 7.5% of the average market value for the previous three calendar years as measured at December 31st of each year. For the first or second year, the spending rate will be no more than 6.5% of current market value until three calendar years of data are collected.

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VII. Investment Managers

The Board of Visitors delegates authority to the President to direct the proposal and selection process, in accordance with State procurement guidelines, and to select the investment management firm(s) that will be awarded the responsibility of investing and managing the University's endowment funds. The final selection must be reported to the Board of Visitors at a regular meeting.

VIII. Performance Standards

In order to measure and evaluate the investment performance of the investment manager(s), the Board of Visitors establishes the following benchmarks by which the investment manager(s) will be evaluated:

Equity Funds: S&P 500 Index and Russell 1000

Bond Funds: Lehman Brothers Intermediate Treasury Bond Index

Total Funds: 50% S&P 500 & 40% Lehman Brothers Intermediate Government Bond Index & 10% Treasury Bills

Cash and Short Term Investments: 90-Day Treasury Bill Index

Other statistics may be utilized for additional comparative purposes.

IX. Reporting

The quarterly analysis reports will be provided to the Development Committee of the Board of Visitors. The investment manager(s) will meet with the Development Committee on an annual basis.

X. Responsibilities of the Development Committee

The Development Committee is responsible for the stewardship role of managing the

University's endowment funds. This responsibility includes monitoring investment performance; establishing and periodically reviewing the investment policies; and upon thorough evaluation, recommending to the Board of Visitors amendments to this policy.

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XI. Standards of Conduct

The Uniform Management of Institutional Funds Act, passed by the Virginia Legislature in 1973, provides for standards of conduct in Section 55-268.6 of The Code of Virginia (1950 as amended), the spirit of which the Board of Visitors hereby endorses:

In the administration of the powers to appropriate appreciation, to make and retain investments, and to delegate investment management of institutional funds, members of a governing board shall exercise ordinary business care and prudence under the facts and circumstances prevailing at the time of the action or decision, and in so doing they shall consider long- and short-term needs of the institution, in carrying out its educational, religious, charitable, or other eleemosynary purposes, its present and anticipated financial requirements, expected total return on its investments, price level trends, and general economic conditions. (1973, c. 167)

Employees of the University or others engaged by the University in any business or advisory capacity are expected to uphold these same high standards of responsible and ethical behavior.

XII. Revisions and Exceptions

This policy can be modified as necessary by the Board of Visitors upon recommendations by the Development Committee and/or the President. It should be formally reviewed by the Development Committee once every two years. Requests for exceptions to this policy must be submitted in writing to the Chair of the Development Committee and approved by the Board of Visitors.

XIII. Custody

All securities will remain in the custody of the University or the investment manager trustee(s).

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IX. Procedures

The Board of Visitors delegates to the President the responsibility to develop procedures to implement this policy.

APPROVED BY: _____
Glen N. Jones, Rector

DATE: _____