UNIVERSITY OF LOUISVILLE

Vice President for Finance
Policy/Procedure

Subject: Management of Endowment and Similar Funds	Author: Joe Gahlinger
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A. Background:

Because of cutbacks in state support for higher education and the likelihood of continuing constraints on new appropriations, the University must use all of its financial resources effectively. The use of endowment funds, gift funds, and similar funds must be used to meet the University's objectives consistent with donor designations. In the future, these funds will play a larger part in the overall budget strategy of a college or school and cannot be viewed as unallocated reserve funds. They must be carefully budgeted and wisely used to carry out the University's mission of instruction, research, and service.

The following policy guidelines are intended to ensure the effective management of endowment and similar funds and will enable accurate reporting to donors on how the funds are expended.

B. Definitions:

For purposes of this policy the following definitions will apply:

1. Endowment funds are gift funds that are unrestricted or have been designated to specific programs by individual donors under the terms of a legal gift agreement. The principal of an endowment fund, or the face amount of the bequest, can not be expended. Instead, it is invested for the purpose of generating annual income which is budgeted each year for use by the programs specified in the endowment instrument. The principal of one endowment fund is also referred to as the "corpus" of the fund.
2. Quasi-endowment funds are funds that function as endowments except that the principal of the fund can be expended under certain limited conditions. Quasi-endowment funds may be established by action of the University's Board of Trustees, the Board of Directors of the University of Louisville Foundation, Inc., or by executive management. The principal is invested and the annual earnings produced by the fund are spent like endowment proceeds.
3. The term "similar funds", for purposes of this policy, will refer to either quasi-endowments or term endowments.
4. "Program budgeted," for purposes of this policy, is a term applied to the financial planning process in which program objectives are established, revenues are projected, and proposed expenditures are reviewed and analyzed to produce an annual operating budget for a specific activity.

C. Policy:

1. Vice presidents and deans will ensure that endowment and similar funds are used for the purposes intended by the donors. In cases where the fund is unrestricted as to use and purpose, funds will be expended as approved through the program budgeting process.
2. Vice presidents and deans will prepare annual reports on major endowment funds, briefly explaining how the funds were used by their college or school to meet program objectives and donor designations. Deans will submit their reports to the University Provost for central coordination and review. These will be forwarded to the President, who will inform the donors as appropriate. Vice presidents will submit their reports directly to the President.
3. Endowments and similar funds will be "program budgeted" each year for revenue and expenditures. The Office of the VP for Finance will coordinate the budgeting process and will ensure that the budgets are realistic and on a firm financial footing each fiscal year. Units will actively participate in this process with the Office of the VP for Finance.
4. Once approved in the budget process, planned expenditures from endowment earnings will be budgeted in the units' annual operating budget. These funds must be used to meet specific program objectives consistent with donor designations. Furthermore, all budgets developed for these funds will be included in the University's overall budget, submitted to the Board of Trustees. The Controller's Office will ensure that expenditure budgets are not overexpended and that expenditures conform to the annual operating budget.
5. The annual spending rate for endowment and similar funds is established by the Board of Directors of the University of Louisville Foundation, Inc. Currently this rate is 5.5% of the three-year moving average of the market value of the endowment's investment portfolio as of the three previous calendar year-ends (December 31). This rate will also be used as the basis for establishing the continuing (CAR) budget with the remaining funds used for one time, nonrecurring expenditures. (See section 7.)
6. The principal of an endowment fund will not be expended for any reason. In certain rare circumstances, the principal of a quasi-endowment fund may be used, however, the unit requesting this must obtain the written approval of the President or his designee.
7. Continuing obligations (C.A.R.'s) including salaries, wages, and fringe benefits may not be budgeted for more than eighty percent (80%) of the annual spending rate of the fund, unless the President or his designee has specifically authorized an exception. The remaining twenty percent (20%) may be used for one-time, nonrecurring expenditures that are programmatically justified. The eighty percent (80%) cap on C.A.R. expenditures is intended to protect future budgets from fluctuations in interest rates and unplanned growth of the C.A.R. budget.
8. The following guidelines specifically refer to the establishment of positions funded from endowments and similar funds:
   a. If funds are earmarked for the establishment of a faculty position, i.e., an endowed chair, units may not use the funds for other purposes without permission from the President or his designee.
   b. A faculty position funded from an endowment or similar fund will not be established until there are sufficient annual earnings to provide the annualized salary amount for the position plus an appropriate allowance for fringe benefits. Where special

circumstances warrant, the President or his designee may make exceptions to this on a case by case basis.

c. University units should plan for future cost increases when budgeting endowment and similar funds. Annual salary adjustments, increases in the cost of fringe benefits, and other nonsalary cost increases normally will be absorbed by the respective fund. When developing budgets, units will ensure that routine cost increases can be accommodated in future years within the projected available earnings of the fund. If this is not possible, units must request a budget supplement to support these cost increases.

d. If the annual earnings of an endowment are not sufficient to provide for the full funding of a faculty position (i.e., an endowed chair), they may be reinvested. Deans wishing to do this must specify the amount to be reinvested on the Endowment Program Budget Worksheet submitted to the Office of the VP for Finance.