Kentucky State University
Policies and Procedures

POLICY TITLE:
Endowment Investment & Spending Policy

VOLUME, SECTION & NUMBER:
4.1.16

ENTITIES AFFECTED:
All Departments and Divisions

ADMINISTRATIVE AUTHORITY:
Institutional Advancement & External Relations

Finance & Administration

APPROVED BY:
The Kentucky State University Board of Regents

EFFECTIVE DATE:
June 24, 2024

REVISED FROM:
December 18, 2023, Version of Policy

POLICY STATEMENT:

This policy aims to outline a philosophy that will guide the management of investment assets toward the desired results. It is intended to be sufficiently specific as to be meaningful, yet flexible enough to be practical.

This Endowment Investment & Spending Policy is set forth in order to:

- Define and assign responsibilities;
- Establish a clear understanding of the investment goals and objectives of the Endowment assets;
- Offer guidance and limitations regarding the investment and spending of Endowment assets;
- Establish a basis of evaluating investment results; and
- Manage the Endowment's assets according to industry best practices and applicable laws.

This Endowment Investment & Spending Policy shall be formally reviewed annually and at such other times as desired by the Board of Regents, or the Board's designated Committee, and the University's administration. Any modifications to the policy shall be approved by the Board of Regents. This Endowment Investment & Spending Policy shall supersede all existing Kentucky State University Endowment Investment Policies and Endowment Spending Policies.

GENERAL INFORMATION:

The Kentucky State University Endowment (Endowment) is an aggregation of funds comprised of gifts from donors and grants from the Commonwealth of Kentucky, with the requirement that they be invested in perpetuity to generate a reliable and steadily growing revenue stream to support the mission of Kentucky State University (KSU) both now and in the future. The revenue stream, or annual spending distributions, supports scholarships, chairs, professorships, and departments, as defined by the executed Endowment agreements. The Endowment is expected to provide fiscal stability because the principal is invested for long-term growth, and spending distributions are generated annually.

KSU has a fiduciary responsibility to prudently manage and preserve the long-term purchasing power of the Endowment, as well as the individual endowment funds, in order to evenly support present and future beneficiaries. This fiduciary responsibility constitutes both a legal and moral obligation to donors and the Commonwealth of Kentucky, who intend that their gifts and grants provide support for KSU into perpetuity.

The Endowment is considered open and can welcome additional funds from current or future donors with the expectation that they be invested on a long-term basis.

DELEGATION OF AUTHORITY:

The Board of Regents delegates to the administration the following investment-related activities.

Hiring and Monitoring of the Investment Manager
In collaboration with the President, the administration will—in accordance with appropriate regulations and guidelines—appoint, monitor, and evaluate the external investment manager or management firm for the investment asset allocation and strategies approved by the Board of Regents or its designated Committee. The administration will provide updates to the Board or its designated Committee on the ongoing monitoring and evaluation of the firm at each meeting and at other times as requested by the Board or its designated Committee. The administration may implement temporary investments as needed due to the firm's investment strategy, portfolio structure changes, and/or domestic/global conditions.

Management of Endowment Assets
The investment manager will exercise discretion over the securities or assets within the specified investment guidelines. Investment managers will follow the approved asset allocation guidelines within this policy.

FINANCIAL AND INVESTMENT OBJECTIVES:

The following financial and investment objectives have been established for the KSU Endowment:

- To preserve the long-term purchasing power of the Endowment assets and the related annual spending distributions over time to evenly allocate support between current and future beneficiaries (intergenerational equity).

- To earn an average annual total return, after expenses, of at least 7.5% per year over full economic market cycles.

Kentucky Uniform Prudent Management of Institutional Funds Act (KRS 273.600 to 273.645)

Endowment assets will be managed by the Board of Regents or its designated Committee in accordance with the provisions of the Kentucky Uniform Prudent Management of Institutional Funds Act (KRS 273.600 to 273.645).

Annual Spending Distribution Policy

A spending distribution policy has been established that is based on a rolling average of market values in order to reduce adverse budgetary impact due to market volatility of the endowment assets. The annual spending distribution will be calculated by a smoothing formula based on a rolling three-year average of the quarterly market values. Ending market values for the last 12 quarters are averaged, and the result is then multiplied by the 4% spending distribution rate (1% per quarter) to determine the total amount to be distributed from the prior December 31st value. This amount is then allocated to participating funds based on their pro-rata share of the total investment pool.

Note: the calculated annual spending distribution rate must fall between 3.5% and 5% of the current market value of the Endowment. Should the rolling three-year average be outside the range, it will be raised to the equivalent of 3.5% or lowered to the equivalent of 5%. The Board of Regents reserves the right to freeze, lower, or increase the annual spending distribution in an extraordinary financial situation.

Management Fee

Eligible Endowment funds will be assessed an annual management fee of no more than 1.00% (100 basis points) of the current market value to support administrative costs by the institution. Inclusive of all services, at no time shall more than 50% of the annual management fee go towards the investment manager or investment services.

Underwater Endowment Funds

The target annual spending distribution rate and management fee represent maximum amounts that can be withdrawn annually from individual Endowment funds. The administration, at their discretion, may reduce or suspend withdrawals from individual endowment funds that are underwater. The administration will define underwater endowment funds annually, and will advise the investment manager of the implementation or removal of reduced or suspended withdrawals from individual Endowment funds.

Spending distributions and management fee withdrawals will be suspended on all Endowment funds underwater by more than 20%. Endowment funds that are underwater more than 10% will undergo a formal review by the Office of the Controller and appropriate staff members to determine the appropriate level of spending distributions in accordance with the following factors set forth in the Kentucky Uniform Prudent Management of Institutional Funds Act:

- The duration and preservation of the Endowment fund;
- The purposes of the Institution and the Endowment fund;
- General economic conditions;
- The possible effect of inflation or deflation;
- The expected total return from income and the appreciation of investments;
- Other resources of the institution; and

- The investment policy of the Institution

New Endowment Funds
Spending distributions on new Endowment funds will be delayed for at least one year in order to build a reserve for future spending distributions. The administration may modify this requirement depending on partial year returns.

INVESTMENT POLICIES:

Diversification
Disciplined management of the asset allocation is necessary and desirable. Diversification of investments among assets that are not similarly affected by economic, political, or social developments is highly desirable. The general policy shall be to diversify investments so as to provide a balance that will enhance total return, while avoiding undue risk concentrations in any single asset or investment category.

Asset Allocation
To ensure broad diversification, the asset allocation will be set with the following target percentages and within the following ranges:

ASSET CATEGORY	TARGET	RANGE
DOMESTIC LARGE CAP. EQUITY	50%	40 – 58%
DOMESTIC MID/SMALL CAP. EQUITY	20%	15 – 25%
INTERNATIONAL EQUITY*	0%	0 – 5%
FIXED INCOME	28%	23 – 37%
REAL ASSETS	0%	0 – 5%
CASH	2%	0 – 2%

Domestic Large Capitalization Equity – The allocation will be represented **only** by investments in a large capitalization index fund such as the Vanguard S&P 500 Index Fund Admiral Shares. All investments in this asset category must be held in passively-managed index funds with low expense ratios (0.05% or less).

Domestic Mid & Small Capitalization Equity – The allocation of Mid-Cap and Small-Cap stocks will consist **only** of appropriate index funds from the two groups. Target investments in this asset category include the Vanguard Mid-Cap Index Fund – Admiral Shares (expense ratio of 0.05%) and/or the Fidelity Mid-Cap Index Fund or the Russell 2500 Index Fund and/or iShares Small Cap 600 Index. All investments in this asset category must be held in passively-managed index funds with low expense ratios (below 0.10%). Mid-cap stocks fall between small-cap and large-cap stocks in terms of market capitalization. These companies are generally more established than small cap companies, but may not have the same level of recognition as large-caps. Small-cap stocks refer to publicly-traded companies with relatively small market capitalizations.

International Equity – The allocation may consist of International Equity endowments from time to time. This asset category represents global companies outside of the domestic large, mid- and small-capitalization equity allocation asset categories. International indexed funds are preferred.

*Any international index fund with fees no greater than 25 basis point may be accepted unless otherwise approved annually by the Board of Regents.

Fixed Income – The allocation will consist exclusively of US Treasury and Agency Bonds and bills, including US Treasury Inflation Protected Securities (TIPS) (when their returns are attractive, relative to other US Treasury securities.) The primary role of this US Government-issued fixed income portfolio is to provide a partial hedge in the event of an economic contraction, deflation, and/or a severe flight to safety/quality. It is expected that this portion of the portfolio would serve as one of the primary sources of spending during such periods, when the prices of other assets in the portfolio may decline. These bonds should be held in a 10-year laddered structure of individual bonds to assure that there will be a regular and predictable source of cash to meet unexpected needs. This asset class should **not** include any bond ETFs or bond mutual funds, because of the lack of control over when bond purchases and sales are made within the fund and when cash comes available to the fund holder.

Real Assets – Strategic Real Estate Assets located near the current and projected campuses. No other real estate investments will be permitted (without explicit case-by-case approval by the Board) due to volatility, default, and liquidity risk.

Cash – The cash allocation will be used to provide liquidity for spending distributions and management fees. The cash allocation should never exceed 2.0%, and should be held in a flexible interest-bearing account such as a Money Market Fund.

Monitoring and Reporting

The investment manager will have full discretion to make all investment decisions for the assets placed under its management within the bounds of the above-stated Investment Policy, including the asset allocations and restrictions approved by Kentucky State University. Institutional pooled funds, such as mutual funds and exchange traded funds, and alternative investment managers will be governed by their prospectus and offering memorandums.

Specific responsibilities of the investment manager(s) include the following:

- Discretionary investment management, including decisions to buy, sell, or hold individual securities in line with the investment guidelines enumerated above.
- Reporting, on a timely basis, quarterly investment performance results, including standard measures of risk and volatility, such as beta, Jensen’s alpha, and the Sharpe ratio, for 1, 3 and 5 year periods, in addition to specific portfolio attributes as requested by Kentucky State University;
- Communicating any expected major changes in the economic outlook, the specific investment strategy (within the bounds of the guidelines enumerated above, or any other factors that affect implementation of investment process, or the investment objective progress of the fund’s investment management;
- Informing Kentucky State University regarding any qualitative change to the investment management organization. Examples include changes in portfolio management personnel, ownership structure, investment philosophy, etc.;
- Voting proxies on behalf of the fund in line with the investment philosophy, management of the portfolio;

and instructions of Kentucky State University – votes should be shared with KSU's administration; and
- The investment manager must operate without any conflicts of interest.

Rebalancing

Rebalancing is a term that describes the periodic movement of funds from one asset class or category to another for the purpose of realigning the assets with the asset allocation target. A rebalancing strategy is an important element of asset allocation policy. Systematic rebalancing will ensure that the portfolio's risk profile remains consistent with this Endowment Investment & Spending Policy. However, excessively tight ranges and frequent rebalancing can lead to unnecessary transaction costs.

The rebalancing policy is governed by allocation ranges rather than time periods. The ranges, specified in the table above, are a function of the volatility and liquidity of each asset class and the proportion of the total fund allocated to the asset category. While the allocation to all asset categories remains within these limits, staff will first use cash flows, as available, to prudently manage allocations relative to the target. When an asset category violates the lower or upper limits, public market funds will be actively rebalanced back within the target range.

When any one of the public market asset categories hits a trigger point, the entire fund may be rebalanced back within the target range. When rebalancing among the investment categories, qualitative considerations (e.g., transaction costs, liquidity needs, investment time horizons, etc.) should be considered in determining the potential timing and extent of rebalancing.

The Investment Management Firm is responsible for developing and implementing a rebalancing plan that is appropriate for existing market conditions, with a primary objective of minimizing transaction costs and portfolio disruptions. In the event an allocation trigger point is not reached, the investment managers, after consultation with KSU's investment officer (staff), may make minor changes among asset categories and within individual asset categories, as needed, to more effectively implement the program and to maintain proper exposure to the approved asset allocation and asset category portfolio structures. Staff will report the results of all rebalancing activity to the Board or its designated Committee at the regular meetings.

Liquidity

The Endowment is intended to provide a reliable and steadily growing revenue stream to support the mission of KSU into perpetuity. As a result, the Endowment has a long-term orientation. In addition, the withdrawal rate from an Endowment fund is well defined, predictable, and of modest size relative to the total assets. The administration is responsible for managing the liquidity of the portfolio to fund spending distributions and capital calls, while maintaining the appropriate market exposure.

Certain appropriate investment options, particularly in alternative asset classes, involve fund structures with liquidity constraints that align with less liquid portfolio holdings. The tradeoff between return opportunities and liquidity will be considered throughout the portfolio construction process.
Sufficient liquidity shall be maintained to fulfill the spending distributions and operating objectives of the Pool. Portfolio liquidity will be monitored using a three-tier system:

Liquid: available within 90 days

Semi-liquid: available in 90 days or more, but less than 2 years

Illiquid: available only in 2 years or more

Classification of Asset	**Guideline**
Liquid	no less than 35%
Combined:	Semi-liquid & Illiquid - no more than 65%
Illiquid	no more than 40%

New commitments will be made to illiquid/private capital investments with the intent to keep current market value of liquid holdings above 35% of the total fund. Illiquid percentages will be calculated based on current market value. The administration, assisted by the Investment Management Firm, will complete annual forecasting and make appropriate commitments to reach and maintain the approved policy allocation and liquidity while ensuring diversification across vintage year, strategy, geography, etc.

It is recognized that significant changes in investment market values could cause the portfolio to be positioned outside of these guidelines. If this occurs, staff will communicate this to the Board or its designated Committee and develop a plan to reposition the portfolio consistent with these guidelines over a reasonable time frame.

Proxy Voting

The Board delegates full authority for proxy voting to the administration for the securities under their discretionary authority and requires the investment managers to vote all proxies in the best interest of the Endowment with input from the administration. In addition, when requested, the administration will report to the Board regarding their proxy-voting policies and activities behalf of the Endowment.

Transaction Costs

The Board requires the Investment Management Firm, in their capacity as fiduciaries, to manage the transactions costs they incur on the Endowment's behalf in the best interests of KSU. When requested, the firm will report to the Board or its designated Committee regarding the transaction costs incurred and the brokers used on the Endowment's behalf.

PERFORMANCE EVALUATION:

Endowment performance will be monitored and reviewed over short and long-term time periods, with an emphasis on longer-term periods in order to include full market cycles and reflect the Endowment's long-term investment strategy. Performance will be evaluated at two levels: total Endowment and asset class. The levels will include a market index and peer group measurement review. Performance will be reviewed on a gross and net return basis and will include risk metrics and risk-adjusted returns.

Performance Benchmarks

The total Endowment performance will be measured against the following:

- The primary performance objective of achieving a long-term total return, net of fees and expenses, of at least 7.5%. It is expected that portfolio performance will vary significantly from this benchmark over shorter periods. Therefore, performance compared to this benchmark will be evaluated only over longer periods such as five to ten years.

- From time to time the performance of the KSU's Endowment should be compared to a peer group of similar institutions.

- The Policy Benchmark will be rebalanced to target weightings on December 31st of each calendar year.

ENDOWMENT EXPENDITURES:

Endowed accounts after they have matured for one fiscal year, will be eligible for disbursement to fund expenditures in accordance with their signed agreement or internal agreement (agreement) for applicable accounts. If an account is underwater as defined herein, then the account will be ineligible for expenditure. The annual spending shall be determined by the December 31st value each year with the smoothing formula based on a rolling 12 quarter average of their market values. Accounts, depending on their type (Scholarship, Professorship/Chair or Departmental) shall be governed by the policy herein and the procedures below:

Scholarship

The campus Scholarship Director or designated employee (Director) shall oversee the selection process for the awarding of endowed scholarships. The Director will annually post the scholarships for student applications following the restrictions of the scholarships in the agreement and applications will be reviewed by a committee formed and chaired by the director. The scholarship committee shall consist of no less than three members and no more than nine members. At no time, shall one singular employee make the decision of who is awarded a scholarship nor shall the funder or family of the scholarship hold a majority vote of the committee.

The scholarship will be awarded in the academic year and may be renewable per the agreement. If a student is no longer eligible, the application will automatically be reviewed by the Scholarship Committee. By definition, a student must be an enrolled student of Kentucky State University and must have a balance to receive funding from an endowed scholarship. The application of payment for endowed scholarships shall be made prior to institutional aid and following external sources including federal and state aid. Endowed scholarship funds are not able to produce a refund unless otherwise directed by the donor agreement.

Professorship / Chair

Upon written recommendation by the Provost to the President, Faculty members will be designated annually, up to three total years, to serve in an endowed professor or chair position. Designation as an endowed professor or chair shall not affect the tenure status of any employee and faculty members may reapply for the position following the initial appointment. Should an employee separate from the institution for any reason, the endowed professor or chair will be deemed vacant and the Provost shall recommend to the President the replacement for the vacant position.

Prior to the initial recommendation by the Provost, the Provost may appoint a selection committee to review any application for the annual professor or chair positions ensuring all Human Resources Policies and Procedures are followed. Should a selection committee be formed, the committee's charge, membership and application process will be shared with all faculty. The selection committee shall follow any written instructions of the Provost, which shall include any instructions from the donor or internal agreement, and may include but are not limited to:

- a review of the current curriculum vita
- solicited letters from stakeholders and extramural reviewers (if any)
- a statement by the professor of no more than five pages that:
    - explains how the goals of the professorship will be met during the first year, and subsequent two years;
    - describes how resources that support the endowment (e.g., funds, space, equipment) will be used during the first year period to meet the criteria of the endowed position, and subsequent two years;

- proposes plans for the stewardship of the endowment in conjunction with the Office of Institutional Advancement and External Relations; and
- addresses any other relevant issues that should be considered during the review process.

The designated endowed professor or chair will annually report the activity of the position to the Provost by May 15th. Following the third year, the employee must reapply for the position if they have served continuously. Preference may be given to faculty with the rank of professor, associate professor, assistant professor, etc.

Annually, the President or their designee will share with the Board of Regents the recipients of the endowed professor or chair positions. The endowed funds shall be treated as a funding source and do not necessarily equate to an increase in salary nor benefits of a professor unless otherwise noted in the donor or internal agreement. The endowed position may include funding for enhanced development, graduate assistants or program support. The endowed position does not alter an appointment from 9 months to 12 months unless otherwise directed by the appointment letter that shall not exceed one academic year but may be renewed for up to two additional years.

Departmental

Endowed departmental funds shall be expended in accordance with KSU's finance and administration policies, which aims to ensure the sustainable and strategic use of financial resources to enhance departmental functions and support academic excellence. Annual spending will be based on the above spending formula. The funds shall be allocated towards priorities such as scholarships, research grants, faculty development, acquisition of cutting-edge equipment or software, and enhancement of academic programs. Annually, the department overseeing the fund shall submit a spending plan to the budget office prior to July 1st of the same year.

All expenditures will be reviewed and approved by the appropriate departments following all KSU policies and procedures and donor restrictions. Expenditures should match the mission and strategic goals of the institution and the department thereby fostering an environment of innovation, academic integrity, and student success.

RELATED POLICIES AND DOCUMENTS:

Gift Acceptance and Donor Recognition Policy

STATUTORY AND REGULATORY REFERENCES:

KRS 164A.550 to 164A.630

KRS 273.600 to 273.645